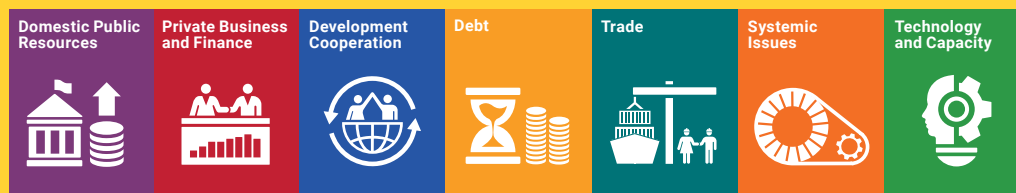




Financing for Sustainable Development Report 2024

Inter-agency Task Force on Financing for Development

Financing for Development at a Crossroads



United Nations

Report of the Inter-agency Task Force
on Financing for Development

Financing for Sustainable Development Report 2024

Financing for Development at a Crossroads



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Inquiries about the Task Force or its report and online annex can be sent to:

Financing for Sustainable Development Office
Department of Economic and Social Affairs
2 United Nations Plaza (DC2–23rd Floor)
New York, N.Y. 10017
United States of America
+1-212-963-4598
developmentfinance@un.org
<http://developmentfinance.un.org>



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Foreword



Nine years ago in Addis Ababa, the global community agreed an agenda to enable countries to mobilize and align the financial resources needed to achieve the 2030 Agenda and the Sustainable Development Goals.

The *2024 Financing for Sustainable Development Report* makes clear that halfway to 2030, the promise of the Addis Ababa Action Agenda remains largely unfulfilled.

Moreover, the past four years of global turmoil have increased the financing needs of developing countries. Financing gaps for those countries now stand at USD\$4 trillion every year.

Decades of progress on poverty and hunger have stalled, and in some cases, been thrown into reverse. Many developing economies are mired in debt, making progress on financing for development even more urgent.

Meanwhile the climate crisis is tightening its grip, unleashing floods, hunger, and deadly droughts on some of the world's most vulnerable communities. Inequalities, already at record levels, are getting wider. Trust in institutions, and solidarity between developing and developed economies, is low and falling.

We have work to do.

Our proposed SDG Stimulus of USD\$500 billion per year of additional investments in sustainable development and climate action includes concrete steps that global leaders can take right now.

These include changes to the lending practices of multilateral development banks that would unleash their potential and get capital flowing back to developing countries. The banks should be empowered to raise more capital and stretch their balance sheets. Creditors should come together to pre-emptively extend loan periods to ease the burden of debt service payments before countries are forced into default. The Common Framework for debt treatment should also be overhauled to enable faster resolution for countries already in default.

At same time, governments must start work on reforming the international financial architecture, which is dysfunctional, outdated, and unfair.

The new architecture must represent the world of today, giving a proportionate voice to the countries of the Global South. And it must respond to the challenges of today – including the climate crisis. It must be sensitive to global shocks, boosting reserves and mitigating imbalances as needed. And it must catalyze flows of private finance into the green economy and incentivize investments in resilience and adaptation.

The Summit of the Future later this year and the Fourth International Conference on Financing for Development in 2025 will be opportunities to galvanize political will, create momentum, and set ambitious benchmarks for action.

Financing for development is a transformative resource that can reduce poverty and hunger and provide billions of people with the opportunity of a better future. It is also an essential tool to bring a measure of justice to the global economy and help to bridge the deep divisions that afflict our world.

We have no time to lose.

Secretary-General António Guterres



Preface



Financing for Development is at a crossroads. This 9th Report of the Inter-agency Task Force on Financing for Development, published as we embark on preparations for the Fourth International Conference on Financing for Development (FfD 4), to be held from 30 June to 3 July 2025 in Spain, paints a sobering picture.

The window to rescue the SDGs and prevent catastrophic climate change is closing. We are falling short on core commitments of the 2030 Agenda such as ending extreme poverty and hunger.

Financing challenges—including an investment crisis, driven by a sluggish global economy and tight financing conditions—have hampered our progress, preventing the urgently needed investment push in the SDGs.

But amid these challenges there lies opportunity. If we can address the big financing challenges of today—close the growing financing gaps, fix the international financial architecture, and create enabling environments at all levels to finance the ambitious transformations we need—then we can still succeed. It will be difficult, but it is doable.

As we prepare for FfD 4, we can build on the shared recognition by all stakeholders that we must act with urgency. The Task Force has highlighted four overarching questions that warrant Member States' attention in a fourth FfD Conference:

- How can we close financing and investment gaps, building on the proposals in the SDG Stimulus, and mobilize and align all sources of finance?
- How can we close gaps in the international financial architecture, and make it fit for purpose for today's challenges?
- How do we close credibility gaps in financing and rebuild trust in the global partnership and multilateralism?
- And how can we formulate and finance new development pathways to deliver on the SDGs?

This Report lays out recommendations on these questions across the action areas of the Addis Agenda. But the work is only beginning.

As the Chair of the Inter-agency Task Force, I am committed to bring the full knowledge, expertise, and range of perspectives of the Task Force to the preparatory process for FfD 4.

As it has done through its nine years of joint work, the Task Force will do its utmost to ensure that these preparations build on a sound evidence base, and make use of creative, ambitious, and technically sound proposals that can be considered to meet today's financing challenges.

Li Junhua
Under-Secretary-General for Economic and Social Affairs
United Nations
Chair of the Inter-agency Task Force



Contents

Foreword	iii
Preface	v
Inter-agency Task Force members	ix
Executive summary	xiv
 I. Introduction and overview	 1
1. Introduction	1
2. The financing challenge today	2
3. How did we get here?	3
4. Conclusion	13
5. Perspectives on the Fourth International Conference on Financing for Development	14
 II. The global economic context and its implications for sustainable development	 27
1. Introduction	27
2. Global and regional growth trends and outlook	28
3. Deterioration in public finances	30
4. Monetary and financial stability risks.	33
5. Weak investment prospects	35
6. Labour markets	36
7. Climate risks and the global economy	37
8. Conclusion	38
 III.A Domestic public resources	 44
1. Key messages and recommendations.	44
2. Domestic resource mobilization	45
3. International tax cooperation	51
4. Illicit financial flows	56
5. SDG-related expenditure and investment	57
 III.B Domestic and international private business and finance.	 68
1. Key messages and recommendations.	68
2. Investment trends in an evolving global economy: The long view	69
3. Aligning business with sustainable development.	73
4. Aligning finance with sustainable development	79
 III.C International development cooperation.	 98
1. Key messages and recommendations.	98
2. Official development assistance	99
3. The role of MDBs	105
4. Blended finance and mobilized private finance	108

5.	South-South cooperation	110
6.	Finance for climate change and biodiversity.	112
7.	Quality, impact and effectiveness of development cooperation	114
III.D	International trade as an engine for development	122
1.	Key messages and recommendations.	122
2.	Trade trends: Long-term trends in trade since Monterrey	123
3.	The multilateral trading system: Changing scope and geographies	127
4.	Trade and sustainable development in a complex global landscape	129
5.	Trade and development financing.	136
III.E	Debt and debt sustainability	144
1.	Key messages and recommendations.	144
2.	Overview of global debt trends	145
3.	Sustainable debt financing and the SDGs	150
4.	Debt crisis prevention and resolution: Progress made and challenges ahead.	154
III.F	Addressing systemic issues.	164
1.	Key messages and recommendations.	164
2.	The global financial safety net.	165
3.	Financial market regulation and supervision for sustainable development.	172
4.	Payments and market infrastructure	175
5.	Global governance and policy coherence.	177
III.G	Science, technology, innovation and capacity building	184
1.	Key messages and recommendations.	184
2.	The transformational but uneven impacts of rapid technological change	185
3.	Technology and financing for development: Fintech and the implications of STI for action areas of the Addis Agenda	196
IV.	Data, monitoring and follow-up	208
1.	Key messages and recommendations.	208
2.	Data frameworks for sustainable development	209
3.	National statistical systems and funding.	217

Inter-agency Task Force members

Task Force coordinator and substantive editor



United Nations Department of Economic and Social Affairs (UN/DESA)

Financing for development major institutional stakeholders



World Bank Group



International Monetary Fund (IMF)



World Trade Organization (WTO)



United Nations Conference on Trade and Development (UNCTAD)



United Nations Development Programme (UNDP)

Regional economic commissions



Economic and Social Commission for Asia and the Pacific (ESCAP)



Economic and Social Commission for Western Asia (ESCWA)



Economic Commission for Africa (ECA)



Economic Commission for Europe (UNECE)



Economic Commission for Latin America and the Caribbean (ECLAC)

United Nations system and other agencies and offices



Basel Committee on Banking Supervision (BCBS)



Committee on Payments and Market Infrastructure (CPMI)



Financial Stability Board (FSB)



Food and Agriculture Organization of the United Nations (FAO)



Global Environment Facility (GEF)



Green Climate Fund (GCF)



International Association of Insurance Supervisors (IAIS)



International Atomic Energy Agency (IAEA)



International Civil Aviation Organization (ICAO)

	International Development Finance Club (IDFC)
	International Fund for Agricultural Development (IFAD)
	International Labour Organization (ILO)
	International Organization for Migration (IOM)
	International Telecommunication Union (ITU)
	International Trade Centre (ITC)
	Joint United Nations Programme on HIV/AIDS (UNAIDS)
	Office of the High Commissioner for Human Rights (OHCHR)
	Office of the High Representative for the Least Developed Countries, Landlocked Developing Countries and Small Island Developing States (OHRLS)
	Office of the Special Adviser on Africa (OSAA)
	Organisation for Economic Co-operation and Development (OECD)
	Principles for Responsible Investment (PRI)
	Secretariat of the Convention on Biological Diversity (CBD)
	South Centre
	Sustainable Energy for All (SE4All)
	The Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES)
	The Global Alliance for Vaccines and Immunizations (GAVI)
	UN Capital Development Fund (UNCDF)
	United Nations Children's Fund (UNICEF)
	United Nations Commission on International Trade Law (UNCITRAL)
	United Nations Convention to Combat Desertification (UNCCD)
	United Nations Educational, Scientific and Cultural Organization (UNESCO)
	United Nations Entity for Gender Equality and the Empowerment of Women (UN Women)
	United Nations Environment Programme (UNEP)
	United Nations Forum on Forests (UNFFS)
	United Nations Framework Convention on Climate Change (UNFCCC)
	United Nations Global Compact (UNGC)
	United Nations High Commissioner for Refugees (UNHCR)
	United Nations Human Settlements Programme (UN-HABITAT)
	United Nations Industrial Development Organization (UNIDO)
	United Nations Office for Disaster Risk Reduction (UNISDR)
	United Nations Office for Project Services (UNOPS)

	United Nations Office for South-South Cooperation (UNOSSC)
	United Nations Office for the Coordination of Humanitarian Affairs (OCHA)
	United Nations Office on Drugs and Crime (UNODC)
	United Nations Population Fund (UNFPA)
	United Nations Research Institute for Social Development (UNRISD)
	United Nations Technology Bank for Least Developed Countries (UN Technology Bank)
	United Nations University (UNU)
	United Nations World Food Programme (WFP)
	United Nations Youth Office
	World Health Organization (WHO)
	World Intellectual Property Organization (WIPO)

Executive summary



Executive summary

Financing challenges are at the heart of the current sustainable development crisis. Yet financing is also key to turning our fortunes around and getting back on track. The Fourth International Conference on Financing for Development next year in Spain provides a unique opportunity to reform financing at all levels to close the gap between aspiration and financing.

Countries are off track on the 2030 Agenda for Sustainable Development, with around half of the 140 Sustainable Development Goal (SDG) targets for which sufficient data is available deviating from the required path. Current projections estimate almost 600 million people will continue to live in extreme poverty in 2030, more than half of them women. Progress is woefully inadequate on climate action, with global greenhouse gas emissions still rising when rapid and deep reductions are needed.

Achieving the economic transitions needed to reach the SDGs will require investments at unprecedented scale. Unmet financing needs for SDGs and climate action are estimated to be in the trillions of dollars annually. Yet, the costs of inaction, both economic and social, would be far higher still. Financing needs are particularly acute in many developing countries which face higher costs of capital and significantly worse terms of access to financing. Due to misaligned incentives, both public and private actors still invest in brown activities and have not yet fully aligned their decision-making and financing with the SDGs.

While there has been real progress across the financing agenda since the adoption of the Monterrey Consensus on Financing for Development in 2002, financing for development has not kept pace with rising needs amid a changing and less benign global environment. Systemic risks, especially climate and disaster-related risks, have risen dramatically. There has been a sea-change in global macroeconomic and macro-financial conditions, with GDP growth rates in developing countries falling to just over 4 per cent annually on average between 2021

and 2025, after averaging around 6 per cent before the 2009 global financial crisis. Income, wealth, gender and other forms of inequality, which are often perpetuated by financing policies, have become entrenched. Enormous technological change, digitalization in particular, is affecting all financing areas. And there are growing risks of fragmentation in the global economy. While some of these trends have created opportunities for development and financing progress, in their totality, they have put national financing frameworks and the international financial architecture under severe stress.

Today, many countries are faced with tight fiscal constraints and high risks of debt distress, with the median debt service burden for LDCs rising from 3.1 per cent of revenue in 2010 to 12 per cent in 2023 – the highest level since 2000. Four in 10 of the global population live in countries where governments spend more on interest payments than on education or health. Private sector development, a key driver of sustainable growth and development, has stalled in recent years as investment growth, trade, and technology diffusion slowed. Structural changes pose new challenges for countries' productive integration into the world economy, necessitating a search for new growth and development strategies. And while financial inclusion is a bright spot, financial and capital markets remain underdeveloped in many developing countries, with financial volatility contributing to the dearth of long-term investment.

The window to rescue the SDGs and prevent a climate catastrophe is still open but closing rapidly. United Nations Member States have given the Fourth International Conference on Financing for Development (FfD4), to be held in Spain from 30 June to 3 July 2025, an ambitious mandate to address financing challenges "in the context of the urgent need to accelerate the implementation of the 2030 Agenda and the achievement of the SDGs and to support reform of the international financial architecture."

This 2024 *Financing for Sustainable Development Report* is designed to enable a productive and substantive preparatory process for this Conference. To that end, the Task Force highlights four sets of overarching questions that warrant Member States' attention:

- **How can FfD 4 help close large financing and investment gaps, at scale and with urgency, and enhance spending effectiveness?** What is the package of reforms that can help deliver the rapid scaling up of public and private investments in the SDGs, and containing actions across tax, private investment and blended finance, concessional financing and development bank reform, and innovative financing instruments? How can the Conference help governments do more on domestic resource mobilization and optimizing spending through growth- and revenue-enhancing reforms, to better allocate scarce resources while prioritizing the SDGs?

How can FfD 4 help address issues in the international financial architecture and support international rules for trade, investment and finance that are fit for today's challenges? Which international financial architecture reforms could enhance countries' resilience in

a more crisis-prone world and enable access to financing on the right terms and conditions? How can the international community fully align trade, investment and technology agreements and rules with sustainable development?

- **How can FfD 4 close credibility gaps and rebuild trust in global partnership and multilateralism?** How can public and private actors reconcile misalignment between rhetoric and action and renew momentum for finally meeting long-standing commitments on concessional financing, global governance reform, and fully aligning domestic and international policy frameworks and investment allocations with commitments to the SDGs?
- **How can FfD 4 help formulate and finance new development pathways to deliver on the SDGs and ensure no one is left behind?** How can the ongoing rethinking of economic development paradigms, not least the relationship between states and markets in achieving sustainable transformations, inform new national and international financing policy frameworks for sustainable development?

Introduction and overview



Chapter I



Introduction and overview

1. Introduction

Financing for development is at a crossroads. The world is running out of time to achieve the Sustainable Development Goals (SDGs) and prevent catastrophic climate change. Only an urgent, large-scale and sustainable investment push can help us achieve these agendas. Despite efforts to advance development financing across the action areas of the financing for development agenda over the last two decades, countries are today faced with large unmet financing needs and a financial architecture unable to close these gaps in an ever more crisis-prone world. The gap between our development aspirations and the financing dedicated to meet them has never been so large.

The window to rescue the SDGs and prevent a climate catastrophe is still open but closing rapidly. Over the last several years, the world has contended with persistent pandemic-related uncertainties, ramped up geopolitical divides and war, and increasingly restrictive financing conditions—all of which represent direct challenges to the achievement of the SDGs. But the SDGs were off track even before this recent confluence of crises, with financing neither mobilized at the scale nor allocated at the terms necessary to achieve deep economic and societal transformation.

Financing challenges are one of the key reasons for slow progress and regression:

- **Financing challenges are at the heart of the current sustainable development crisis.** Unmet financing needs for the SDGs and climate action are estimated to be in the trillions of dollars. The needs are particularly acute in many developing countries: When the series of shocks and food and energy crises set back sustainable development around the world, a finance divide severely hampered many developing countries in responding aggressively; as a result, they saw larger and more persistent SDG regression. Globally, and despite commitments to the contrary, many actors,

both public and private, still invest in brown activities and have not yet fully aligned their decision-making and financing allocations with the SDGs.

- **Today's tight financing conditions are exacerbating an investment crisis, hampering the urgent scaling up of sustainable development investments.** Tighter global financial conditions in a world awash with debt reduce fiscal space for many sovereigns, create high costs of capital for private investors, and contribute to a sluggish recovery of the global economy, with subpar growth and investment prospects.

A key to getting back on track lies in financing. Financing challenges have played a key role in creating the sustainable development crisis we face today. But financing can also play a role in turning our fortunes around. The United Nation's financing for development discussions can be a catalyst for change. In the spring of 2002, world leaders convened in Monterrey, Mexico, to “address the challenges of financing for development around the world, particularly in developing countries”.¹ The Monterrey Consensus represented a historic breakthrough. It recognized the critical importance of mobilizing and effectively using financial resources, and enabling national and international economic conditions, to eradicate poverty and achieve sustainable development. It anchored discussions on financing and the international financial architecture in the development agenda. That link is now more important than ever, with a broader development agenda agreed in 2015—embodied in the 2030 Agenda for Sustainable Development and the Paris Agreement on climate change—laying out an ambitious but indispensable set of sustainable development objectives. At the same time, financing for development commitments were reaffirmed and updated in the Addis Ababa Action Agenda, which provided a global framework for financing sustainable development.

