INTERNAL BRIEF FOR UNDP SENIOR MANAGERS
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A Contribution from UNDP to the 3rd Financing for Development Conference Addis Ababa, July 2015

I. Abstract

The world is now characterized by a more nuanced and complex range of development situations. The international community is on the verge of agreeing on an ambitious and far-reaching post-2015 development agenda. These realities require us to think anew about how we approach the challenge of financing development.

UNDP recognizes the continued importance – and value – of development aid. The Addis Ababa conference represents an opportunity for donor countries to reaffirm their longstanding commitment to allocate 0.7% of GNI to ODA as well as pledge to allocate at least 0.15-0.2% of GNI to the LDCs. But the post-2015 agenda cannot be achieved through aid alone. There is a need to consider other forms of international public finance for investments in communicable disease control, climate change adaptation and mitigation, science, innovation and new technologies. More public resources for climate finance are needed, but these should not come at the expense of ODA. Transparency is essential to build a complete picture of the funds available for sustainable development. Measures of official development finance (such as what constitutes ODA) could also be developed in an open and transparent forum.

The post-2015 agenda cannot be achieved through public finance alone. Incentives are needed to ensure that private investment decisions move the world towards sustainable development aspirations. The progressive elimination of inefficient and ineffective subsidies and pricing greenhouse gas emissions could contribute to the changes in incentives that are needed. Satisfying the need for a major step-change in infrastructure development across large parts of the world could fuel economic development as well as fulfil essential human needs. Enhancing financial inclusion, especially targeting women, can make an important contribution to the financing for development agenda.

Volatility is becoming the new normal. There are many sources of risk and the financial costs of shocks as diverse as conflict, natural disasters, disease outbreaks and economic crisis are high and increasing. It is essential that all development is risk-informed. It is vital for governments to invest in resilience and set the right regulatory, investment and legal regimes to ensure that risk is reduced and managed.

While the range of challenges which need to be tackled is much wider than in the past, there are more resources and capabilities than ever before to tackle them. Globalization and new technologies also afford governments and other stakeholders new opportunities to collaborate and to tap into the pool of global resources – capital and knowledge – to pursue sustainable development objectives. The Addis Ababa process represents a chance to build a development finance architecture that represent all constituencies, is well resourced and delivers high-quality finance that supports internationally agreed objectives. Some of these choices will be difficult to make, but there will be major dividends if we get financing for sustainable development right.

Introduction

The Sustainable Development Goals (SDGs) are expected to define a more ambitious and bolder development agenda than their predecessor, the MDGs. On the one hand, the post-2015 development agenda is about problems inherited from the past, such as continued extreme poverty, hunger and gender inequality. On the other hand, the new agenda aims to tackle other problems which have emerged, or become more pronounced, over recent years, such as climate change, accelerated environmental degradation and income inequality. Whereas the MDGs focused on the process of development *within* countries, the post-2015 agenda is about the dynamics of development processes both *within* and *beyond* national borders, reflecting how intertwined nations' and peoples' prospects are.

The post-2015 agenda will be *universal* and will demand structural transformations in countries at *all* income levels to ensure that the planet's natural limits are respected. Technological innovations will play a critical role in these transformations. We know that while action by individual countries is essential, it will also be insufficient with effective international cooperation being more essential than ever.

These realities require us to think anew about how we approach the challenge of financing development. A key feature of the MDG-era was a tendency to emphasize the idea of resource 'gaps'. According to this narrative, developing nations needed to strengthen their capacities to mobilize domestic resources and combat corruption, as well as take measures to stimulate and attract private investment – domestic and international. Aid would come in where any 'gaps' remained. This approach will still be important in the post-2015 period. But the new agenda requires us to go beyond considering goal-specific resource gaps. The post-2015 agenda is at its core about the kinds of economic growth and development strategies that *all* countries choose to pursue, and whether these are consistent with sustainable development objectives.

UNDP's Administrator, Helen Clark, opened the consultations for the UN's 3rd Financing for Development Conference in November 2014. In her message, she emphasized that we have to see financing for development in a new way, integrating three elements.

1. First, we need to **recognize the continued importance – and value – of development aid**. Official Development Assistance (ODA) is often the largest source of external finance in some of the poorest and most vulnerable countries in the world, and plays a catalytic role in others. It is not easily substituted by private finance. It is also increasingly clear that the range of challenges that the new agenda aims to tackle requires us to go beyond development aid and that international public finance has to expand. This includes, but goes beyond, climate finance. The international community needs to ensure adequate public finance is available for a whole range of areas in ways which do not compromise or undermine ODA.

2. Second, it is clear that **the post-2015 agenda cannot be achieved through public finance** alone, whether mobilized domestically or flowing from external sources. Most of the resources needed to finance the post-2015 agenda will come from the private sources – households, businesses and investors. We need to ensure that private investment decisions – in both the real economy and in the financial sector – move the world towards the sustainable development aspirations set out in the post-2015 agenda. Philanthropic and social corporate responsibility actions by businesses and financial institutions are important (and welcome), and successes should be scaled-up but changes in regulatory frameworks will be needed – at both the national and international level – to provide incentives to ensure that more private finance supports long-term sustainable development aims.

3. Finally, we have to recognize that **volatility is becoming the new normal**. This means that financing for development in the post-2015 era cannot be considered only in the context of 'stable times'; there are fewer of them. There are many sources of risk and the costs of shocks as diverse as conflict, natural disasters, disease outbreaks and economic crisis are high and increasing. Achieving sustainable development will be impossible unless nations and communities are resilient, able to anticipate, shape and adapt to the many shocks and challenges that can frustrate development processes. What is essential is that all development is risk-informed.

This short document outlines in more detail UNDP's perspectives in these three areas as well as offers some views on several others which are currently under discussion in the context of the Addis Ababa Conference. These are, specifically:

- Domestic resource mobilization;
- Sovereign debt
- Inclusive global governance
- FfD follow-up

The Addis Ababa Conference provides an important opportunity for the international community to discuss the demands of the new agenda when it comes to financing, and to chart viable steps that *all* countries can take to support it. It could be a breakthrough moment going beyond Monterrey; an opportunity for a new compact that will be remembered in years to come and which will send a powerful signal of political support just before the September 2015 Summit that will define the SDGs. UNDP is working hard to support a successful outcome.

For the Administrator's speech, see: Helen Clark: Keynote address to Preparatory Session for The 3rd International Conference on Financing for Development United Nations, New York.

1) Development aid and other international public resources for development

i. Private financing is intrinsically not structured to help people without purchasing power to meet their basic needs or to fully finance projects where social benefits exceed private returns. In this context, it is clear that **ODA** will remain critical in the post-2015 period, in particular for the **Least Developed Countries** (LDCs) as well as countries in 'special' situations, such as **Small Island Developing States (SIDS)** and **fragile states.** It also has an important role to play in middle-income countries. ODA not only remains below commitments, but the share allocated to the poorest and most vulnerable countries remains low. In 2013, OECD DAC donors allocated, on average, just **0.3% of GNI to ODA**. The Addis Ababa conference represents an opportunity for donor countries to **reaffirm their longstanding commitment to allocate 0.7% of GNI to ODA** as well as pledge to **allocate at least 0.15-0.2% of GNI to the LDCs**. For UNDP, it will be important to emphasize that no country should be left behind.

ii. It is also increasingly clear that the demands of the post-2015 agenda and the **range of challenges that it seeks to address requires international public finance beyond ODA.** For example, funding will need to be stepped up for investments in areas such as communicable disease control, climate change adaptation and mitigation, science, innovation and new technologies in order to support and enable the kinds of economic transformations the world needs to see if we are to make progress on the post-2015 agenda. The role of technological innovation will be particularly critical to enable the transformations needed to sustain improvements in wellbeing while respecting the planet's natural boundaries. It is important for the

international community to think about how it can ensure adequate finance for all of these areas in ways which do not compromise or undermine ODA.

iii. **Climate change** threatens to reverse progress on poverty reduction, economic development and stability around the world. Many countries emphasize the **inadequacy of public climate finance, and a complex architecture** for these resources**.** External resources for climate change mitigation help development in the recipient nation, but also benefit all countries, when they have as principal objective emissions reductions. Given that financing for climate change mitigation is crucial and these flows need to be properly accounted for and recognized, the Addis Ababa conference provides an opportunity for the international community to consider the **UN Secretary-General's recent proposal for an expert technical group** to propose options for a more coherent framework that accounts for climate finance and ODA. More public resources for climate finance are needed, but these should not come at the expense of ODA. Building capacity to access, leverage and deploy climate finance is also an urgent priority. A balanced allocation of adaptation and mitigation finance for developing countries is also needed and the international community needs to ensure that adaptation finance is directed to those countries and communities facing the greatest climate impacts.