The Fourth International Conference on Financing for Development, to be held in Spain in mid-2025, provides a unique opportunity to commit to reforms of financing frameworks at all levels to close the gap between aspiration and financing. Today, the enabling environments for financing sustainable transformations are not in place. At the same time, the recognition that the world is running out of time has triggered a new commitment to financing reform by governments, the private sector and the international community. As daunting as the financing challenges are, there is at least a shared understanding that we must address them with urgency and ambition. Member States have acknowledged this urgency in discussions at the United Nations and beyond. They have given the Fourth International Conference on Financing for Development an ambitious mandate to address financing challenges “in the context of the urgent need to accelerate the implementation of the 2030 Agenda and the achievement of the SDGs and to support reform of the international financial architecture”.²

The Inter-agency Task Force highlights four overarching questions that warrant the attention of Member States:

- **How can the conference help close the large financing and investment gaps, at scale and with urgency, and enhance the effectiveness of spending?** What is the package of reforms that can help to deliver the rapid scaling up of public and private investments in the SDGs, building on the Secretary-General’s SDG Stimulus, and containing actions across the action areas: on tax, private investment and blended finance, concessional financing and development bank reform, and innovative financing instruments? And how can the conference help governments to do more on domestic resource mobilization and optimizing spending through growth- and revenue-enhancing reforms, to better allocate scarce resources while prioritizing the SDGs?
- **How can the conference help close gaps in the international financial architecture and support international rules for trade, investment and finance that are fit for purpose for today’s challenges?** Which international financial architecture reforms could enhance countries’ resilience in a more crisis-prone world and enable access to financing on affordable terms and conditions? How can the international community align trade, investment and technology agreements and rules fully with sustainable development?
- **How can the conference help close credibility gaps and rebuild trust in the global partnership and multilateralism?** How can public and private actors reconcile misalignment between rhetoric and action and renew momentum for finally meeting long-standing commitments on concessional financing and global governance reform and fully aligning domestic and international policy frameworks and investment allocations with commitments to the SDGs?
- **How can the conference help to formulate and finance new development pathways to deliver on the SDGs and ensure that no one is left behind?** How can the ongoing rethinking of economic development paradigms, not least the relationship between States and markets in achieving sustainable transformations, inform new national and international financing policy frameworks for sustainable development?

To help address these questions, the 2024 Financing for Sustainable Development Report aims to support a productive

and substantive preparatory process for the upcoming Fourth International Conference on Financing for Development. To this end, this overview chapter lays out the key financing challenges (section 2), the underlying drivers (section 3.1), and progress and gaps in implementation across the action areas, highlighting key findings from the rest of the report (section 3.2), before concluding (section 4). In section 5, the major institutional stakeholders of the FfD process and UN DESA share institutional perspectives on and expectations for the forthcoming Fourth Conference

2. The financing challenge today

The world is severely off track to achieve the SDGs by 2030. At the midpoint towards 2030, around half of the 140 SDG targets for which sufficient data is available deviate from the required path. This includes central commitments such as the eradication of extreme poverty; current projections estimate almost 600 million people will continue to live in extreme poverty in 2030, more than half of them women.³ On a “business-as-usual” pathway, where social, economic and technological trends do not shift markedly from historical patterns, the SDGs as a whole would remain out of reach even in 2050.⁴

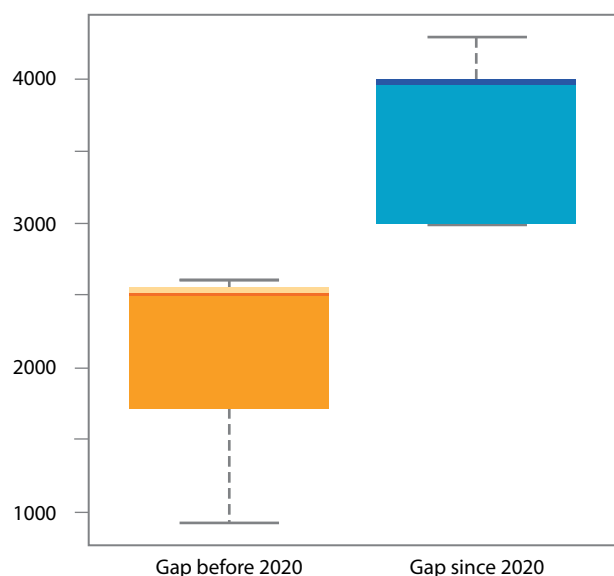
Progress is woefully insufficient on SDG 13, climate action. The year 2023 was the hottest year on record by a significant margin. Rapid and deep reductions in global greenhouse gas emissions would be needed this decade (a decline of 43 per cent compared to 2019 emissions) to keep temperature increases below 1.5 degrees Celsius;⁵ instead, emissions from fossil use are expected to have reached a record high in 2023.⁶

Financing gaps

Financing gaps are large and growing. Achieving the large-scale transitions needed to avoid catastrophic climate change will require investments at an unprecedented scale. There have been various efforts, including from members of this Task Force, to estimate SDG financing and investment gaps. While they vary, the gaps found are inevitably very large, particularly for developing countries, ranging between \$2.5 trillion and \$4 trillion annually (figure 1.1).⁷ Such gaps were already large before 2020, but they have since widened significantly, with the Organisation for Economic Co-operation and Development (OECD) Global Outlook estimating an increase in the financing gap of developing countries of 56 per cent.⁸ The COVID-19 pandemic and subsequent shocks negatively impacted resources, including lost tax revenue from lower growth rates, further widened investment gaps and have added to financing needs. From a global perspective, financing gaps are largest in middle-income countries (MICs). However, relative to available resources and capacity to mobilize additional resources domestically, least developed countries (LDCs) and low-income countries (LICs) face the most significant gaps, with estimates ranging between around 15 per cent and 30 per cent of their respective GDP (for example, a recent assessment by the International Monetary Fund (IMF) found the financing gap to achieve significant progress toward five SDGs—education, health, water and sanitation, electricity, and roads—to amount to 16.1 per cent of the GDP of LDCs and other LIC by 2030).⁹

As high as financing gap estimates are, they pale in comparison to the costs of inaction. This is best understood for the climate-related SDGs (primarily SDGs 7 and 13, which account for a significant share

Figure I.1
Range of estimates of annual SDG financing gaps in developing countries
 (Billions of United States dollars)



Source: Matzner and Steininger 2024.

of overall SDG financing needs) and the social and economic costs of climate change under business-as-usual scenarios. The cumulative additional economic and social costs incurred from climate change under a business-as-usual scenario through 2050 are estimated to be almost five times larger than the climate finance needed to limit temperature increases to 1.5 degrees Celsius.¹⁰ Every dollar invested in risk reduction and prevention can save up to 15 dollars in post-disaster recovery efforts.¹¹ These costs will only increase the longer investments in climate action and resilience are delayed.

Finance divides

Developing countries are faced with significantly worse terms of access to both long-term and contingency financing, implying a finance divide (see the *Financing for Sustainable Development Report 2022*). In the current high interest rate environment, sovereign spreads (the difference between the yields paid by developing country issuers and United States Treasuries) have increased particularly strongly for developing country issuers below investment grade (see chapter III.E), increasing their reliance on concessional resources to abate overall financing costs. The implicit interest rate on the sovereign debt of LDCs and MICs is more than twice that of developed countries, on average (figure 1.2), reflecting sizeable country premia, driven both by domestic factors and the retrenchment of capital flows to these countries.

Higher sovereign borrowing costs are also mirrored in higher costs of capital for private investors. For example, costs of capital for comparable projects in the renewable energy sector have been estimated to be significantly (two to three times) higher in developing countries than in developed countries, with perceptions of macroeconomic risks, rather than project-specific risks, driving risk premia (see also chapter III.B).¹²

Many developing countries also have less access to contingency financing in times of need, constraining their ability to respond to and recover from shocks. Few developing countries have access to central bank swap lines, which have been the most effective instruments for crisis management in the past 15 years, providing urgent liquidity at almost no cost (see chapter III.F). At the same time, IMF financing is limited in volume. While Special Drawing Rights (SDRs) were effectively allocated in crisis periods, the mechanism for allocating SDRs in proportion to countries' IMF quota shares means that developing countries received only around one third of the 2021 SDR allocation. During the pandemic, many developed countries enacted massive fiscal stimuli to protect their economies and societies, supported by aggressive monetary policy. Most developing countries, especially LDCs, have been unable to respond at a comparable scale.

Weak enabling environments for sustainable development

The enabling environment is lacking from a macro and micro-economic perspective. Policy, regulatory and tax frameworks, while pursuing a wide range of policy objectives, also set incentives for private investors; currently, these are often not sufficiently aligned with the SDGs and climate action; public expenditure is also not fully aligned. Rapid transformations require enabling environments so that all actors align their actions, through appropriate regulatory and legal frameworks, fiscal systems and trade and investment agreements. Currently, public subsidies and private investment in fossil fuels are still very high, and public expenditure and tax systems do not completely comport with the SDGs, including SDG 5 on gender equality.

3. How did we get here?

Today's financing challenges are the result of a dramatically changing global landscape, with financing not keeping pace.

Recent crises have revealed structural deficits and challenges that have arisen over longer time periods. Section 3 will briefly discuss the changing global context and broad underlying trends in the global economy that have shaped development finance decisions and outcomes over the last 20 years (section 3.1.) before reviewing the progress that has been achieved in the action areas of the financing for development outcomes within that rapidly evolving global context (section 3.2).

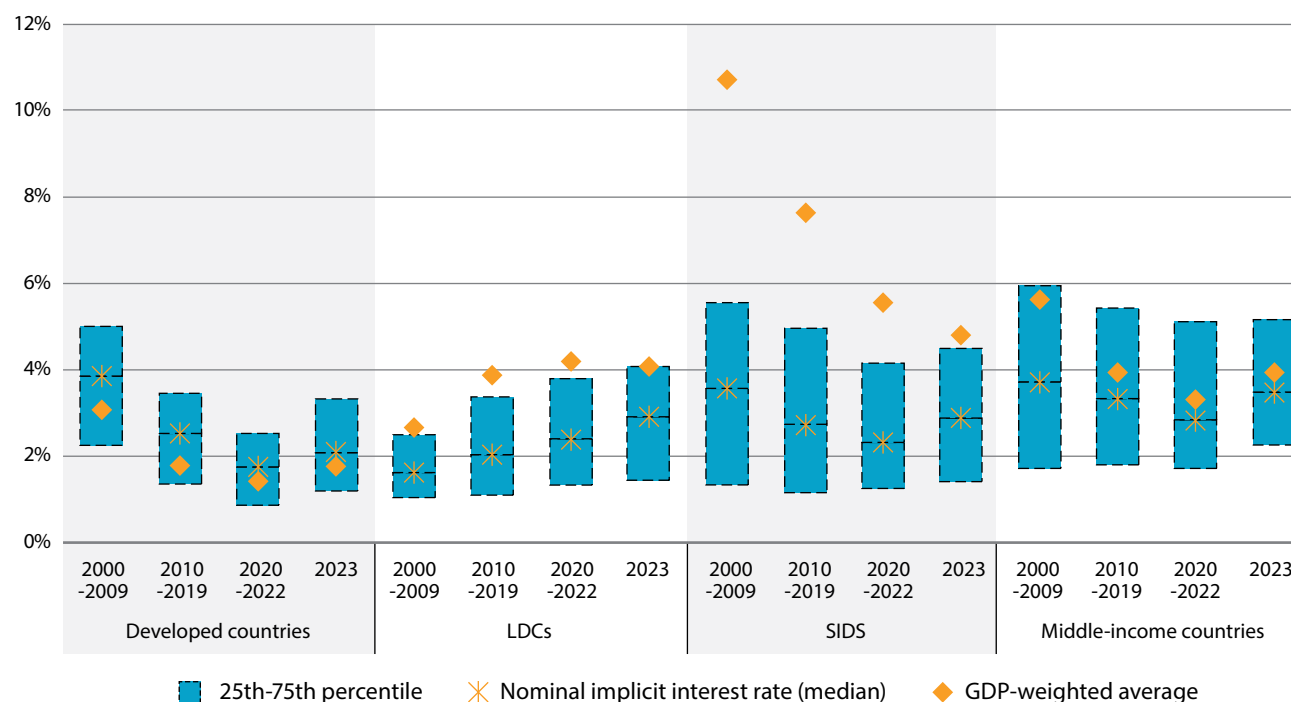
3.1 Underlying drivers and trends

A number of global trends and developments have significantly reshaped global development prospects and the development financing landscape. These include the rise in systemic risks, above all climate and disaster-related risks; a sea-change in global macroeconomic and macro-financial conditions; dramatic changes in the international division of labour and the pace of global economic integration; rising and entrenched income, wealth, gender and other forms of inequality; enormous technological change, with digitalization in particular affecting all financing areas; and growing risks of fragmentation in the global economy. Some trends have also created tremendous opportunities for development and financing progress. But in their totality, they have put national financing frameworks and the international financial architecture under severe stress.

Figure I.2

Implicit interest rates on sovereign debt, 2000–2023

(Percentage)



Source: UN DESA calculations, based on IMF WEO data.

Rising systemic risks

Risks continue to accumulate and become more complex and systemic at a rate faster than our capacity to predict, reduce or prevent them—we live in an age of uncertainty. Together, these risks create a macro-environment that has challenged, and in many cases overwhelmed, policymakers' ability to respond (see the *Financing for Sustainable Development Report 2021*).

- **The climate crisis is omnipresent.** It not only weighs on sustainable development, particularly in vulnerable countries such as LDCs and small island developing States (SIDS),¹³ but is also affecting financing: rising financing needs for investments in adaptation and mitigation, growing stresses on public and private balance sheets, and growing risks to financial sector and macroeconomic stability.
- **Disasters are becoming more frequent and intense, with losses, damages and recovery costs increasing.** Annual economic disaster damage is estimated at \$173 billion between 2020 and 2023, up from \$108 billion during the first decade of the century (see chapter II). By 2030, the world is projected to face 560 medium- to large-scale disasters per year.¹⁴ Conflict and displacement persist. In 2022, a record 32.6 million disaster displacements were recorded, 41 per cent higher than the annual average of the past 10 years.¹⁵
- **The COVID-19 pandemic further underscored the dramatic impacts that global non-economic systemic risks can have on social and economic progress.** In addition to the loss of life, economic losses from the pandemic and subsequent global shocks have

been staggeringly high, especially for vulnerable countries, translating into much larger SDG financing gaps. Cumulative output losses—calculated as the sum of the annual difference between pre-pandemic projections of GDP and actual GDP—amounted to around 40 per cent of the 2019 GDP in SIDS, and about 30 per cent in LDCs (see chapter II).

- **Systemic risks from economic and financial channels also remain elevated.** Financial globalization has contributed to capital flow volatility and exposed developing countries more directly to shocks and to spillover effects from monetary and financial policies in major developed countries (see chapter III.F). The 2008 world financial and economic crisis exemplifies the impacts that cross-border spillovers of financial instability can have on development prospects. Global factors such as global interest rates, risk aversion and uncertainty have become more important relative to idiosyncratic host country factors in determining cross-border capital flows.¹⁶

*A more challenging global economic environment***Closing financing gaps has become more challenging in today's context of tight financing conditions and a weak global economy.**

The global macroeconomic context, more favourable in the early years of the new millennium, has become less benign over the last two decades, impeding countries' efforts to mobilize development financing.

A sluggish world economy has led to subdued growth prospects in developed and developing countries (see chapter II). Average growth rates have steadily declined over the last 25 years, and the 2020s are primed to become another lost decade for development (see

chapter II and figure 1.3). The world economy developed dynamically in the first decade of the new millennium on the back of rapid growth of large emerging economies, a commodities boom and other factors. The 2008 world financial and economic crisis proved to be an inflection point, with developed economies experiencing severe recessions and very slow recoveries. Developing countries initially demonstrated more resilience but experienced a significant slowdown in dynamism from around 2014. The COVID-19 pandemic then sent the world economy into a free fall, triggering the most severe global economic crisis in the past century.

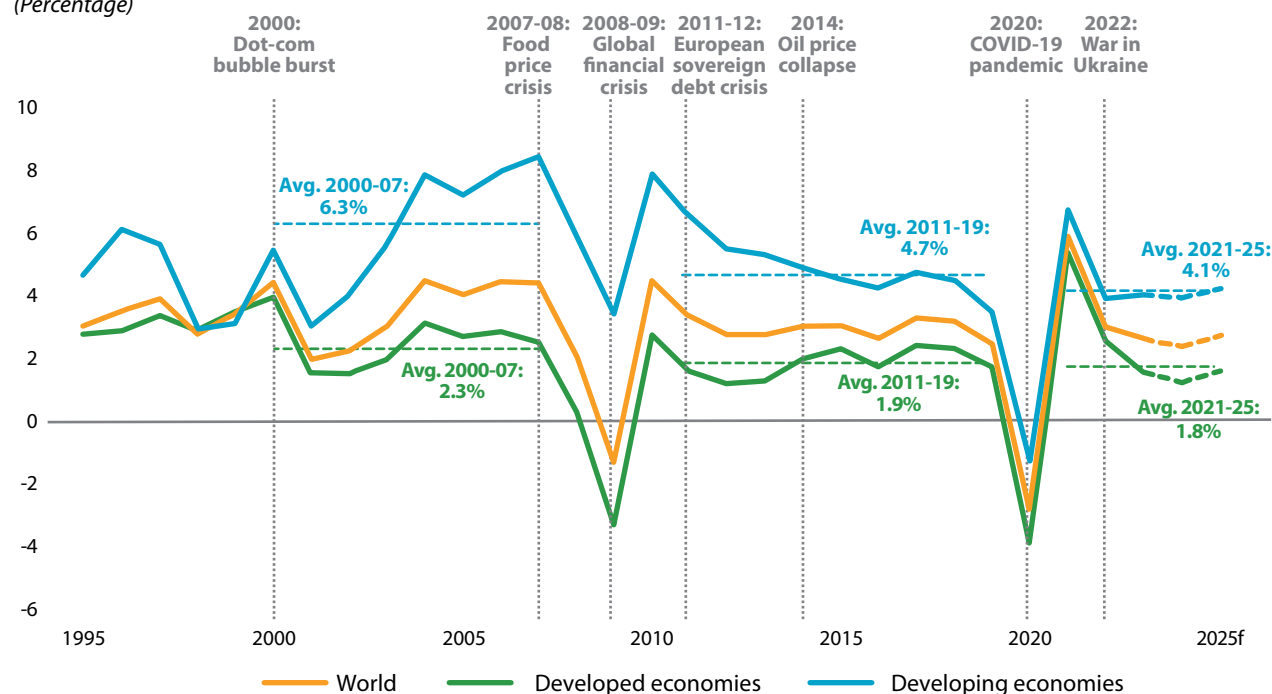
A prolongation of tight financing conditions severely dampens investment prospects. Global interest rates are at four-decade highs in inflation-adjusted terms (see chapter II). In a world awash with debt following a long period of very low global interest rates, this translates into fast-rising debt service burdens for sovereigns, reduced public spending and SDG investments. Already, more than 20 developing countries spend more on debt service than on public investment (see chapter III.E). In the period following the 2008 world financial and economic crisis, developing countries accessed bond markets at high volumes—for the first time in the case of many LDCs and other LICs. While this provided welcome access to new financing, the build-up in commercial debt has left many countries more vulnerable to changing global financing conditions. The dramatic fall in net debt inflows from 2020/21 means that many developing countries are facing an external financing squeeze (bond issuances have mostly seized in LDCs and other low- and lower-middle income countries, though some African countries have recently returned to markets). Under these circumstances, multilateral lending was a critical lifeline (see figure 1.4).

Tight financing conditions impact private investment. Rising interest rates have exacerbated weak investment trends, including contributing to a slump in blended finance deals (see chapter III.C). Higher costs of capital are particularly harmful for investments in the energy transition, with transitions by definition more sensitive to the interest rate environment than the status quo, and capital-intensive renewable energy production more sensitive to higher interest rates. Some estimates suggest that a doubling of the cost of capital from 5 to 10 per cent would raise the final cost of electricity from wind and solar by around 50 per cent, while the cost of gas-fired electricity would rise by only 8 per cent.¹⁷

Persistent inequalities

Inequality has become a central concern of policy debates over the last 25 years. Inequality has risen to the top of political agendas, following growing concerns by populations across the world¹⁸ and due to its corrosive effects on trust in public institutions and on the social contract.¹⁹ The 2030 Agenda for Sustainable Development embodies this prioritization, with SDG 10 and “leave no one behind” as a key cross-cutting principle. These broader trends are mirrored in commitments to address gender inequality. Since the 1995 Beijing Declaration and Platform for Action, normative frameworks—including the 2030 Agenda—have increased attention and commitment to gender equality and the empowerment of women and girls. Many Member States have adopted gender responsive legislation and policies. But insufficient financing for gender equality continues to be a significant barrier to the full implementation of these commitments.

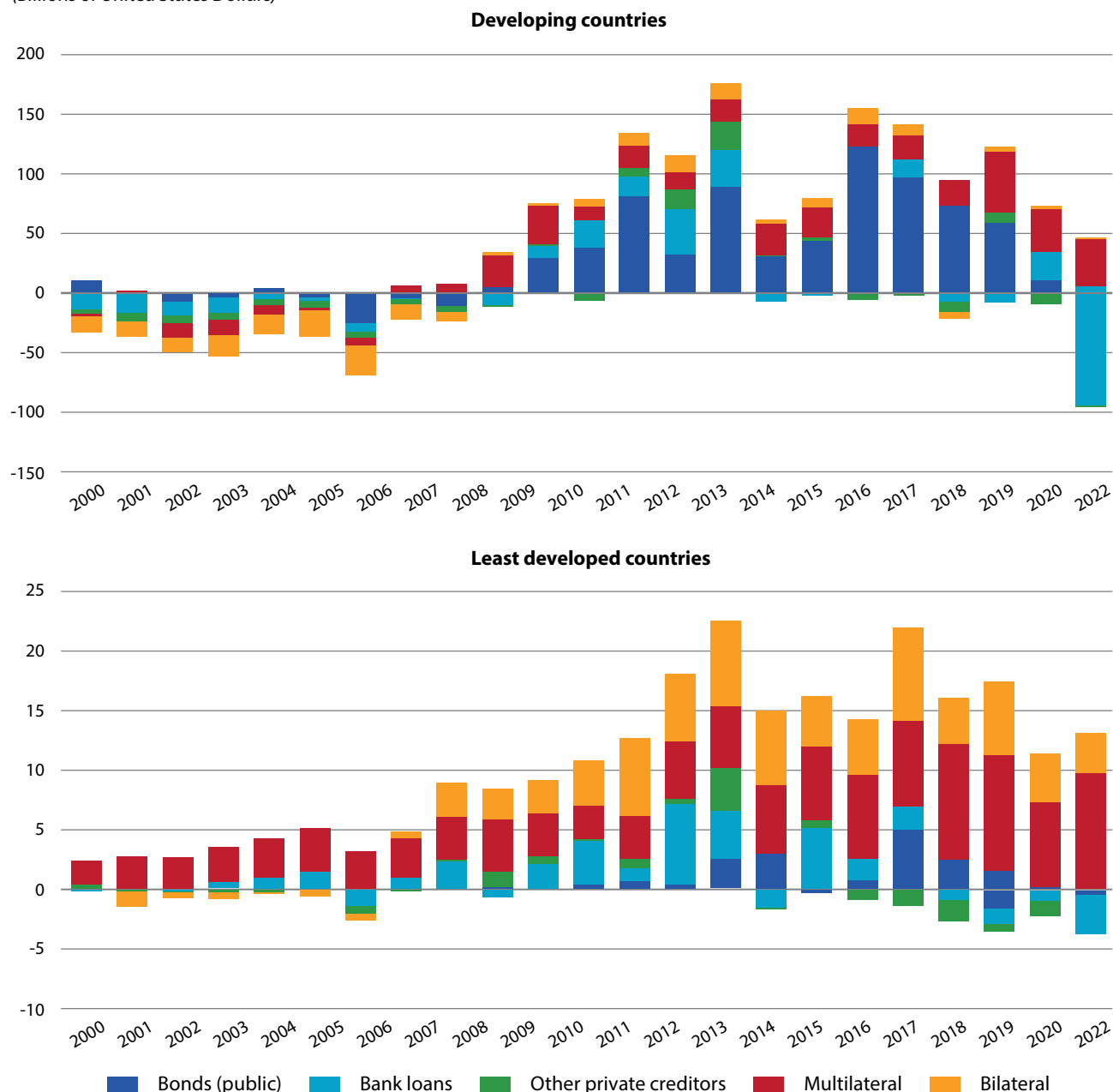
Figure 1.3
GDP growth rates
(Percentage)



Source: UN DESA calculations based on estimates and forecasts produced with the UN DESA World Economic Forecasting Model.

Notes: f=forecasts.

Figure I.4

Net debt transfers to developing countries*(Billions of United States Dollars)*

Source: UN DESA calculations, based on IMF WEO data.

Despite growing attention and corresponding policy commitments, inequalities remain very high. Inequalities are elevated across many dimensions—between and within countries, in income and wealth, and across geographies, opportunity, race, gender and human mobility status. Economic inequalities have increased in many developed and some MICs, with more benign trends in the rest of the world. Data from 114 countries shows that none of the countries have achieved full women’s empowerment or complete gender parity.²⁰ Even in areas with demonstrable

progress, there continue to be challenges and, in some cases, reversals. For example, improved education for girls has done little to shift deeply entrenched occupational segregation. The global gender pay gap persists, with women earning 51 cents to every dollar earned by men.

Development financing is both a significant impediment to mitigating inequality and a key lever to rectify it. Inequalities can undermine the mobilization of development financing through

their detrimental impact on growth and financial stability, or through their undermining of the social contract and more resistance to taxation. Perhaps more importantly, financing policies are crucial tools to overcome inequalities. However, despite commitments to the contrary, financing policies today still often perpetuate inequalities rather than tackle them. Fiscal and tax systems, financial and macroeconomic policies, and trade, investment and technology policies have all come under scrutiny as uneven trends across countries and time reveal that inequality is usually a (financing) policy choice.²¹

Rapid technological change and digitalization

Novel technologies' impacts on economies and societies have been profound and multifaceted over the last 25 years. Technological advances have been an important driver of progress on the SDGs, and they are also the main reason that a narrow path remains to keep global temperature increases below 1.5 degrees Celsius (see chapter III.G). At the same time, the benefits of rapid technological change have not been distributed evenly, neither among nor within countries, as innovation remains highly geographically concentrated and technology diffuses more slowly than in the past.

Digital technologies have impacted all action areas of the Addis Agenda (see the *Financing for Sustainable Development Report 2020*). Digital technologies have been a driver of financial inclusion and improved public governance, but they have also created new risks for financial stability and integrity. They have profoundly impacted the tax landscape and resource mobilization through their transformative effect on production processes and tax administration. And they have reshaped the international division of labour, with digitalization and advanced digital production technologies further "raising the bar" for developing countries. Demands on infrastructure, logistics and connectivity as well as educational and skills requirements are rising, making it more difficult for firms in many countries to compete.²²

Rising geopolitical tensions

In a moment when global challenges abound and global cooperation is more important than ever, growing geopolitical tensions risk undermining the international community's capacity to respond effectively. Geopolitical tensions, violence, conflict and war have contributed to the challenging global macro-environment, present a major downside risk for future growth prospects, and make it more challenging to arrive at effective global policy responses. Tensions have played out across several financing policy areas, including investment, trade and technology policies. Some countries are reducing external dependencies in sectors that are deemed strategically important, such as semiconductors, other high-tech sectors and energy. Trade restrictions imposed for geopolitical and national security purposes have surged since 2020. Some estimates suggest that severe fragmentation of the global trading system could cost up to 7 per cent of global GDP.²³ Current arrangements in the international financial architecture and in international tax cooperation have also not kept pace with changes in the global economy. There is, however, widespread recognition of the need for reform to avoid further geo-economic fragmentation and an erosion of multilateralism and a rules-based order, which would affect vulnerable and the least powerful countries the most.

3.2 Progress in the financing for development action areas within a challenging global context

Notable progress in sustainable finance has been made over the last 25 years, but it has not kept pace with rising financing needs and has come more haltingly, and in some cases was reversed, in an increasingly challenging global environment. Deceleration is an oft-repeated trend in revenue mobilization, private sector dynamics, trade and cross-border investment flows. Commitments have become harder to meet, and long-standing gaps in policy frameworks and the international financial architecture are more pertinent in a period of more frequent shocks and rising systemic risks. In the last several years, this has led to setbacks and even regression, and a widening of SDG financing gaps. Simultaneously, the collective recognition that the world is running out of time on climate action and the SDGs has triggered a new commitment to financing reform.

Public finance and investment

(Action areas A, C, E)

With demands on public financing increasing, many countries today find themselves with large public financing gaps amid tight fiscal constraints. The mobilization and effective use of public financing—domestic resources, international concessional and non-concessional financing and public debt—has been a central focus of efforts. Despite notable progress, particularly early in the millennium, many developing countries today face tight fiscal constraints. Despite rising international support and efforts to mainstream the SDGs in countries' and donors' budget and allocation decisions, more needs to be done to increase support, fully align spending with the SDGs and enhance its effectiveness.

Domestic revenue

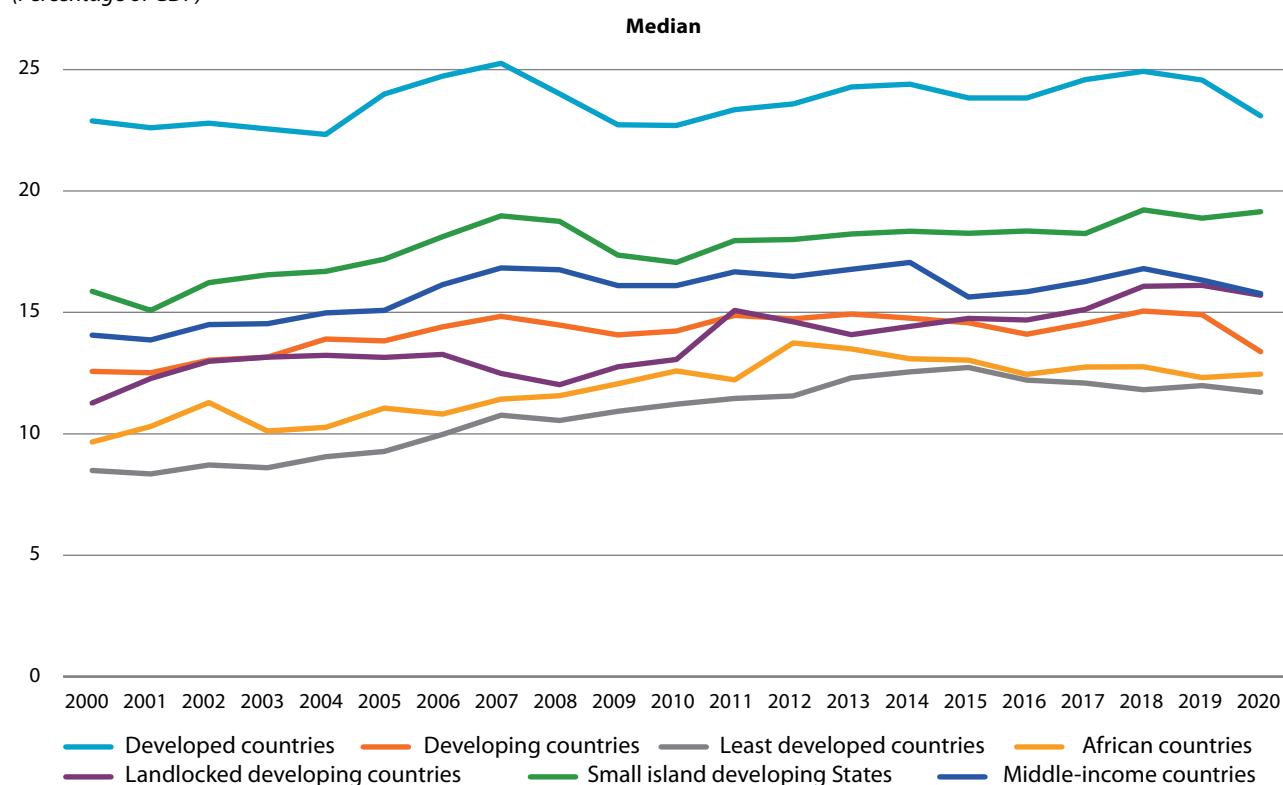
Many developing countries were able to significantly increase tax revenues in the decade before the 2008 world financial and economic crisis. Since then, the record has been more mixed. On the back of a dynamic global economy, two thirds of countries were able to improve tax-to-GDP ratios in the first decade of the millennium, supported by revenue administration and tax policy reforms. However, that dynamism was not sustained; median revenue ratios have been stagnant since then. Only a fraction of countries have seen rapid revenue gains sustained over time; this suggests that expectations for rapid and sustained revenue increases in a large number of countries may be too optimistic. Median tax-to-GDP ratios in developed countries were over 22 per cent before the pandemic but amounted to just 12 per cent in LDCs (figure 1.5). The average finance minister in a developed country mobilizes more than \$17,000 in revenue per every inhabitant to provide public services; in the average LDC, that sum is just above \$100.

Globalization and digitalization have challenged the effectiveness and efficiency of revenue mobilization systems. Greater adoption of digital technologies by revenue administrations has helped to collect revenue and reduce compliance gaps but developing countries have been slower to adopt such technologies. Over the last 20 years, developing countries have been squeezed between their relatively less formalized economies and smaller tax bases, declining tariff revenue due to trade liberalization, and competitive pressures to lower corporate

Figure I.5

Tax revenue, by country groups, 2000–2020

(Percentage of GDP)

**Source:** UN DESA calculations based on IMF World.**Note:** General government tax revenue as a percentage of GDP, M49 geographic groupings.

taxes. In combination with growing public financing needs, efforts to constrain harmful tax competition and combat tax evasion and avoidance have prompted much of the attention paid to advancing international tax cooperation (see below).

International development cooperation

International development cooperation has increased since the adoption of the Monterrey Consensus in 2002 and played a critical role in addressing successive crises, but it has not kept pace with rising demands:

- **Bilateral official development assistance (ODA):** Donors have responded to growing global challenges by increasing ODA, with ODA provided by members of the OECD Development Assistance Committee reaching an all-time high of \$211 billion in 2022, more than double in real terms the level two decades ago. Nonetheless, most donors fall significantly short of the 0.7 per cent of gross national income commitment. A more crisis-prone world has put pressure on concessional financing, with country programmable aid, which excludes donor refugee costs, humanitarian aid, debt relief and administrative costs, declining as a share of total ODA compared to its peak in 2009.
- **Multilateral development bank (MDB) lending:** Lending by MDBs has grown significantly. Annual disbursements increased from \$30 billion in 2000 to \$96 billion in 2022, with MDBs providing vital

countercyclical support during crises, sharply increasing disbursements in 2009 and after the pandemic. Multilateral development banks are in a unique position to accelerate investments in sustainable development, but the size of the paid-in capital bases of MDBs has not increased in line with the global economy's expansion, nor with growing investment needs. Scaling up MDB resources has become a key priority for the international community, and the MDBs have begun to undertake a range of reforms to expand their financial capacity. MDBs are also well placed to improve aid coordination and a key source of concessional financing. But their concessional arms that rely on periodic replenishments have been facing falling donor contributions in real terms. The World Bank's International Development Association remains the primary source of concessional finance for lower-income countries. The upcoming 21st replenishment, under negotiation during 2024, will need to be the largest ever to help meet SDG financing needs.

- **South-South cooperation:** South-South cooperation has evolved substantially over the period and has expanded in scope, volume and geographical reach. It includes a more diverse range of both governmental and non-governmental actors, notably two new South-led development banks.
- **Climate and biodiversity finance:** While climate finance has grown over time, the commitment of “\$100 billion climate finance per annum by 2020” that was agreed by countries at the fifteenth Conference of

the Parties (COP15) and confirmed at COP21 (Paris) is yet to be met. The latest OECD assessment finds that climate finance amounted to \$89.6 billion in 2021, an increase of over 70 per cent compared to 2013. Climate finance mobilized by MDBs, bilateral development agencies and global climate funds plays a catalytic role but remains small relative to total financing requirements and will require more public and private capital mobilization for climate actions. With a proliferation of funds (81 active climate funds as of 2022, of which 62 are multilateral), the climate finance architecture has also become increasingly complex and fragmented. This has not only created monitoring and reporting challenges but has also made coordination and access to finance more difficult for developing countries, especially LDCs and SIDS.

Debt financing

After declining in the 2000s, debt levels increased rapidly in the last decade as a result of debt-financed infrastructure drives and have been a central concern since 2020. In the early years of the millennium, many developing countries benefited from strong growth, and LDCs and other LICs benefited from major debt relief initiatives, leading to a significant easing of debt burdens. Over the past 10 to 15 years, many countries embarked on ambitious, externally financed infrastructure drives, which led to rapid increases in public and external debt. The rapid build-up of debt was enabled in part by new creditors: In a period of exceptionally loose global monetary conditions, many poor countries issued international bonds for the first time; non-Paris Club official creditors also became a major source of debt financing. Recent shocks and rapidly tightening financing conditions have led to a dramatic reversal, with only scaled-up multilateral financing preventing a collapse in external financing.

Rising debt levels, changing creditor composition and tighter financing conditions have culminated in greater debt service burdens and liquidity and solvency risks. Twenty-five developing countries dedicate more than a fifth of their total revenue to servicing public external debt alone, and 3.3 billion people live in countries where governments spend more on interest payments than on education or health. Debt burdens crowd out SDG financing, and they threaten debt crises for more than half of all LDCs and other LICs assessed as either high risk or already in debt distress.

Aligning public expenditure with the SDGs

Efforts to align expenditure more fully with the SDGs and use public resources more efficiently have seen mixed progress. For example, many countries have attempted to align their budgeting practices with gender equality and other SDGs. But while gender responsive budgeting has been increasingly implemented globally, only one in four countries has a comprehensive system to track budget allocations for gender equality. Significant progress has also been made on delivering the human right to social security; most countries today have social protection schemes in place. But large gaps remain—for example social protection schemes are typically only at a nascent stage in LDCs and other LICs. In other areas of expenditure there has been regression in alignment, with fossil fuel subsidies growing over time, reaching \$1.3 trillion globally in explicit subsidies in 2022 when energy prices experienced a dramatic spike.

Development cooperation providers have also taken steps to align their operations with the SDGs, but the development

effectiveness agenda must be revitalized. International development cooperation has changed in multiple ways over the last decade, attributable to a broader set of priorities but also to growing demands on humanitarian aid, more diverse providers and more complex instruments. Actors have responded to these changes, with the MDBs for example taking steps to better align their lending and business practices with the SDGs and climate action. Overall, however, attention to the development effectiveness agenda has been lagging: more aid is untied, but the share of ODA reaching partner countries has plateaued and there has been limited progress on country ownership. There is a clear need to revitalize this agenda and develop a shared understanding of development effectiveness.