iv. Many developing countries have increased the size of their economies in recent years. It is important to bear mind, however, that income levels are not the only determinant of external public financing needs. Despite similar income per capita levels, countries can have extremely **differentiated capacities to mobilize domestic and external resources** for development. Some Small Island Developing States, for example, continue to experience severe constraints in their efforts to raise more revenues domestically, despite relatively higher income levels. I*n addition to* income per capita, other considerations such as **vulnerability** to **shocks** and to **climate change, countries' debt levels** and the **type of programme** being funded determine external financing needs as well as the most appropriate type of financial instrument. B**oth concessional and non-concessional finance** have a role to play in supporting sustainable development. However if a larger share of official financial flows are made available on non-concessional terms, the international community must be careful not to sow the seeds of future debt crises. The appropriate mix of concessional and non-concessional resources must be tailored to individual countries' specific circumstances.

v. Efforts to increase the volume of financing for development, must be accompanied by efforts to **strengthen the quality** of those resources. Enhancing the effectiveness of development cooperation – including through strengthening county ownership, use of country systems, a focus on results, transparency and accountability – can support implementation of the post-2015 agenda. The **Development Cooperation Forum of the Economic and Social Counci**l and other fora, such as the **Global Partnership for Effective Development Cooperation** can make a contribution by strengthening the quality of development cooperation and development partnerships.

vi. **Transparency** is essential in order to build a complete picture of the funds available for sustainable development, and how they are used. This can be achieved by **publishing timely, comprehensive and forward–looking information** on development activities in an **independent, common, open, electronic format.** We could learn from and strengthen existing initiatives and open data standards**.** A focus on **data and statistical systems at the country level** will be especially important in order to strengthen domestic capacity and accountability. Targeted support will be needed for this effort.

vii. **Measures of official development finance** (such as what constitutes ODA) could also be developed in an **open and transparent forum** with the widest possible participation of donor and recipient countries and other relevant stakeholders.

2) Leveraging private sources of finance

i. It is clear that the post-2015 agenda cannot be achieved through public finance alone, whether it is through domestic resources or ODA. Inevitably, most of the resources needed to finance the post-2015 agenda will come from **private sources – households, businesses and investors.** We need to ensure that private investment decisions – in both the real economy and in the financial sector – move the world towards the sustainable development aspirations set out in the post-2015 agenda. Growing pockets of **socially responsible investing** are welcome – and efforts should be made to scale up successful initiatives – but they will not on their own be sufficient to meet the demands of the post-2015 agenda.

ii. Government actions are needed to steer investment by the private sector towards sustainable and inclusive development. **Changes in regulatory frameworks** will be needed – at both the national and international level – to address misaligned incentives, minimize risk and ensure more private finance is aligned with long-term sustainable development aims. The progressive elimination of inefficient and ineffective subsidies – while minimizing any adverse impacts on the poor and affected communities – can play a useful role.

iii. In market economies, even with growing privately funded green investments, private finance continues to contribute to greenhouse gas emissions. Incentives need to change to have more private finance flow towards a low-carbon economy. **Pricing greenhouse gas emissions could contribute to the changes in incentives that are needed**. Measures which could be explored include the domestic and international auctions of emissions allowances and/or carbon taxes.

iv. The need for a **major step-change in infrastructure development** across large parts of the world to fuel economic development as well as fulfil essential human needs is well recognized. With populations and aspirations growing, some estimates suggest annual spending on infrastructure in the developing world needs to increase to between US$ 1.8-2.3 trillion each year by 2020. It is essential that this infrastructure be **developed sustainably.** Domestic budgets will continue to play an important role in infrastructure development. Unlocking capital flows at the local level can be transformative. But there will be inevitable constraints, such as debt sustainability considerations. Often private capital is available but it is not affordable and/or provided at maturities that would enable countries to make longer-term investments in areas such as infrastructure. One option which could be explored by the international community is to agree to work on **'Sustainable Infrastructure Action Plans'.**

v. Enhancing **financial inclusion** can make an important contribution to the financing for development agenda. When people and businesses have access to appropriate and responsibly provided financial services such as savings, credit, insurance, payments and other financial instruments, they can use these to engage productively in the real economy. It is especially important to **target women** and to ensure that they have access not only to resources, but also to capacity building opportunities and are able to participate in key decision-making processes.

vi. While **migrant remittances** cannot be considered as a source of development finance for governments, those funds will help the balance of payments and contribute to greater economic activity. This can be

enhanced, in part, by reducing the cost of sending remittances to migrants' countries of origin. Globally, officially recorded remittances are expected to reach US$515 billion in 2015 with the vast majority of these resources sent to developing countries. **It is both efficient and right to reduce the high costs associated with making these transfers.** A **global not-for-profit remittance platform** could also be valuable.