Private investment, trade and technology policies

(Action areas B, D, G)

Private sector development, a key driver of sustainable growth and development, has stalled in recent years. As noted in the Addis Agenda, “private business activity, investment and innovation are major drivers of productivity, inclusive economic growth and job creation”. To deliver on these promises, business activity and investment need to be dynamic, inclusive and sustainable. However, private sector dynamism slowed after the 2008 world financial and economic crisis, visible in decelerating investment and trade trends. Many developing countries struggled to diversify their economies, integrate productively into the global economy and absorb and productively use new technologies. Geopolitical fragmentation could further exacerbate these challenges, as barriers to trade, investment and technology diffusion grow.

Investment, trade and technology trends

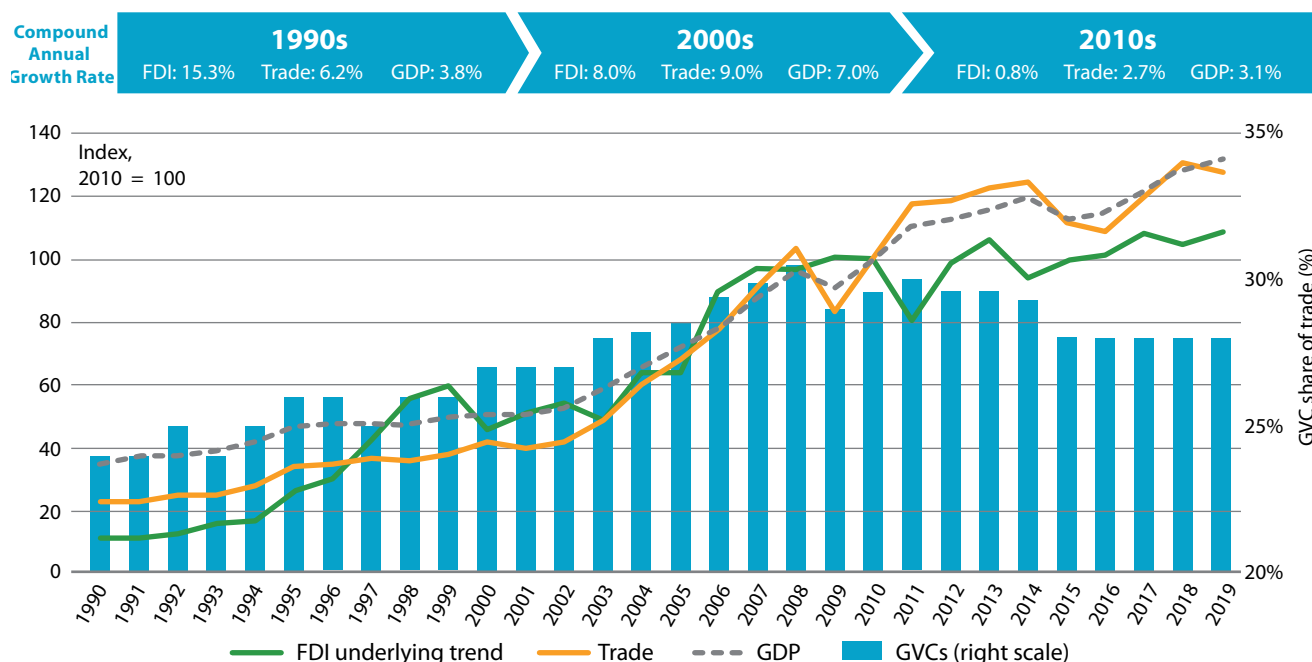
Investment growth has slowed and is expected to remain subdued. The growth of investment has slowed over the past two decades, particularly in developing economies, with gross fixed capital formation after the 2008/09 crisis remaining below earlier levels across regions. This broader trend is mirrored in foreign direct investment (FDI): Following rapid acceleration during the 1990s and 2000s, the past 15 years have seen a slowdown in FDI, along with decelerating trade growth and a stagnation in global value chains (GVCs) (figure 1.6). Investment growth is expected to remain subdued globally, with high borrowing costs and heightened economic and geopolitical uncertainties continuing to weigh on business and consumer confidence.

Trade dynamism has also slowed significantly. World merchandise trade nearly quadrupled in nominal terms over the period from 2000 to 2022. Yet, the pace of trade expansion has been highly uneven. A decade of rapid export growth, driven particularly by developing countries in Asia and the multilateral market opening between 1995 and 2005, was followed by weaker trade dynamism and a decline in trade openness due to a slowdown in the expansion of GVCs, diminishing impacts of technological advances, and a recent rise in strategies prioritizing domestic consumption and domestic supplier bases.

LDCs remain marginalized. Both trade and investment expansions have been driven by fast-growing developing countries but have largely bypassed the poorest countries. LDCs continue to trail behind as recipients of FDI and remain largely marginalized in international trade.

Technological progress has enabled economic integration and SDG progress, but innovative activity remains highly concentrated

Figure I.6
Foreign direct investment and trade trends, 1990 - 2019



Source: UNCTAD.

Note: Trade is global exports of goods and services. GVC share of trade is proxied by foreign value added in exports, based on the UNCTAD-Eora GVC database (see Casella et al., 2019). The underlying FDI trend is an UNCTAD indicator capturing the long-term dynamics of FDI by netting out fluctuations driven by one-off transactions and volatile financial flows.

and technology diffusion has slowed down. Technological advances underpinned rapid trade and investment expansions in the 1990s and 2000s. The impacts of novel technologies, foremost digital technologies, on economies and societies were much broader of course, supporting progress across the SDGs. Meanwhile, the production of new technologies remains highly concentrated—a trend that could become starker still with highly complex frontier technologies like artificial intelligence systems, and technology diffusion has slowed down due to rising complexity and the market power of key actors. Combined with the slowdown in technology diffusion driven by the increasing complexity of technologies, this could lead to further divergence.

The search for new development pathways

These significant structural changes pose new challenges for countries' productive integration into the world economy, necessitating a search for new growth and development strategies.

Private sector development has traditionally been associated with industrialization and diversification. A thriving manufacturing sector has often been at the heart of such transformations. In the context of digitalization and asset-light production models, less trade dynamism and the geographical concentration of manufacturing in several large developing countries, this has become more challenging, with manufacturing less effective as a "development escalator". "Traditional" models of development based on attracting FDI and exports of manufactured goods are increasingly difficult to pursue. Increased fragmentation could further undermine prospects: Rising geopolitical tensions have spurred efforts to de-risk

supply chains, including through so-called friendshoring and nearshoring, and strategic measures to limit technology spillovers.

New growth strategies must be sustainable and inclusive, and policy frameworks adjusted accordingly. There are no ready-made recipes for new private sector development pathways. Manufacturing will remain critical, but labour-absorbing services could play an important role for decent job creation. And they will need to focus on sustainable transitions, with policy frameworks adjusting accordingly. Countries' efforts to create enabling environments for private investment must be aligned with the SDGs: the sequencing and prioritization of public investments; setting the "right" incentives through fiscal and tax policies; ensuring that regulatory frameworks reflect appropriate labour, environmental and health standards; and aligning investment and trade facilitation policies with sustainability. Similarly, selective policies such as industrial policies which had already been resurgent since the 2008 world financial and economic crisis, must be sustainable and inclusive (see the *Financing for Sustainable Development Report 2023*). Identifying country-owned strategies suitable to specific country contexts and aligning financing policies with them will be a key challenge going forward.

Financial sector development: The search for enhanced access, stability and sustainability

(Action areas B, F)

A more dynamic and sustainable business sector relies on more inclusive and sustainable financial markets. Lack of access to affordable finance along with financial incentives misaligned with sustainability are

often among the most binding constraints for sustainable private sector development—and for sustainable development at large. Availability of long-term financing continues to be a challenge, particularly in developing countries. Investors' short-term incentives also often stand in the way of sustainable finance reaching scale, even as interest in sustainable financing and sustainable investing has increased dramatically. Extending investors' time horizons is thus imperative to fully align their incentives with long-term sustainable development so that financial sector stability and sustainability can be mutually reinforcing.

Access to (long-term) finance

Over the past two decades, innovations in public policies and digital finance have driven significant progress in financial inclusion for businesses and individuals alike. Enhancing access to finance for all individuals, including women, has been a success story: global account ownership increased from 51 per cent of households in 2011 to 76 per cent in 2021. In developing countries 567 million adults gained access between 2017 and 2021 alone. Nonetheless, significant challenges remain, especially for women in LDCs and other vulnerable countries, where many remain excluded from financial services. Cost reductions in financial services also fall short of commitments, notably for migrant remittances, which have grown steadily over the past two decades but whose average costs are still more than double the SDG target of 3 per cent of the remittance amount.

At the same time, financial and capital markets remain underdeveloped in many developing countries. Despite efforts to promote long-term finance in domestic markets and an increase in domestic lending to the private sector over the past 20 years, financial market liquidity remains shallow in many developing countries, and long-term credit

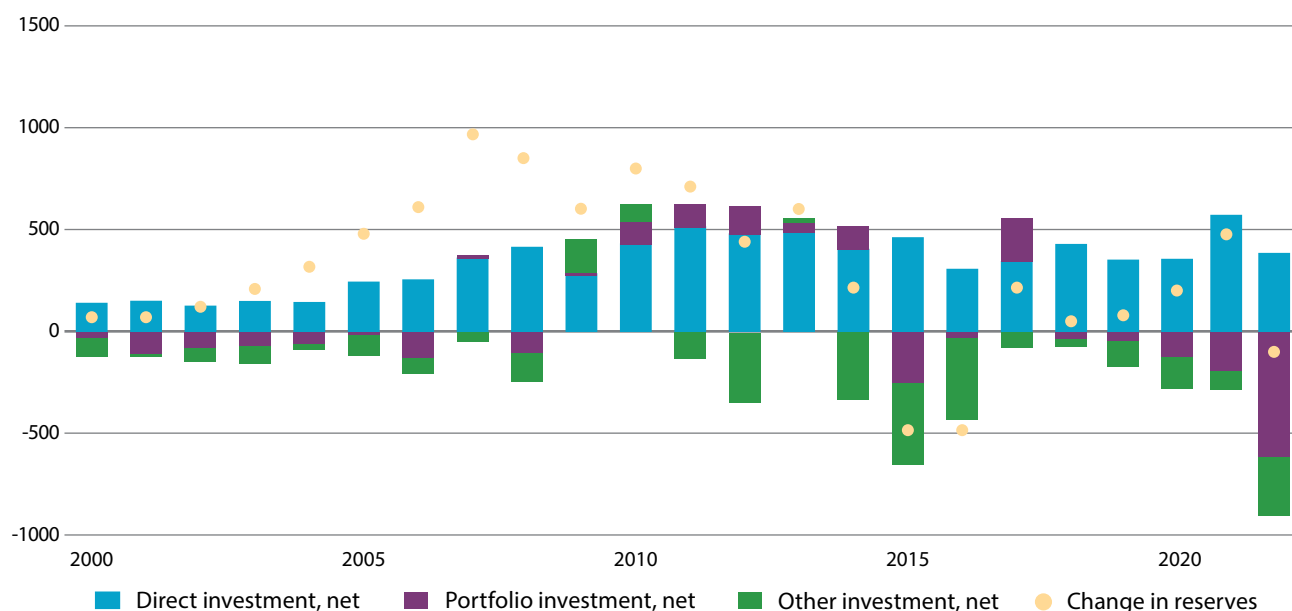
continues to be scarce. This reflects market inefficiencies and institutional gaps—which call for stepped-up efforts to develop domestic financial markets. But it also reflects investors' risk perceptions. The comparatively high costs of capital for project financing in many developing countries are driven more by macroeconomic risk perceptions than by project risk.

Public development banks (PDBs) could play a major role in closing long-term financing gaps. PDBs usually provide longer-term funding than commercial banks, thus lengthening time horizons; plus, their development focus makes the financial durations of their lending better aligned with social and environmental sustainability. Due to their greater appetite and ability to bear perceived high risks and long payback periods, well-governed PDBs can be important financing tools to implement economic and social policies, especially to directly finance large infrastructure projects and, more recently, to address climate change and investments in resilience. PDBs and other development finance institutions can also leverage private investment and foster capital market development, for example through public-private risk sharing and other blended finance instruments.

Financial sector stability and sustainability

Financial volatility has contributed to the dearth of long-term financing. Following the end of the Bretton Woods exchange rate system in the 1970s, the global economy saw financial sector growth, deeper global integration, and increasing complexity in financial instruments and intermediaries and, along with that, growing systemic risks. Financial globalization enabled spillover effects from global financing conditions and macroeconomic policies in major developed countries to affect the exchange rate and financial stability, debt sustainability and access to

Figure I.7
Net financial flows to developing countries, 2000–2022
(Billions of United States dollars)



Source: UN DESA calculations based on IMF data.
Notes: Positive values reflect a financial inflow.

long-term finance in developing countries. This was borne out during crises in 2008/09 and at the onset of the pandemic, which carried ripple effects from market instability. Indeed, developing countries have seen numerous surges and reversals of portfolio capital and other investment flows over the last two decades (figure 1.7). The most recent flight to safety left many developing countries in a very challenging external position and in many cases reliant on official support, with net financial inflows, trade and investment all developing unfavourably.

Recent market turbulence has also rattled the sustainable finance field, although investor interest remains high. Investor interest in sustainable finance has grown steadily since the 1990s, with a net acceleration from 2015. Despite some fluctuations following the COVID-19 pandemic, sustainable fund flows have also largely remained resilient. Global sustainable investing assets amounted to \$30.3 trillion in 2022. Nonetheless, sustainable assets make up only a small fraction of total global assets under management today, and bypass countries most in need. They remain dominated by environmental, social and governance (ESG) integration (which uses ESG factors to better manage financial risks) and negative screening (which excludes sectors such as armaments and tobacco). Impact or thematic investing, which aims to maximize sustainable development impact, represents only a small share. The field also remains hampered by a weak information infrastructure and lack of transparency and accountability, with multiple competing terminologies, standards and frameworks (despite important progress in the streamlining of voluntary standards), and by systemic barriers within the wider financial system.

Successful transitions require financial stability and sustainability. There is growing recognition of the need to adopt a more systemic approach that makes sustainable finance part of a broader set of economic and financial policies that support greater alignment of financial flows with national and international sustainability goals. The drive for sustainable finance is bypassing those who need it the most, with less than 3 per cent of sustainable investments in LDCs and other LICs.²⁴ As long as costs of capital continue to favour traditional investments and do not systematically reflect long-term climate risks, investor interest will not drive sustainable financing at the scale needed, nor will it prevent investments in brown assets. For transformations to succeed, sustainable finance policy must be part of a broader set of economic policies that can align incentives of real economy actors with sustainability.

Aligning policy frameworks and governance

(Cross-cutting)

The financing for development outcomes emphasize the central role of policy, institutions and governance for the mobilization and effective use of financing. These frameworks have come under scrutiny in the last few years both at the national and global level, as a more expansive development agenda and a more challenging macro- and financing context have put existing arrangements under strain.

Progress at the national level: Integrated financing frameworks

Since the adoption of the Addis Agenda, a growing number of countries have adopted integrated financing approaches at the national level, in line with the broader revival of economic planning. The need for transformative change for the SDGs and climate action has fuelled a revival in national planning, but such plans have often not been fully

budgeted and are poorly linked to broader financing policies. A 2019 review of more than 100 national development plans, for example, found that less than 30 per cent explained how they would be financed.²⁵ In response, there has been growing interest in integrated financing approaches, with more than 80 countries now using integrated national financing frameworks (INFFs) to develop national financing strategies and integrate planning and financing policy functions. The concept of INFFs was first introduced in the Addis Agenda, in which Member States noted that “cohesive nationally owned sustainable development strategies, supported by integrated national financing frameworks (INFFs), will be at the heart of our efforts”.

Integrated financing reforms are now under way in many countries (see box 1.1 for country-level examples). Among the main lessons from these pioneering countries is that INFFs need strong political backing and broad-based country ownership. Where such ownership is in place, INFFs hold great potential for the international community to align its efforts with these country-led approaches.

International architecture and global governance

The international financial architecture is in flux with countries in agreement on the need for reform. The fallout from the pandemic and other recent shocks have galvanized calls for the reform and strengthening of the international financial architecture. Efforts are now under way to remake international organizations, norms, rules and frameworks across the action areas of the financing for development outcomes:

- On **international tax cooperation**: Bilateral relationships and agreements were long the dominant form of international tax cooperation, but this has changed in recent years; several multilateral legal agreements have been concluded since 2009, including on transparency and exchange of information. Nonetheless, attempts to address the challenges from globalization and digitalization have yet to yield an agreement that sufficiently addresses tax avoidance and evasion—and has full support from all Member States. Concerns also remain about the inclusiveness and effectiveness of existing international tax cooperation mechanisms.
- On **investment and trade**, the complex set of existing agreements has led to calls for reforms to enhance coherence between trade, investment and sustainable development. This includes calls for World Trade Organization (WTO) reform, with a focus on dispute settlement, updating rules to reflect global economic changes, and reinvigorating multilateral negotiating functions; and continued efforts to update investment treaties, with modern agreements now often including a sustainable development orientation, a focus on preservation of regulatory space, and improvements to or omissions of investor-State dispute settlement mechanisms.
- On **development cooperation**, reforms of the MDBs are under way with a focus on scale, quality of lending and development impact (see above). From an architecture perspective, growing systemic risks and more frequent and severe hazards have increased the urgency of incorporating vulnerabilities into access to concessional finance across providers—key dimensions of sustainable development (or lack thereof) are currently not sufficiently considered in the international financial architecture. Efforts to move beyond GDP have gathered steam, including measures of vulnerability, and could help to further complement income-based criteria in the allocation of concessional finance.

Box 1.1

Financing policy reforms in the context of INFFs

Mongolia is advancing reforms through its integrated national financing strategy. On the public finance side, reforms to align the budget with the SDGs are expanding, now covering more than \$900 million of annual expenditure. The Mongolian Development Bank has adopted a sustainability risk management framework and the National Audit Office has adopted SDG performance audits. An SDG finance taxonomy for private investment was launched in 2023 and sustainability reporting standards have been adopted by the Stock Exchange for compliance by over 200 companies with a market capitalization of \$3 billion.

In the Maldives, the gender-responsive climate financing strategy^a is advancing 16 financing policy objectives pivotal to the transition from a fossil fuel-based economy to a low carbon development path.^a A Sustainable Finance Hub set up by the Ministry of Finance coordinates

financing across government for the country's national development plan and its nationally determined contribution. In Nigeria, the financing strategy^b has catalysed federal innovations in areas such as investment promotion and tax in the artisanal and small-scale mining sector, with a number of states also exploring how to use the INFF approach. In Uzbekistan, SDG budgeting reforms have seen a \$4 billion increase in SDG-aligned expenditure alongside a \$1 billion reduction in harmful expenditure; in Sierra Leone, pilots to digitalize local tax administration have yielded over \$300 million in additional revenue; and in Cabo Verde, the Blu-X platform launched under the INFF has hosted issuances totalling more than \$40 million to advance the economic transition towards a blue economy.

Source: INFF Facility.

^a Accessible at: <https://www.finance.gov.mv/public/attachments/lzyzHlHy0ZWB7Yl17aw16YkFhE5o8DfVxThmru0.pdf>

^b Accessible at: <https://inff.org/resource/nigeria-integrated-national-financing-framework>

- On **debt**, the restructuring of sovereign debt has highlighted deficiencies in the rules-based international financial system, with the system relying on contractual approaches to restructure private debt and informal negotiation processes for bilateral debt. The Group of Twenty (G20) Common Framework represents an advance in this architecture, but many challenges remain and further improvements are critical to speed up the resolution of ongoing restructurings, find more effective tools in case of a widespread systemic debt crisis, and to better address the development dimension of current debt challenges.
- On **systemic issues**, the global financial safety net, with the IMF at its centre, has come under enormous strain in recent years, revealing both gaps in the architecture and uneven coverage. Developed countries are best served by the safety net as they can rely on the unlimited bilateral swap network among the reserve currency-issuer countries. Most developing countries rely only on their own reserves and limited IMF resources and have been the main users of the 2021 SDR allocation.
- On **global governance**, despite repeated commitments to increase the voice and representation of developing countries, significant reforms to institutional arrangements have so far not been agreed, and the pace and scale of change, where it has happened, has left many countries dissatisfied.

Ongoing reform processes hold the potential to deliver a more coherent and effective international architecture, and the Fourth International Conference on Financing for Development is a key opportunity to adopt a coherent package of reforms. Discussions and institutional reform processes have the potential to close some gaps in the international architecture, align it better with the needs of the twenty-first century, and scale up financing for the SDGs and climate action. However, if they proceed in piecemeal fashion and fail to take the SDGs fully into account, the architecture will remain fragmented and inadequate to deliver sustainable development. Failure to deliver real reform could risk undermining faith in multilateralism itself. The financing for development process at the United Nations provides an opportunity to bring these different strands together.

4. Conclusion

This report of the Inter-agency Task Force on Financing for Development puts forward key questions and challenges that Member States may wish to address at the Fourth International Conference on Financing for Development. All five major institutional stakeholders of the financing for development process, the IMF, the World Bank, WTO, the United Nations Conference on Trade and Development (UNCTAD) and the United Nations Development Programme (UNDP) as well as the United Nations Department of Economic and Social Affairs (UN DESA), are also sharing their respective institutional perspectives and expectations for the Fourth International Conference on Financing for Development, in attributed contributions (see section 5 below).

The subsequent chapters of this ninth report of the Inter-agency Task Force lay out the global macroeconomic context (chapter II); and review progress and challenges across the seven action areas of the Addis Agenda, and with regard to data (chapters III.A to III.G and IV). In response to the mandate received at the ECOSOC Forum on Financing for Development Follow-up 2023, to assess “*progress made in the implementation of the Monterrey Consensus of the International Conference on Financing for Development, the Doha Declaration on Financing for Development and the Addis Ababa Action Agenda, identifying obstacles and constraints encountered in the achievement of the goals and objectives agreed therein, with a view to informing an inclusive informal dialogue on all issues related to a potential fourth international conference on financing for development*”²⁶ the chapters expand the time horizon of analysis, looking back to 2000, and put forward recommendations on questions and challenges that Member States could address at the Fourth International Conference on Financing for Development.

The Inter-agency Task Force is made up of more than 60 United Nations agencies, programmes and offices, the regional economic commissions and other relevant international institutions. The report draws on their combined expertise, analysis and data. The major institutional stakeholders of the financing for development process play a central role, jointly with the Financing for Sustainable Development Office of UN DESA, which also serves as the coordinator of the Task Force and substantive editor of the report.



5. Perspectives on the Fourth International Conference on Financing for Development



The road to the Fourth International Conference on Financing for Development: Delivering an investment push for the Sustainable Development Goals

Li Junhua, Under-Secretary-General for Economic and Social Affairs

The 2030 Agenda is in trouble. Last year, as we hit the halfway mark for achieving the Sustainable Development Goals (SDGs), the data told a sobering tale. With just 15 per cent of assessable targets on track, on current trajectories, we would be unlikely to achieve our global goals by mid-century, let alone six years from today. But as world leaders came together to reflect on this reality at the SDG Summit the tone was hopeful. Member States reaffirmed the SDGs and committed to act with urgency to realize the vision of the 2030 Agenda. They responded to the call of the Secretary-General to rescue the SDGs, committing to “bold, ambitious, accelerated, just and transformative actions”.

But delivering on this rescue plan will require urgent action that turns these commitments into transformative policies and practices. This means budget allocations, investment plans, domestic financing policy and international financial architecture reform that align with our global sustainable development goals. Financing is where rhetoric has to translate into real action.

The Fourth International Conference on Financing for Development in June 2025 provides a unique opportunity to do just that. It is a chance to adopt an ambitious package of reforms across the action areas of the financing for development outcomes, and to deliver an investment push for the SDGs.

So how do we use the next 15 months to make this a reality?

Today, we have a broad consensus on the need for reform in each of the financing policy areas. The series of crises and shocks since 2020 and the development setbacks they caused also triggered a tremendous amount of creative policy work on options for reform. Academics, think tanks, national governments, members of the Inter-agency Task Force and many other stakeholders have tabled ambitious proposals that have been discussed in the United Nations and beyond. But in most cases, they still await adoption, with both technical and political hurdles to clear.

In preparation for the Conference, my department will bring ideas to intergovernmental discussions that are both ambitious enough to change the unsustainable status quo, but that could also find consensus as part of a broader package that meets this moment – a moment that we all agree requires transformative change.

To this end, UN DESA will bring together relevant work ongoing in the United Nations and beyond, and where needed, organize dedicated workstreams. Below are some examples of our focus of work ahead of June 2025:

Domestic public resources

- First, UN DESA supports the historic negotiations on a United Nations Framework Convention on International Tax Cooperation. These discussions will unfold in parallel to the preparatory process for the Conference but are undoubtedly part of the broader effort to reform and make fit for purpose the international financial architecture that the Conference will aim to achieve.
- A second priority is to further strengthen the role of public development banks, a key vehicle to finance transformation. Public development banks were recognized in the Addis Agenda, but their importance is more widely accepted today, and as we undergo a broader rethink of our development models and pathways and the role of public institutions in steering them. We will work with the Finance in Common Coalition (FICS) of more than 500 public development banks to bring these institutions and their expertise to the United Nations discussions.

Private business and finance

- A first priority will be to rethink blended finance and to “get it right” this time. There was tremendous hope, in 2015, that blending would help to mobilize trillions of dollars. These hopes were not met. At the same time, with the revival of industrial policies, there is a renewed emphasis on using public policy and public financing instruments to incentivize and sometimes subsidize private investment, for example in energy transitions. The Conference is our chance to better connect these discussions: to ensure that blended finance supports national priorities and to focus blending instruments on development outcomes rather than quantities

leveraged. This should also help to mobilize more investment for vulnerable countries such as the least developed countries, which may require additional and dedicated support mechanisms for investment.

- Second, the Conference is an opportunity to address the remaining challenges in the field of sustainable finance, and to identify and commit to complementary policy to achieve broader systemic change. This includes harmonization of sustainable finance legislation while recognizing the different conditions and needs of countries, adoption of mandatory national disclosure standards with a double materiality vision, and a broader set of macroeconomic and financial sector policies that create enabling conditions for the financial sector to contribute to sustainable transformations.

International development cooperation

- The Fourth International Conference on Financing for Development must reaffirm existing official development assistance commitments and further support reform discussions at the multinational development banks, with a view to support ambitious outcomes.
- The Conference will also be well placed to help us consider how we can scale up financing for global public goods, additional to scarce development financing that is urgently needed in developing countries, what innovative instruments we could put in place to mobilize such financing, and how we can transparently account for it.
- The dramatic changes in the development cooperation landscape also call on us to revitalize the development effectiveness agenda, ensuring that all providers support country-owned plans and financing strategies.

Trade and technology

- We will seek to explore, with all stakeholders, how the Conference can give a positive impetus to related discussions in other decision-making bodies. Benign trade, investment and technology environments are central to progressing on financing for development; risks of divergence and fragmentation of the global economy loom large.
- The Conference will take place against this backdrop; its preparations may help to clarify what trade, investment and technology reforms developing countries, especially commodity-dependent countries, will need to be able to finance and achieve ambitious transformations, and what priorities negotiations in related decision-making bodies should pursue in the years ahead.

Debt and systemic issues

- For the Fourth International Conference on Financing for Development to be successful, it will have to offer a response to the urgent debt challenges that are currently engulfing the developing world. With so many countries severely constrained in their SDG investments due to extremely high debt service burdens, we must find ways to provide additional fiscal space for countries that may not be insolvent, but that have big liquidity challenges over the next few years, a period absolutely critical for the SDGs.
- We must also and finally meet the long-standing commitment to build a debt resolution architecture that is both effective and fair.
- The Fourth Conference on Financing for Development can also be a place to increase the ambition on governance reform, and to meaningfully increase the voice and representation of developing countries in international economic and financial governance – a long-standing commitment of the financing for development outcomes.



Domestic resources remain the bedrock of country-led efforts for sustainable development

Kristalina Georgieva, Managing Director, International Monetary Fund

The Fourth International Conference on Financing for Development comes at a time when mobilization of the international community to support the Sustainable Development Goals (SDGs) is more crucial than ever. The world is growing more shock-prone and threatened by fragmentation. Growth in low-income countries remains weak, holding back the path of income convergence. Recent shocks have led to reversals in poverty reduction, inequalities have worsened, gender gaps may never close, and high debt and a

liquidity squeeze are limiting policy space for many countries to reverse these and other worrying trends.

For its part, the IMF has mobilized all available capabilities and resources to support developing countries through these challenging times. By adapting its lending toolkit, the IMF has provided over \$350 billion in assistance to nearly 100 countries since 2020 and, in 2021, it made an historic allocation of Special Drawing Rights amounting to \$650 billion. The IMF also provided an unprecedented level of concessional support to low-income countries through the Poverty Reduction and Growth Trust (PRGT). Moreover, the IMF recently concluded the 16th General Review of Quotas approving members' 50 per cent quota increase, reinforcing the IMF's role at the center of the Global Financial Safety Net.

Still, much more must be done, and the Fourth International Conference on Financing for Development provides an opportunity to take decisive action to accelerate our efforts to achieve the SDGs. I would like to highlight the following priority action areas:

First, the Conference will send a strong signal that countries need to take decisive measures to support strong **domestic reforms** to unlock stronger and more inclusive growth, ensure strengthened and sustainable revenue mobilization and improve governance and transparency. Domestic resources remain the bedrock of country-led efforts for sustainable development, and macroeconomic buffers must be restored after the recent global shocks of conflict and pandemic, to foster long-term resilience.

- Recent IMF research indicates that many developing countries could increase their tax-to-GDP ratio by up to 9 per cent of their GDP through a combination of tax revenue reform and institutional capacity-building. More efforts are also needed to cut non-priority spending and redirect financing towards health, education, well-targeted social safety nets and growth-enhancing public investments.
- Economically empowering women promotes inclusive growth and stability and, as such, should be a key part of the solution to the weakest medium-term global growth outlook in decades. Emerging and developing economies (EMDEs) could boost GDP by about 8 per cent over the next few years by raising the rate of female labour force participation by 6 percentage points.

Second, the Conference will send a strong signal supporting global innovation and coordination on **financing for sustainable development** among all development partners as a complement to countries' own efforts. Such a response must encompass policy advice, capacity development and adequate levels of financial support, including from international financial institutions. And, where needed, action on debt, including through further improvements in the **Common Framework** to ensure solvency and liquidity issues can be resolved in a timely and effective manner, is needed.

- All relevant international organizations and institutions, including international financial institutions, must adapt and innovate to meet the evolving needs of countries, including through deepening cooperation to meet global challenges while fulfilling each institution's mandate. This is especially true when increasing global fragility and shocks are not evenly distributed.
- Deepening domestic financial markets will also be needed. While still small in absolute size, the share of domestic debt in many low-income developing countries has been increasing over the past decade, helping to mitigate external debt vulnerabilities.
- Debt restructuring processes should be further improved to ensure timeliness, efficiency and predictability, and to provide stock or liquidity debt relief where it is needed.

Third, the Conference will also focus on risks to macroeconomic and financial stability stemming from **climate change**. Achieving the transition to net-zero emissions to mitigate and adapt to such risks requires substantial climate investment and therefore the Conference could focus on actionable solutions to scale up climate financing, in line with the 2023 United Nations Climate Change Conference (COP28) priorities.

- Well-designed **carbon pricing** in the form of a tax or emissions trading scheme (ETS) is a fair, proven and cost-efficient solution. While its domestic price impact on poor households can be covered with a modest share of the resulting revenue, carbon pricing can help to address equity issues by adding to climate finance for developing countries.
- Financial sector policies should be refocused towards creating climate impact (i.e. not only identifying activities that are already "green") while considering the specific requirements of EMDEs. Transition taxonomies in EMDEs can help to identify activities,

underlying technologies and industrial processes that have the potential for substantial reduction in greenhouse gas emissions, including in the most carbon-intensive sectors.

- And by designing climate financing and mitigation and adaptation strategies in a gender-responsive manner, we can help ensure that women and girls are part of the solution.

Finally, **artificial intelligence** (AI) will transform the global economy, affecting almost 40 per cent of jobs around the world. The profound impacts could be comparable to the Industrial Revolution. To help countries craft the right policies, the IMF recently developed an **AI Preparedness Index** measuring readiness in digital infrastructure, human capital and labour-market policies, innovation and economic integration, and regulation/ethics in 125 countries, which revealed considerable variation across countries.

- EMDEs face fewer immediate disruptions from AI. At the same time, many of these countries don't have the infrastructure or skilled workforces to harness AI for sustainable development, raising the risk that over time the technology could worsen both gender and income inequality among nations.
- Advanced economies must prioritize AI innovation and integration while developing robust regulatory frameworks to optimize benefits. For EMDEs, the priority must be laying a strong foundation through investments in digital public infrastructure and a digitally competent workforce.



Building coalitions to close the financing gap

World Bank Group

The world is at an inflection point, facing a multitude of intertwined challenges: declining progress in the fight against poverty, an existential climate crisis, food insecurity, fragility, conflicts, and more. This perfect storm is reversing development gains and exacerbating inequality.

The Fourth International Conference on Financing for Development offers an opportunity for us as a global community to come together and create a strong coalition that can deliver the kind of impact the world so desperately needs. Because the only way we can do this is together—multilateral development banks, the private sector, governments, and philanthropists all have a role to play.

At the World Bank Group, we have adopted a new vision—to *create a world free of poverty on a livable planet*. It widens the aperture of the 80-year-old institution to confront today's intertwined challenges aggressively, simultaneously, and comprehensively.

That new vision is just the beginning. We are changing the way we do business, working to become a better Bank.

We are stretching every dollar, while preserving the World Bank's AAA credit rating. This rating gives us access to low-cost funding from bond markets and allows us to lend to developing countries with little or no interest. This and other steps we're taking will help us maximize the impact of every dollar that comes in the door.

Those steps include adjusting our loan-to-equity ratio to free up \$40 billion over the next 10 years, a portfolio guarantee mechanism for risk sharing, a hybrid capital instrument that allows resources to flow in quickly and finding new ways to leverage callable capital.

We're also creating a Livable Planet Fund by opening the Global Public Goods Fund to governments and philanthropies, increasing its ambition, and further incentivizing cooperation across borders.

Taken together, these measures could potentially deliver more than \$150 billion in financing over the coming decade.

But we know we can't do this alone. We are stepping up our partnerships—including with other multilateral development banks—to expand joint financing, standardize processes, track climate outcomes, and to work together with the credit rating agencies to improve their understanding of our work and risks.

And despite all these efforts, we know there still won't be enough money to meet the world's demands. We need the scale, resources, and ingenuity of the private sector.

The Private Sector Innovation Lab we launched last year engages top corporate leaders to identify barriers and solutions to private sector investment. They already have honed in on four areas of focus: regulatory certainty, political risk insurance, foreign exchange risks, and an originate-to-distribute model, and are working on all.

That work has led us to deliver a major change to our political risk insurance platform, an essential step that will allow us to triple our guarantees by 2030 to more than \$20 billion annually. We're also consolidating all our guarantee products into a one-stop shop to make them easier to access and faster to execute.

To overcome another key constraint to private investment in developing economies, we are working with the Global Emerging Markets Risk Database (GEMs) consortium of 25 multilateral development banks and development finance institutions to publish—for the first time—critical statistics on the credit risk profile of investment in emerging markets. The goal: getting more private sector capital into developing economies to drive impact and create jobs.

Another source of potential development funding is the more than \$1 trillion a year currently spent on subsidies for fossil fuels, agriculture, and fisheries, most of which have been proven to be environmentally damaging. While some of these are needed, most come with economic costs estimated at \$6 trillion a year. Instead, these funds should be repurposed to incentivize sustainable practices.

We are also working on developing sound, voluntary carbon markets and ensuring their integrity. These would be an excellent means of transferring resources at scale from the developed world to the developing world. With better policies, the right regulations and improved domestic resource mobilization, we can achieve much more and spend less.

We can't deliver on our goals without our International Development Association (IDA)—the world's largest source of development finance for emerging and developing countries. IDA can access capital markets to turn every \$1 in contributions into \$4 for our clients. Its concessional and grant financing is the most efficient way to deliver development assistance to the countries most in need.

IDA is replenished every three years, and this year's replenishment is a critical priority for the World Bank Group.

Our ongoing work to become a better World Bank Group will benefit all IDA clients through a sharper focus on speed, quality, replicability, scalability, and impact. We have undertaken an important initiative to simplify IDA's policy and financial architecture, putting more focus on supporting clients' implementation and results and, more importantly, making IDA funding more accessible for those who need it.

Confronting a world in crisis demands partnership. Let's make this conference the beginning of our shared drive to address these challenges and improve lives.



Navigating global challenges: the WTO's outlook on the Fourth International Conference on Financing for Development in 2025

Dr. Ngozi Okonjo-Iweala, Director-General, World Trade Organization

As the global community gears up for the fourth international conference on financing for development in 2025, the WTO envisions a transformative event that mobilizes financial resources at speed and scale and leverages the full spectrum of complementary policy tools to deliver sustainable economic growth and development for people around the world.

With only five years to reach the Sustainable Development Goals, anticipation surrounding the conference is palpable, particularly in light of the setback dealt to the pursuit of the SDGs by the COVID-19 pandemic and the wider polycrisis of international conflict, environmental strains, debt distress, and other challenges to future growth and stability.

Trade is both a means to achieve development and climate goals and a force multiplier for sustainable development financing writ large. Trade policy choices shape the extent to which we can capitalize on these benefits. Bringing more countries and communities from the margins of global trade to the mainstream—what we at the WTO are calling ‘re-globalization’—is crucial for making the global economy more prosperous, equitable, and inclusive, in line with the spirit of the 2030 Agenda. Moreover, trade diversification and access to global markets are important factors in building resilience, by enhancing developing countries’ capacity to withstand economic shocks and other climate-related vulnerabilities. Open and predictable international trading conditions are a prerequisite for re-globalization.