3) Managing risk and building resilience

i. **Risk and resilience** are often not front and centre of international policy discussions on financing for development. But in our highly interconnected and challenged world, **volatility** is the new normal. There are many sources of risk and the financial costs of shocks as diverse as conflict, natural disasters, disease outbreaks and economic crisis are high and increasing. Financing for development in the post-2015 era cannot be considered only in the context of 'stable times'; there are fewer of them. Achieving sustainable development will be impossible unless nations and communities are resilient, able to anticipate, shape and adapt to the many shocks and challenges that can frustrate development processes. **What is essential is that all development is risk-informed.**

ii. It is vital for governments to **invest in resilience** and set the right **regulatory, investment and legal regimes** to ensure that risk is reduced and managed, while also boosting the coping capacity of nations and communities. We now have a significant opportunity to develop a more sophisticated framework which tackles underlying vulnerabilities and incorporates risk management and resource allocation *over time*. Investments now in critical areas, whether they are public health or renewable energy, will minimize risk and future costs in the years to come.

4) Domestic resource mobilization

i. **Effective domestic resource mobilization** is at the core of financing for sustainable development. **Tax and expenditure policies** in countries at *all* income levels should be fully aligned with sustainable development objectives. Publishing analysis and information on the distributional and environmental implications of tax and expenditure policies can support this aim. Given the importance of the **gender dimension** in development, commitments to gender equality and the **universal adoption of gender-responsive budgets** at all levels are of the utmost importance.

ii. Governments' efforts to raise more domestic resources are sometimes constrained by **tax evasion and avoidance**, and by **illicit financial flows**. Global co-operation is the only way to solve these problems. At the national level, **strengthening legal environments** to tackle tax avoidance and evasion will be important. Governments could also make an important contribution by **analyzing and publishing information on the international spillovers of domestic tax policies.** At the international level, the Addis Ababa conference provides an opportunity for the international community to consider establishing an **intergovernmental committee on tax cooperation**, under the auspices of the United Nations. The mandate, structure and governance for this committee should be agreed by the UN General Assembly.

iii. Capacity to mobilize domestic resources improves as countries grow and develop. Strengthening support in developing countries for **building the capacities of tax systems and administrations** is important, as well as the means to help inform decisions on resource allocation that are efficient and spur sustainable development.

5) Sovereign debt

i. **Sovereign debt crises** affect countries at *all* income levels and can lead to considerable human development set-backs. Debt crises continue to be addressed too late and too slowly. Debt crises prevention and management needs to improve.

ii. In relation to **debt crisis prevention**, it will be important for governments to further **strengthen debt management capacities**, and be supported in their efforts to do so. **Independent and regular** debt sustainability analyses can also help to provide timely information on the risks of debt distress – but should not be relied on in a mechanistic fashion. **Strengthening transparency** in lending and borrowing and strengthening **data collection** will also be crucial.

iii. The 2008 global economic and financial crisis and, more recently, the Ebola crisis in West Africa have highlighted how **fragile countries' debt positions** can become when a **major shock** occurs. There is a need for the international community to help countries to respond to such crises, through making sure appropriate financing is made available on a timely basis and, where appropriate, debt relief. Discussions around approaches **for sovereign debt crisis resolution which are comprehensive, timely, transparent and impartial need to continue**.

iv. Finally, it is important for UNDP to highlight that some countries, including some **Small Island Developing States (SIDS)**, are currently experiencing significant debt sustainability challenges; their predicament requires urgent and special attention. To devise an appropriate response to their debt challenges, the international community can draw on valuable lessons learned from the recent Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI).

6) Inclusive global governance

i. The "scaffolding" matters. Many developing countries continue to be **underrepresented or excluded from decision-making in key international fora.** More effective participation and representation of developing countries in international dialogues and decision-making processes was a key aim of the 2002 Monterrey Consensus on Financing for Development. But progress has been slow. The Addis Ababa conference provides a window to reinvigorate this effort.

7) FfD Follow-up

i. A robust follow-up process will be an important measure of the conference's success. It will be critical to put in place a system to **monitor all financial commitments independently and effectively** as well as **strengthen national capacities to monitor and publish data on different financial flows**, and their impact on sustainable development.

ii. A dedicated inter-governmental body to monitor progress on FfD commitments and ensure that there are no gaps between commitments and implementation will also be important.