Our hope is that FfD4 will serve as a venue for fostering a renewed commitment to international cooperation, with concrete actions and pragmatic solutions. The SDG funding gap is substantial: estimates by both UNCTAD and the OECD suggest that developing countries will need an additional \$4 trillion in financing to meet sustainable investment needs by 2030. Yet as the OECD notes, this amount is equivalent to less than 1% of total global finance. In many developing countries, the high cost of capital—far higher than in richer economies—is holding back investments that would accelerate both growth and the low-carbon transition.

FfD4 needs to deliver substantially increased resource mobilization and expand the envelope of low-cost finance, from the public and private sectors, together with innovative mechanisms including blended finance, special drawing rights, voluntary carbon markets, philanthropy, and guarantees.

To enhance the developmental returns on these enhanced flows of investment, we need greater policy coherence to ensure that trade and regulatory policies are pulling in the same direction. For instance, green investment needs to be complemented with supportive trade policy: in most countries, no matter how much financing is made available for renewable electricity generation, it will not go very far if they are unable to import green technologies. We saw the importance of such non-financial constraints with vaccine access during the pandemic: the availability of funds was not the problem. Trade restrictions and other regulatory barriers were.

Subsidy policy offers another point of intersection between the trade and finance agendas. Trade policy reforms can free up resources that governments currently devote to subsidising a wide range of different activities—often with environmentally harmful, distributionally lopsided, and market-distorting effects—so that they can be repurposed towards achieving the SDGs. The amounts concerned are substantial. The OECD estimates that between 2020 and 2022, governments provided \$630 billion each year in support to agricultural producers. The IMF estimates that explicit subsidies to fossil fuels were worth over \$1.2 trillion in 2022—with vastly more in implicit subsidies if we factor in environmental costs that are not reflected in prices. Water and sanitation subsidies amount to approximately \$300 billion annually in the developing world, typically favouring the well-off and corporations more than the poor. The WTO’s 2022 Agreement on Fisheries Subsidies, which once it enters into force will curb the roughly \$22 billion in annual spending on harmful fisheries subsidies, illustrates how trade reform can help shift resources to better purposes.

One of the foremost challenges on the FfD4 agenda will be the persistence of income inequality within and among nations. Bridging this divide is essential to ensure that the benefits of economic growth are distributed more equitably, in line with the SDG focus on equitable growth. On the trade front, bringing small businesses and marginalized economies into cross-border production networks for goods and services would help boost incomes and jobs for people and places that urgently need them. There is also the pressing need to address inequitable access to finance, with major existing disparities in investment flows and access to credit, particularly for LDCs, LLDCs and SIDS and other vulnerable countries, as well as for SMEs and women.

Geopolitical fragmentation and decoupling pose threats to the stability of the global economy and the growth prospects of poor countries. WTO economists estimate that if the world economy fragments into two self-contained trading blocs, it would lower the long-run level of real global GDP by at least 5%. Developed economies would experience an average 4% reduction in real output—worse than what they sustained after the 2008–09 financial crisis. Low-income economies would miss out most from the loss of technology spillovers that come with open trade: least developed countries are looking at a 6.5% reduction in real GDP—a harsh blow to economic progress. These costs underscore the urgency of fostering dialogue and cooperation on trade.

In addition, the mounting environmental crisis, with climate change disrupting ecosystems, impacting economies and jeopardizing the well-being of communities worldwide, also threatens to roll back years of economic progress. Members must confront those new economic and macro-critical challenges head-on, integrating climate action into their development strategies—and making full use of trade to drive climate mitigation and adaptation.

We should view FfD4 as a major opportunity to forge inclusive partnerships and generate collaborative financing mechanisms, leveraging the strengths of both the public and private sectors.

There is an important agenda for financing that will help countries and businesses participate more effectively in the global economy: support for unleashing the potential of digital technologies to enhance financial inclusion and accessibility; for closing what the Asian Development Bank estimates to be a \$2.5 trillion gap between the demand for trade finance and its availability in emerging markets and developing economies; and for addressing the supply side weaknesses that keep many countries and communities on the margins of the global division of labour. The conference should explore ways to leverage digital platforms to connect previously underserved populations to financial services, so as to empower marginalized communities and stimulate economic growth.

Finally, the urgency of addressing climate change necessitates a dramatic shift towards green and blue finance and sustainable investments—as well as coordinated approaches to carbon pricing. The conference is an opportunity to better align financial incentives with ecological responsibility to drive a global transition towards a low-carbon and resilient economy.

To maximize its impact, the FfD4 conference should prioritize these five key areas as deliverables:

1. **Enhance policy coherence for development:** Achieving sustainable development requires policy coherence across various sectors, with finance working in tandem with trade, health, environmental and other policies. The conference should call for reforms in this direction.
2. **Build momentum on subsidy reform and repurposing:** The conference will be also a logical venue for a serious discussion on how to address and repurpose environmentally harmful and market-distorting subsidies.
3. **Develop a roadmap for reform of the international financial architecture:** The international financial architecture must be reformed to address the evolving needs of the global economy, notably to respond more effectively to the current wave of debt distress, so that development initiatives are not undermined by financial instability.
4. **Unlock private sector investment:** The conference should seek outcomes which will help create environments conducive to attracting private capital in support of development goals. Implementing policies that inspire confidence and reduce investment risks can encourage increased private sector participation in sustainable development projects.
5. **Strengthen trade finance and financial support for sustainable trade policies:** Inadequate access to trade finance in emerging markets and developing economies prevents otherwise-viable transactions from going forward—with disproportionate impacts on small and women-owned businesses. Research by the WTO and IFC suggests that in regions like West Africa and the Mekong region of Southeast Asia, only 25% of trade is supported by trade finance—and that increasing coverage to 40% would boost trade flows by an average of 8% per year. Increased financial support for MSMEs engaged in sustainable trade practices would catalyse economic growth while advancing environmental sustainability.

Like so many of the biggest challenges confronting people and countries today, international cooperation and a sense of shared responsibility will be critical both to re-globalize successfully and to mobilize and catalyse the financial resources needed to meet the 2030 agenda. The fourth international conference on financing for development represents a crucial moment for governments to reaffirm their commitment to international cooperation, and shape policies that foster inclusive and sustainable development for the benefit of all.



Is the Fourth International Conference on Financing for Development up to the net resource transfer problem?

Rebeca Grynspan, Secretary-General, UNCTAD

Nine years after the Third International Conference on Financing for Development, its objective of establishing a revitalized global partnership to meet the 2030 Agenda remains unfulfilled. The Sustainable Development Goal (SDG) reckoning shows that half the world is being left behind, with only 15 per cent of the SDGs likely to be met. Meanwhile, developing countries face escalating economic, social and environmental challenges that hinder their ability to scale up investment to the levels required to achieve

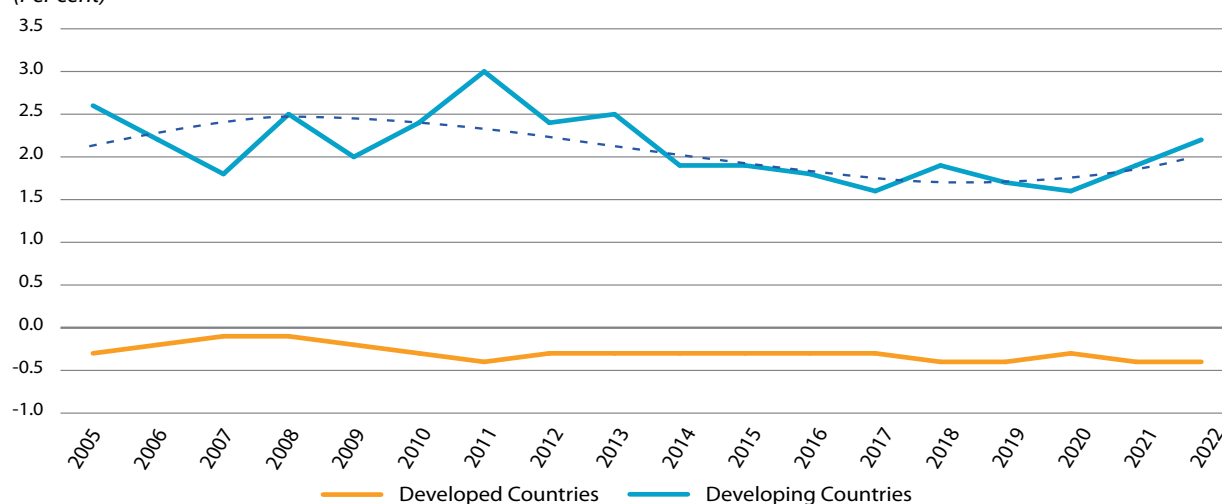
the SDGs. UNCTAD estimates that the gap in annual investment required to deliver the SDGs is \$4 trillion per year, 60 per cent greater than in 2014.^a

Closing the gap requires not just domestic resource mobilization but improved access (both in quantum and terms) to global financial flows. The persistent current account deficits of most developing countries are a key driver of their negative external investment positions. Such deficits require financing by inflows of foreign capital, giving rise to external liabilities (stocks of foreign direct investment, portfolio investment and debt). Two simultaneous processes after the 2008 world financial and economic crisis have underpinned this trend: the deepening of the financial integration of emerging market economies, associated with the opening of their domestic financial markets to foreign investors and liberalization of foreign direct investment regimes;^b and the integration of many lower-middle-income and low-income countries into international capital markets, making them frontier-market economies.^c The capacity of developing countries to sustain a growth path that enables structural transformation depends on their ability to manage these rising external liabilities—irrespective of the form they take—during their development journey.

A critical, yet underrecognized, outcome of the inequities in the global financial architecture is the net resource transfer that occurs from developing countries to developed ones. Rising levels of foreign investment and other external financial inflows need to be serviced by dividends, royalties and other investment returns, and interest payments. These flows are captured in the primary income account of a country's current account. Most developing countries have rising deficits on their primary income accounts – not just because of increases in the scale of external liabilities relative to external assets, but because the cost of servicing those liabilities is consistently, and significantly, higher than the returns they are able to earn on their external assets. Typically, developing countries are creditors in safer, lower-yielding assets (mainly foreign exchange reserves which act as insurance for their high vulnerability to external financial shocks), while they are debtors in riskier, higher-yielding assets (foreign direct investment, portfolio investment in equity and external debt). Higher debt servicing costs and insufficient official development assistance and concessional finance contribute further to this imbalance.

Figure 1 indicates the average return earned by developed and developing countries on their external assets less the average cost paid by each group of countries on their external liabilities. Developing countries consistently had to pay a notably higher cost on their liabilities than they earned on their assets. Between 2005 and 2022 this difference averaged 2.1 per cent. By contrast, developed countries consistently earned a higher rate of return (averaging 0.3 per cent) on their external assets than they paid on their liabilities.

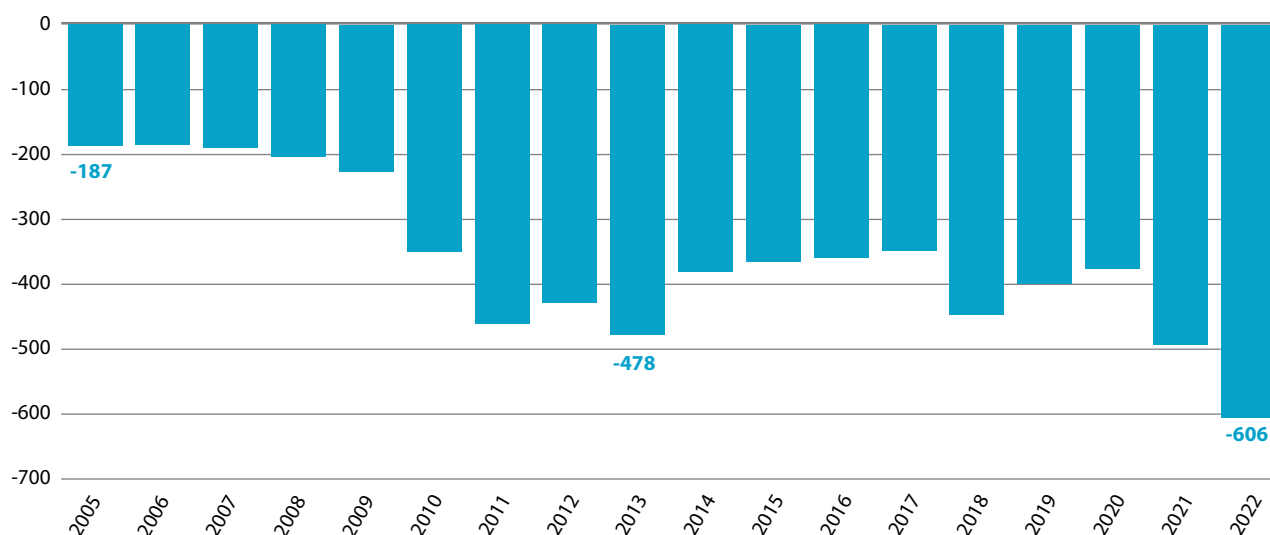
Figure 1
Trends in net costs of servicing external liabilities of developing countries relative to developed countries
(Per cent)



Source: IMF balance of payments and international investment position database, January 2024.

Note: Net cost of external liabilities equals cost of external liabilities less return on external assets.

Figure 2

Trends in net resource transfers from developing countries*(Billions of United States Dollars)*

Source: IMF balance of payments and international investment position database, January 2024.

Note: Net Resource Transfer is calculated as Primary Investment Income Credits Less Primary Investment Income Debits.

As a consequence of trends in the scale of external assets and liabilities, and these differences in the net costs of servicing these liabilities, developing countries have been transferring resources to developed ones increasingly over the years. Net outflows (primary income investment credits less primary income investment debits) from developing countries rose from around US\$200 billion per year between 2005 and 2009, to US\$478 billion in 2013, and to US\$606 billion in 2022 (figure 2).

In the view of UNCTAD, the Fourth International Conference on Financing for Development should put forward action areas to reverse this trend. Ideally, developing countries should be net recipients of resource transfers from developed countries. To meet this goal, the international community must step up efforts to reform the institutions, policies, rules and practices of the international monetary and financial architecture. This should aim not just to scale up the volume, but also to change the profile of development finance in terms of cost, currency composition, maturity structure and destination. The new development finance ecosystem should support developing countries in managing their net external liabilities on their path towards a low-carbon and climate-resilient structural transformation, which is a precondition for sustainable development and for reverting their negative net international investment positions.

a UNCTAD. 2023. *World Investment Report* (United Nations publication. Sales No. E.23.II.D.24. New York and Geneva).

b Akyüz, Y. 2017. *Playing with Fire: Deepened financial integration and changing vulnerabilities of the Global South*. Oxford University Press. Oxford.

c UNCTAD. 2019. *Trade and Development Report: Financing a global green new deal* (United Nations publication. Sales No. E.19.II.D.15. New York and Geneva).



The Higher Price Tag for Inaction on Finance and Climate

Achim Steiner, UNDP Administrator

More than two decades have passed since the First International Conference on Financing for Development was held in Monterrey, Mexico in 2002. As we now prepare for the Fourth International Conference on Financing for Development in Spain next year, our global community unfortunately cannot claim to have made great progress in ensuring that developing countries have the means to finance the future they want. The upcoming Conference is a chance to change that.

A lack of finance is one of the main impediments holding back progress on the Sustainable Development Goals (SDGs), and with **only 15 per cent of SDG targets estimated to be on track**, finance must urgently find its way to development spending to close the SDG investment gap. To make meaningful progress on the SDGs, including on climate mitigation and adaptation, it is estimated that emerging markets and developing economies—excluding China—will need to **increase annual spending by at least \$3 trillion by 2030**.

The urgency of bridging the SDG investment gap is pivotal as the climate emergency intensifies. Discouragingly, global emissions show no signs of coming down, meaning that we are rapidly depleting our remaining carbon budget -- the maximum amount of CO2 the world can still emit if we are to stay within agreed global warming limits. As an example, at current levels of emissions, we only have about **six years left until we have 'spent' the remaining 1.5°C degree budget**. Many developing economies do not have the resources to fund mitigation without being forced to trade-off other urgent development needs. With a recognition that only action by each and every country can slow the steady march of climate change, this inaction will put our global community's chances of staying within agreed warming limits in jeopardy – the consequences of not doing so being extremely costly and **potentially catastrophic**.

The trade-offs facing developing economies worsened sharply as a consequence of the COVID-19 pandemic and remain highly concerning in today's challenging environment of high levels of debt and interest rates. More than 50 per cent of developing economies with a credit rating are now considered *below* “**non-investment grade**” and more than 50 per cent of the poorest countries are in or at high risk of debt distress. Over the past decade or so, interest payments in developing economies have been consuming an ever-increasing share of revenue and expenditure. For many of them, debt servicing levels are at an all-time high and crowding out critical spending in areas such as social protection, health, and education.

Action must follow on all fronts of the financing for development agenda. Countries must undertake domestic reforms that raise revenue, cut unnecessary spending, develop capital markets, and lower credit risk to attract more private capital. In this vital area, more than 85 countries are leveraging **Integrated National Financing Frameworks** (INFFs) to help drive game-changing finances to the SDGs and the Paris Agreement with support from key partners including UNDP, UNICEF, UNDESA and the OECD. As a result, 13 governments have operationalized holistic, impact-oriented financing strategies; and more than 50 are implementing reforms to reconfigure key elements of their domestic financial architecture in ways that leverage and align finance for sustainable development. Realising the potential of these country-led INFFs will require enhanced support from the international community.

Indeed, as the international community, we must do more to ensure that countries in need gain access to effective and fair means of restructuring debt and liquidity support, enabling them to break free from the negative ‘debt-development feedback loop’. We must also address issues of unfairness in international trade and taxation and do more to combat illicit financial flows. Crucially, we must recognize that many developing economies cannot achieve a sustainable development transformation without a much larger and more responsive multilateral financial system as outlined in the United Nations Secretary-General's **SDG Stimulus Plan**. To reach the scale of finance needed, more official sector funding must also be accompanied by new and better approaches to leveraging private sector finance for development.

The challenge for the Fourth International Conference on Financing for Development will be to reset and recommit on the global partnership to facilitate the financing needed to meet the 2030 Agenda and the Paris Agreement's objectives. This will require an honest stocktake of progress made to date and a critical assessment of current priorities and approaches. The Financing for Sustainable Development Report 2024 is a crucial input in this regard.

In short, we need a stronger recognition of the fact that we are running out of time. We need urgent action and a focus on what is likely to work given the constraints we are operating under while ensuring that our proposals are evidence-based and strongly rooted in principles of global fairness.

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The global economic context and its implications for sustainable development



Chapter II



The global economic context and its implications for sustainable development

1. Introduction

At the midpoint for achieving the 2030 Agenda for Sustainable Development, the world economy lacks dynamism and is grappling with an array of risks and challenges. After a period of rapid economic expansion early in the millennium, the global economy's momentum has waned, creating a challenging environment for financing development. Global investment, trade and productivity growth have all decelerated amid a series of major crises and economic and non-economic shocks, from the 2007/08 food price crisis and the 2008 world financial and economic crisis to the COVID-19 pandemic and escalating geopolitical conflicts. Hard-earned development gains have been reversed, particularly in poor and vulnerable countries, which have yet to fully recover from the pandemic shock. These countries are also most affected by ever-increasing climate challenges that threaten to jeopardize people's lives, health and productivity, and pose substantial economic tail risks.

In this highly challenging environment, the global economic outlook remains fragile, with growth prospects subdued. The world economy avoided the worst-case scenario of a recession in 2023, with growth estimated at 2.7 per cent. But global growth, on a market exchange rate basis, is projected to slow to 2.4 per cent in 2024 before experiencing a moderate improvement to 2.7 per cent in 2025,ⁱ and is expected to remain weak in the medium term amid subdued investment and high levels of debt. Downside risks include: commodity price spikes and supply disruptions due to conflicts

and further escalation of geopolitical tensions; a prolonged period of tight financing conditions; persistent inflation; and trade fragmentation. On the other hand, faster disinflation could ease financing conditions while a fiscal stance that is less contractionary than expected across countries as well as a stronger economic performance of major economies provide additional upside risks to the forecasts.

The global shift in monetary policy since 2022—from ultra-loose to restrictive stances—has exacerbated public finance pressures and is weighing on investment prospects. Globally synchronized monetary tightening to address surging inflationary pressures in 2022 has resulted in more restrictive global financial conditions and pushed up borrowing costs. While global inflation declined in 2023, real policy interest rates are expected to remain elevated for some time due to concerns over a resurgence of inflationary pressures. Against this backdrop, many developing countries are expected to face constrained access to international financial markets and elevated borrowing costs, which will likely limit countries' capacity to invest in the Sustainable Development Goals (SDGs), boost long-term productivity and combat climate change.

To boost investment and improve medium-term growth and sustainable development prospects, national actions and international cooperation must be stepped up. Comprehensive national policy packages that foster macroeconomic stability and promote structural transformations have been shown to be effective at driving investment.¹ At the

ⁱ The growth figures are based on the United Nations World Economic Situation and Prospects 2024. Other Task Force members also projected a slowdown of global growth—on a market exchange rate basis—in 2024. The IMF World Economic Outlook January 2024 projected world gross product to grow by 2.6 per cent in 2024, down from 2.7 per cent in 2023. The World Bank Global Economic Prospect January 2024 projected a global growth of 2.4 per cent in 2024, down from 2.6 per cent in 2023.

same time, greater global cooperation is more important than ever across the action areas of the Addis Ababa Agenda to reduce debt distress and provide relief where needed, facilitate trade integration and technology transfer, alleviate food insecurity, scale up climate finance and stimulate investment in the SDGs. Without a concerted effort, the world faces a protracted period of weak investment, slow growth and high debt service burdens, which would put the SDGs out of reach.

2. Global and regional growth trends and outlook

The past 20 years have been marked by several large crises alongside major shifts in the geopolitical and economic landscape.

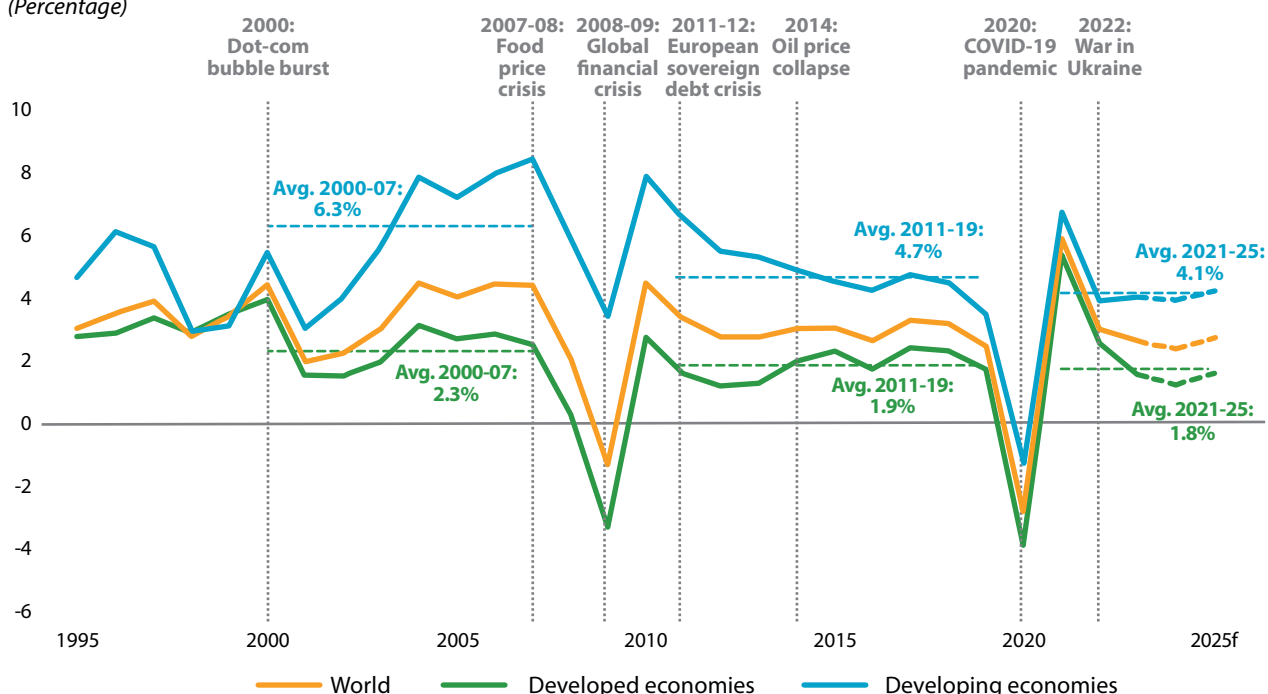
In the early 2000s, the global economy experienced a period of significant expansion driven by globalization, advancements in technology and robust economic growth in large developing countries, notably China and India. The rise in global demand during this period fuelled a commodity boom. Global trade activities were also buoyed by the proliferation of global value chains as well as key milestones in trade liberalization, including China's accession to the World Trade Organization in 2001 as well as the earlier formation of the European Union in 1995. Against this backdrop, global foreign direct investment (FDI) flows grew rapidly. This strong performance came to a halt in 2008. Developed economies were hit hard by the 2008 world financial and economic crisis, which caused severe recessions and massive job losses. A prolonged period of deficient demand combined with stagnant productivity growth raised fears of economic stagnation.

Developing economies initially demonstrated resilience, but the crisis reverberated across the world and affected global financial markets and trade. The decade following it was eventually characterized by a noticeable slowdown in growth across developed and developing economies. In 2020, the COVID-19 pandemic then sent the world economy into a free fall, triggering the most severe global economic crisis in the past century (figure II.1).

Over the past four years, a series of severe and mutually reinforcing shocks have led to a substantial reversal in development progress, particularly for some of the world's poorest countries.

The COVID-19 pandemic exposed systemic vulnerabilities in the world economy, while inflicting extensive damage on lives and livelihoods. By the end of 2023, nearly 7 million people had lost their lives directly due to the virus.^{2,3} The pandemic triggered the worst global economic crisis since the Great Depression, as widespread mobility restrictions led to a collapse in consumer spending and investment, massive job losses and severe disruptions to global supply chains. Recovery from the crisis was uneven and more subdued in developing countries due to slower vaccination progress and more limited macro-policy support in countries with very limited fiscal and monetary policy space. The war in Ukraine in early 2022 subsequently exacerbated rising prices and led to a global cost-of-living crisis. Acute supply disruptions drove food and energy prices to record levels, disproportionately impacting the most vulnerable populations. As global inflation surged to a two-decade high, central banks worldwide tightened monetary policy stances in efforts to rein in inflationary pressures. The aggressive pace of interest rate hikes by the United States Federal Reserve generated spillovers on developing countries, with many experiencing

Figure II.1
Global growth, 1995–2025
(Percentage)



Source: UN DESA calculations based on estimates and forecasts produced with the UN DESA World Economic Forecasting Model.

Notes: f=forecasts.

bouts of sizeable capital outflows and currency depreciations. For many developing countries, the sharp tightening of global financial conditions has intensified debt vulnerabilities and balance-of-payment pressures.

Against this backdrop of lingering risks and uncertainties, global growth is expected to weaken further in 2024 before picking up modestly in 2025. *The United Nations World Economic Situation and Prospects 2024* projects that global growth will decelerate to 2.4 per cent in 2024, from 2.7 per cent in 2023. Growth is forecast to improve moderately to 2.7 per cent in 2025 but will remain below the pre-pandemic average growth rate of 3.1 per cent. A protracted period of low growth would make a full recovery of pandemic losses ever more elusive for vulnerable countries. Indeed, in 2023, the cumulative output losses from recent crises—calculated as the sum of the annual difference between pre-pandemic projections of GDP and actual GDP—amounted to about 40 per cent of the 2019 GDP in small island developing States (SIDS) and about 30 per cent in the least developed countries (LDCs) (figure II.2).

While immediate risks to the global outlook appear more balanced, downside risks remain and prospects are subpar in the medium term. Global inflation is projected to moderate further. Fiscal stances that are less contractionary than expected across countries as well as faster growth in China and sustained growth in the United States would also lift growth prospects. On the other hand, there are several major downside risks that threaten short- and medium-term prospects. First, energy and food prices could surge again due to escalating conflicts and the increasing likelihood of climate shocks. Major central banks could keep interest rates “higher for longer” as inflation risks remain. This would

weigh on aggregate demand and further increase debt sustainability risks. Second, global merchandise trade and global industrial production remain exceptionally weak amid cyclical and structural headwinds. This weakness is partly attributable to tighter financial conditions and a continued shift towards spending on services, but it also reflects heightened economic and trade policy uncertainties associated with geopolitical tensions and fragmentation. A more fragmented global economy poses risks to production efficiency and spillovers of technology and knowledge which—together with subdued investment—would dampen medium-term growth prospects. The International Monetary Fund estimates that geoeconomic fragmentation could cause a permanent world gross product loss of 7 per cent through disruptions in trade alone.⁴ Third, and relatedly, digitalization and related frontier technologies such as artificial intelligence (AI) have the potential to stimulate global growth, but digitalization gaps persist between developed and developing countries due to lack of required infrastructure, technology equipment, and human resources and expertise.⁵ Such a digital divide will affect people’s access to the benefits of technologies and risk further exacerbating economic and social divides. Fourth, the ever-increasing adverse impacts of climate change pose a major risk to global development, especially for vulnerable countries such as LDCs and SIDS, which are already facing severe economic challenges and have limited fiscal space to respond.

Poverty, hunger and inequality

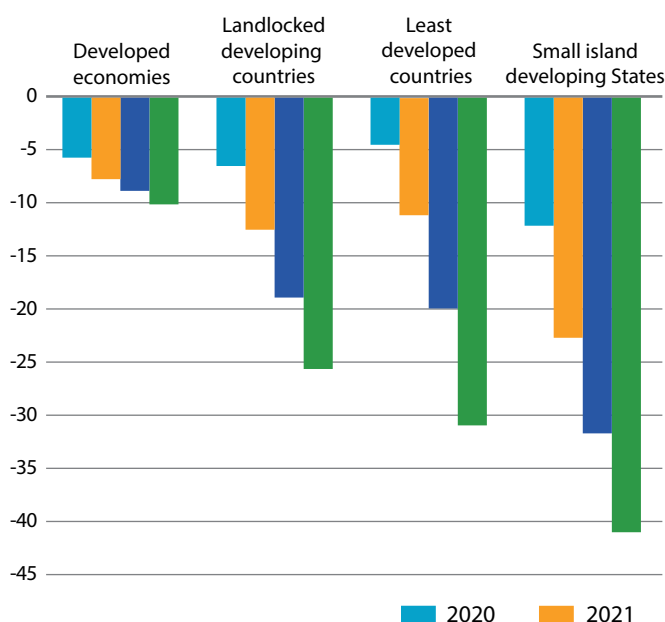
The highly challenging macroeconomic environment threatens to significantly set back global poverty eradication. Over the past

Figure II.2

Cumulative output losses relative to pre-pandemic projections, 2020–2023

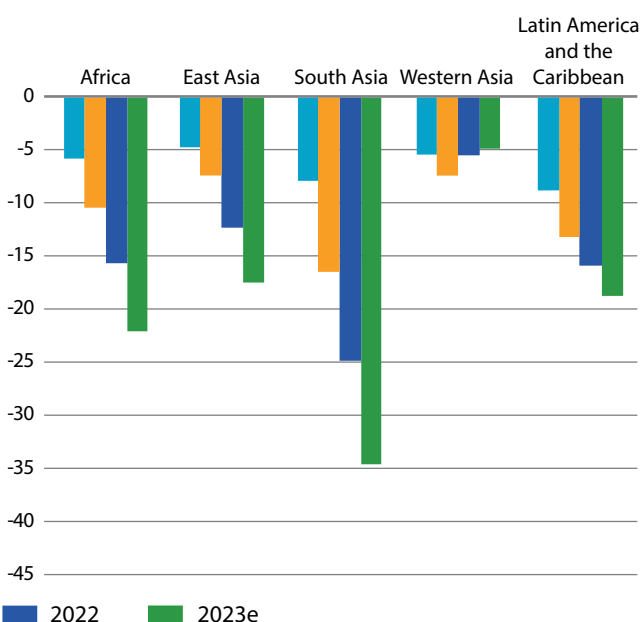
(a) Country groupings

(Percentage of 2019 GDP)



(b) Developing regions

(Percentage of 2019 GDP)



Source: UN DESA calculations based on estimates produced with the UN DESA World Economic Forecasting Model.

Notes: e = estimates. Cumulative output losses are calculated as the sum of the annual difference between actual GDP levels and pre-pandemic GDP projections.

two decades, tremendous progress has been achieved in alleviating poverty across the world. Between 2000 and 2019, the number of people living in extreme poverty (\$2.15 per day or less) globally declined from 1.8 billion to 701 million.⁶ However, even before the pandemic, the pace of progress was slowing. Between 2015 and 2019, the global poverty rate fell by around 0.54 percentage points per year, less than half the reduction observed between 2000 and 2014. The confluence of shocks and crises since 2020 then reversed gains, with an additional 75 million to 95 million people being pushed into extreme poverty in 2022 relative to pre-pandemic baseline forecasts.⁷ While global poverty declined marginally in 2023,⁸ progress has been highly uneven. Average poverty rates in lower-middle-income, upper-middle-income and high-income countries moved closer to pre-pandemic levels. In contrast, poverty rates were still well above pre-pandemic levels in low-income countries, particularly those in Africa and the Middle East.⁹ These trends are mirrored in per capita GDP growth rates (figure II.3): a significant deceleration across regions after 2008, and lagging performance in Africa in particular, which saw average GDP per capita increase by less than 1 per cent annually over the last 15 years. Overall, the World Bank projects that by the end of 2024, one out of every four developing countries and around 40 per cent of low-income countries will still be poorer than they were in 2019.¹⁰ Without significantly faster economic growth and targeted measures for supporting livelihoods, enhancing social protection and addressing inequality, poverty eradication will remain elusive in many low-income countries.

Elevated food prices have been a significant driver of food insecurity in developing countries. In 2023, an estimated 238 million people experienced acute food insecurity, an increase of 21.6 million

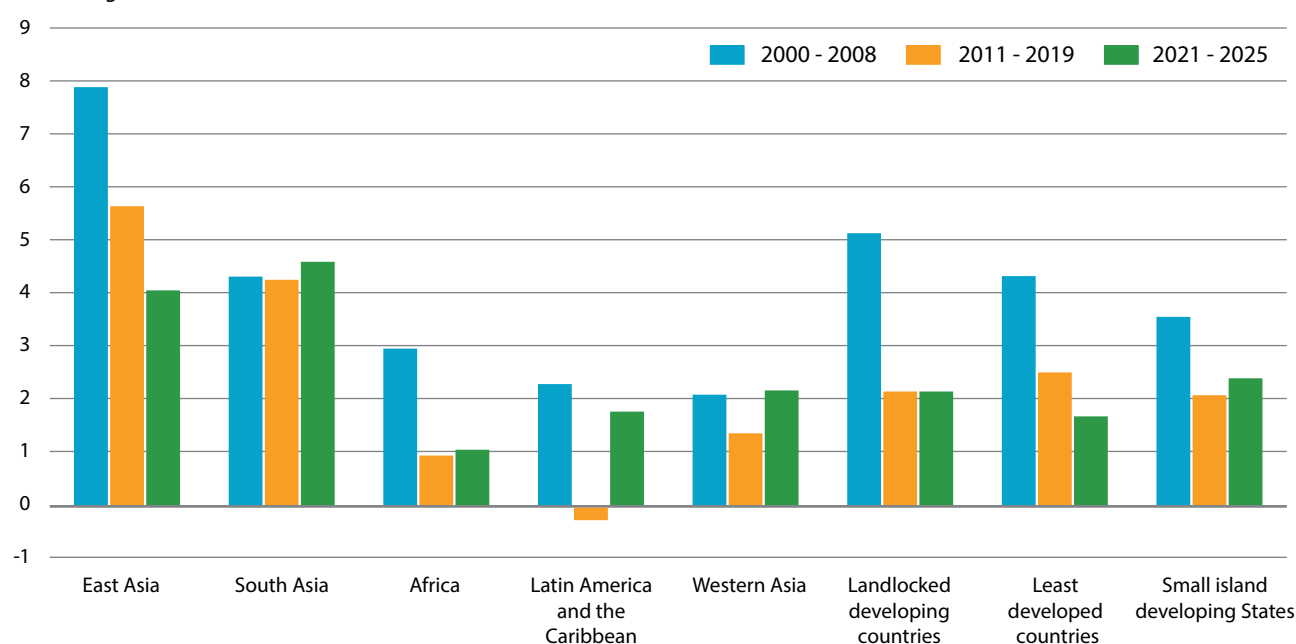
people from the previous year. The rise in food prices have disproportionately affected the poorest households, which spend a larger share of their income on food.

The overlapping crises have exacerbated inequalities between and within countries. Across countries, governments' capacity to provide fiscal support and roll out COVID-19 vaccines was very uneven. Within countries, there were significant disparities in the ability of households to shield themselves from job and income losses during recent crises. Education losses for disadvantaged students could have lasting effects on their future earnings and reduce intergenerational mobility.¹¹

3. Deterioration in public finances

Public finances have deteriorated over the past decade. Since 2000, fiscal deficits have expanded in both advanced economies as well as emerging markets and developing economies (figure II.4a). This was particularly the case during the 2008 world financial and economic crisis and the COVID-19 pandemic, as many countries increased public expenditures to cushion their economies from the adverse effects of these crises and stimulate growth. With fiscal revenues as a share of GDP stagnating or even falling in several regions since 2010 (figure II.4b), countries have relied on borrowing to finance their growing spending needs. Ultra-loose global financial conditions in the aftermath of the 2008 world financial and economic crisis allowed many low-income and lower-middle-income countries to access international financial markets, many for the first time—albeit at higher interest rates—and caused a significant expansion of global public debt (see chapter III.E.).

Figure II.3
Average annual GDP per capita growth by region, select years between 2000 and 2025
(Percentage)

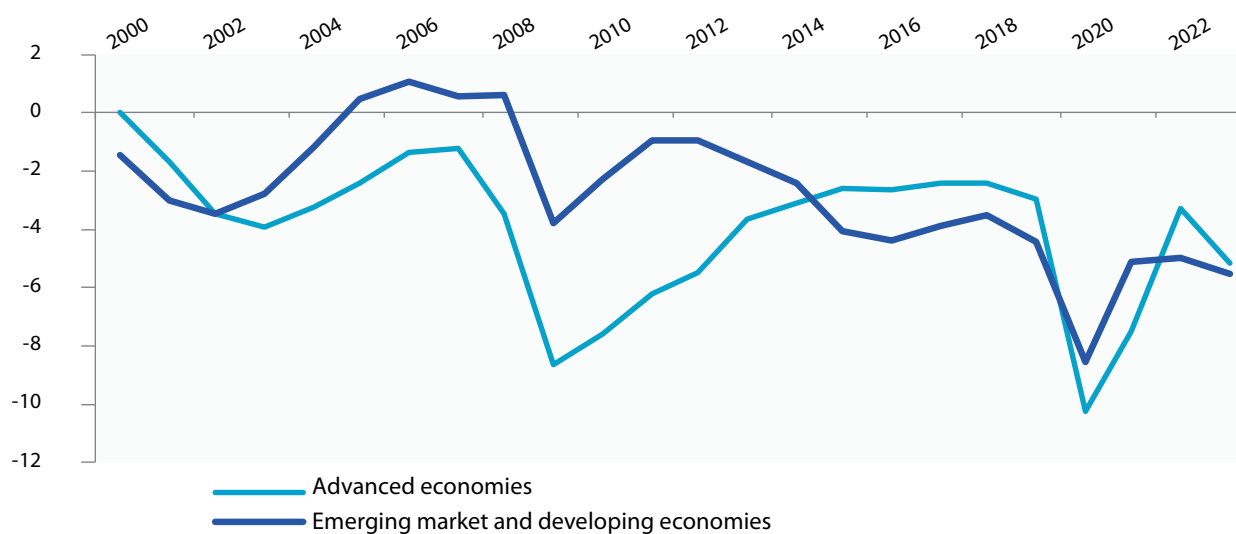


Source: UN DESA, based on estimates and forecasts produced with the UN DESA World Economic Forecasting Model.

Figure II.4

Trends in public finances**(a) Fiscal deficits, by country group, 2000–2023**

(Percentage of GDP)

**Source:** UN DESA calculations based on data from the IMF World Economic Outlook database, October 2023.**Notes:** Regional groups follow the source.**(b) General government revenue, by region, select years during 2000–2023**

(Percentage of GDP)

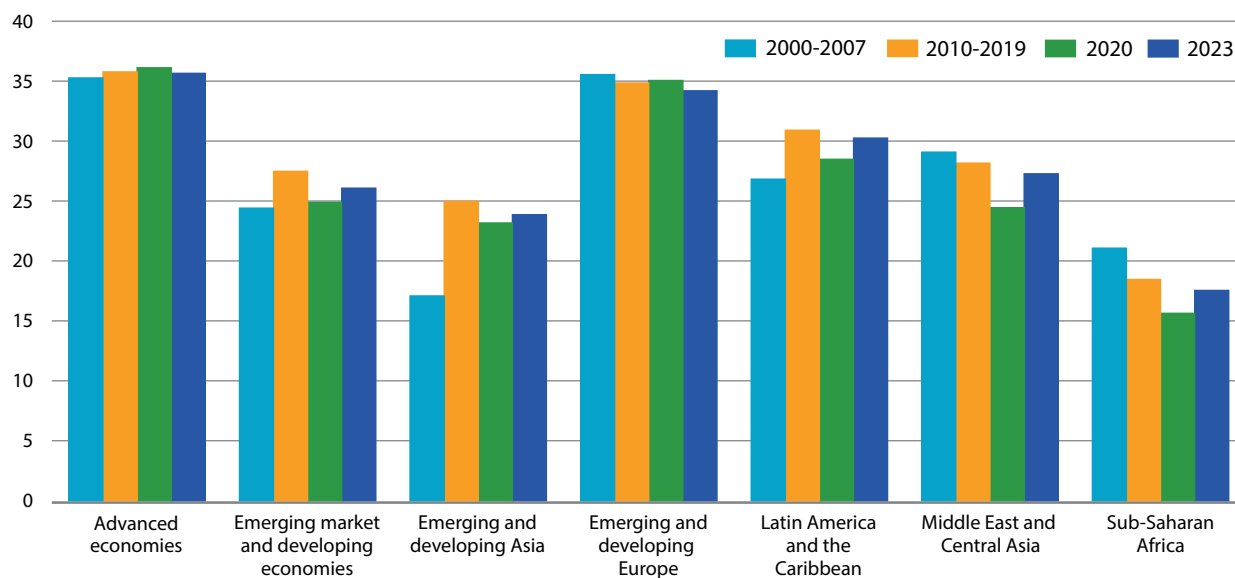
**Source:** UN DESA calculations based on data from the IMF World Economic Outlook database, October 2023.**Notes:** Regional groups follow the source.

Figure II.4

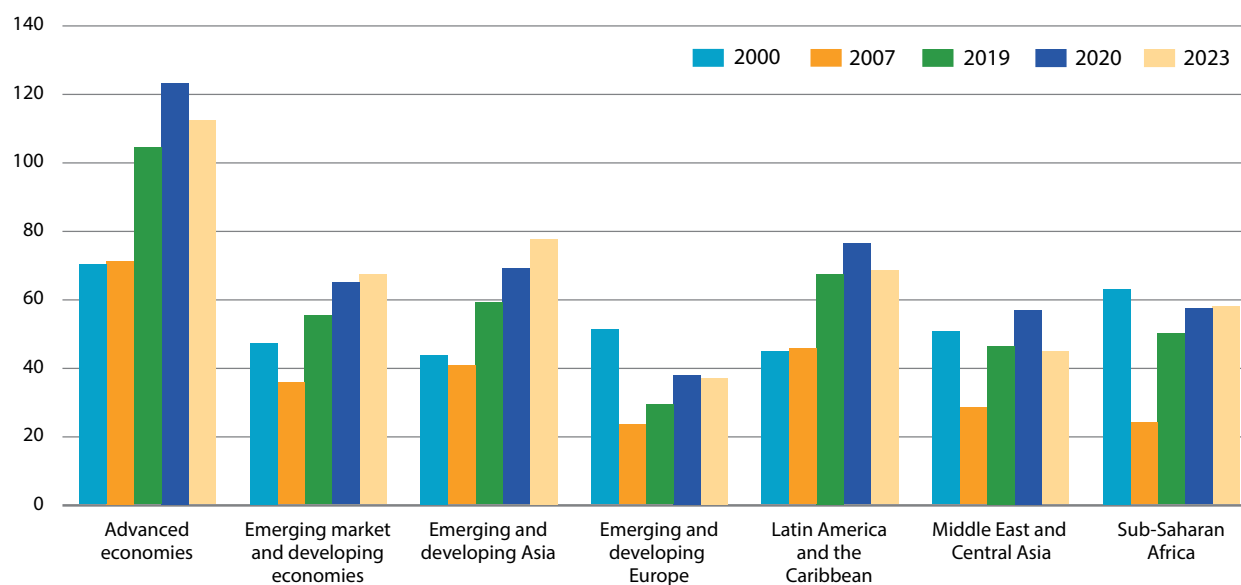
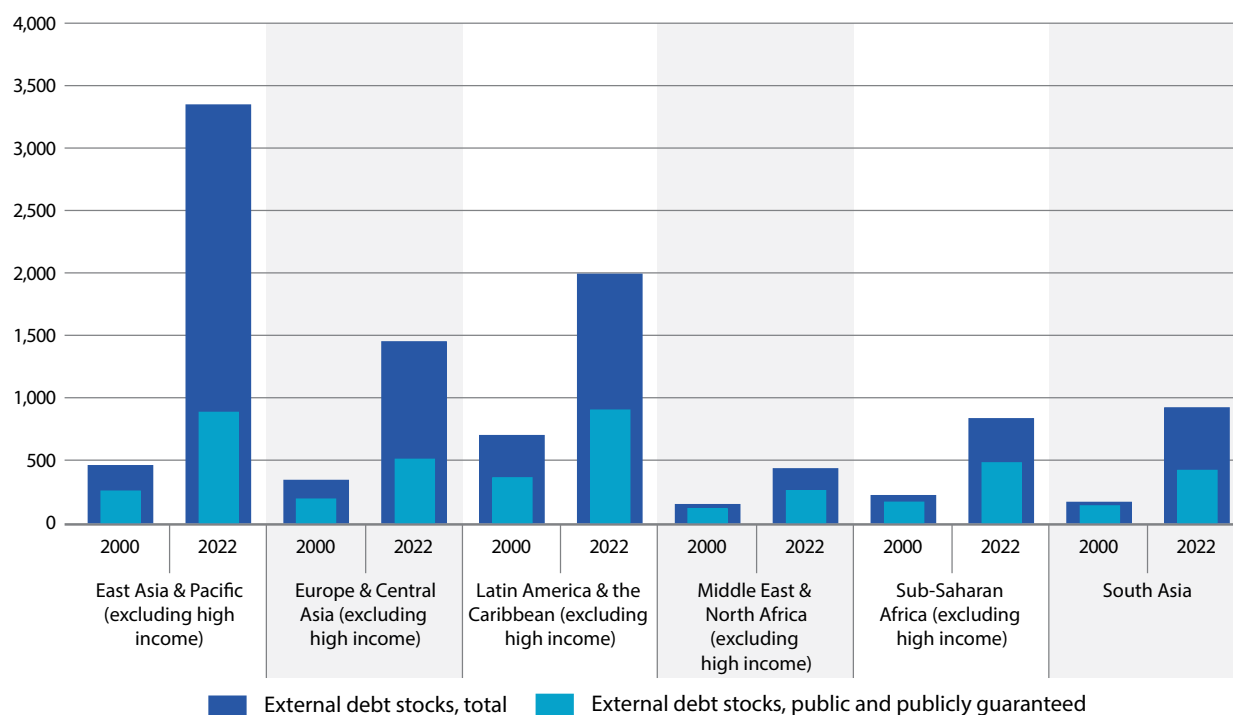
Trends in public finances**(c) General government gross debt by region, select years between 2000 and 2023***(Percentage of GDP)***Source:** UN DESA calculations based on data from the IMF World Economic Outlook database, October 2023.**Notes:** Regional groups follow the source.

Figure II.5

External debt stocks by region, 2000 versus 2022*(Billions of United States dollars)***Source:** UN DESA calculations based on data from the World Bank International Debt Statistics.**Note:** Regional groups follow the source.

The debt challenges of developing countries are compounded by high interest rates and debt service burdens. While global inflation eased significantly in 2023, major developed country central banks have signalled their intention to keep interest rates higher for longer; real policy interest rates may remain elevated for some time. A prolonged period of tighter credit conditions will keep borrowing costs for developing countries at a high level, exacerbating debt sustainability risks and adding to debt service burdens (see figure II.5, figure II.6 and chapter III.E.). High and growing debt-service burdens could further constrain fiscal space at a time when developing countries need to mobilize financial resources to stimulate investment and growth, address climate change-related risks and accelerate progress towards the SDGs.

4. Monetary and financial stability risks

Global monetary policy has seen major shifts in the past two decades amid the introduction of new frameworks and instruments.

In the United States, for instance, as the world financial and economic crisis took hold in 2008, the Federal Reserve was quick to slash interest rates, taking them to nearly zero in December 2008 (figure II.7a). In the face of a systemic financial crisis at the zero lower bound, the Federal Reserve then turned to alternative and unconventional tools, particularly quantitative easing (QE),¹² to provide liquidity, restore confidence and stimulate the economy. The outbreak of COVID-19 forced it to cut rates again to near zero

and conduct quantitative easing. The size of the Federal Reserve's assets peaked at nearly \$9 trillion in April 2022, compared with \$890.7 billion in January 2008 (figure II.7b). Europe experienced similar monetary policy episodes, while in Japan, the central bank has kept interest rates low and maintained a negative rate since 2016 amid economic stagnation and deflation. Policy rates in developing countries, while at higher levels, largely tracked those of the central banks in major economies (figure II.8).

The prolonged period of “easy money” came to an end as major central banks responded to the return of high inflation in 2021.

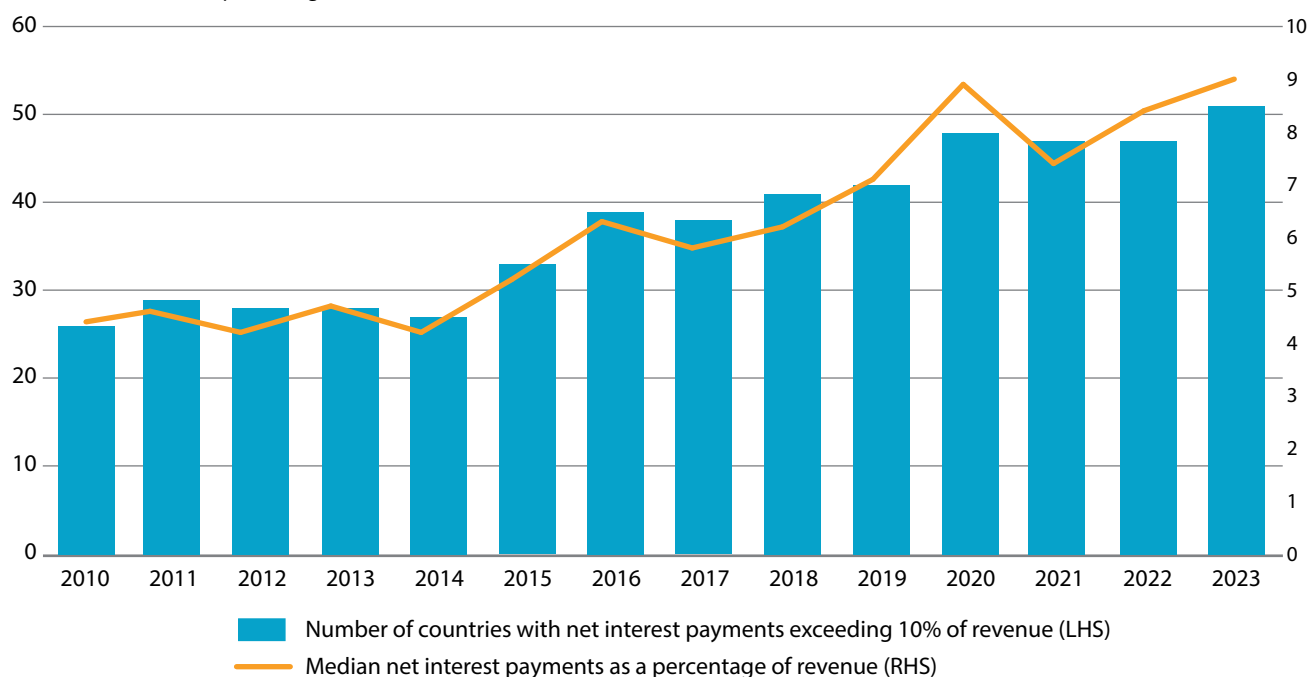
Major developed country central banks began to raise interest rates in 2021 and 2022.¹³ Although inflation slowed considerably in 2023, major central banks have signalled their intention to keep interest rates “higher for longer”. In addition to rate hikes, major developed country central banks have also started selling off assets on their balance sheets—pursuing a process known as quantitative tightening (QT)—to reduce liquidity in financial markets.

Monetary policies in major developed countries have significant spillover effects on developing countries, with synchronized tightening since 2022 constraining policy space for developing country central banks. Low interest rates and ultra-loose monetary policies after 2008 prompted large capital flows to developing countries, lowering sovereign spreads during this period (figure II.9). However, capital flows remained very volatile throughout this period, experiencing significant fluctuations and later a downward trend, with significant outflows during and since the pandemic amid the tightening of global financing conditions. The resulting rising interest rate spreads and currency

Figure II.6

Government interest expenditures in developing countries, 2010–2023

(Number of countries, percentage of revenue)



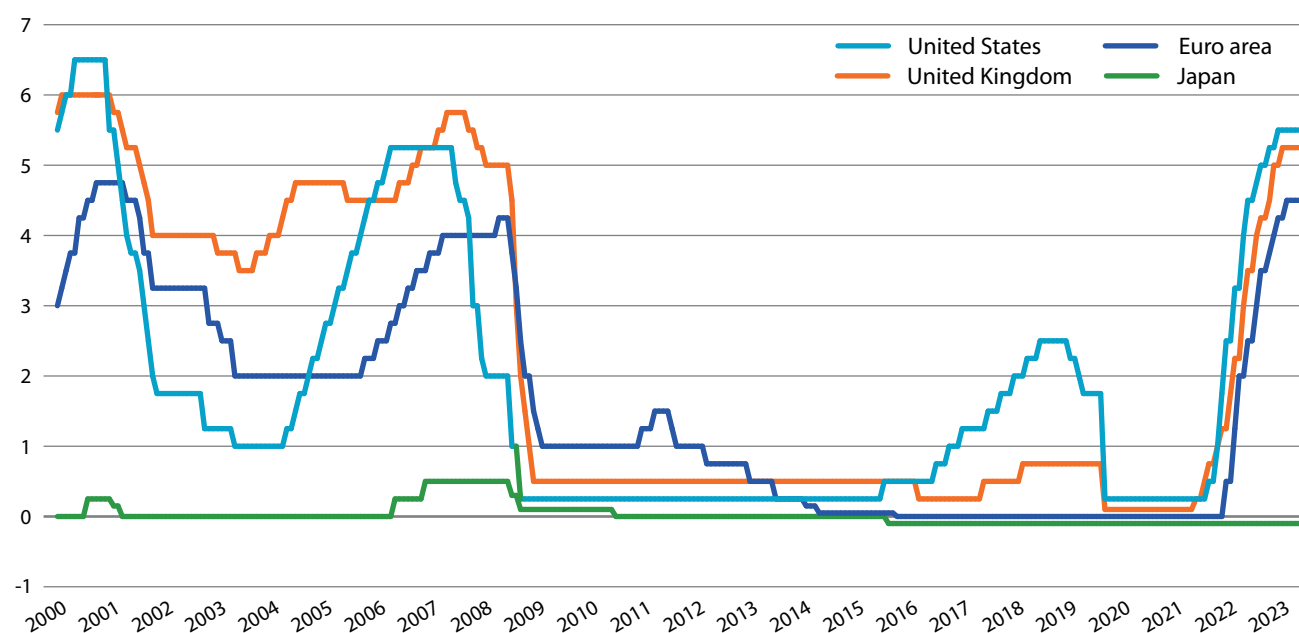
Source: UN DESA calculations based on data from the IMF World Economic Outlook database, October 2023.

Note: LHS = left-hand scale; RHS = right-hand scale. Net interest payments of the general government equal the total amount of domestic and external interest expenses incurred from loans and other forms of borrowing minus any interest income received.

Figure II.7

Monetary policies in selected major developed countries**(a) Policy rates, 2000–2023**

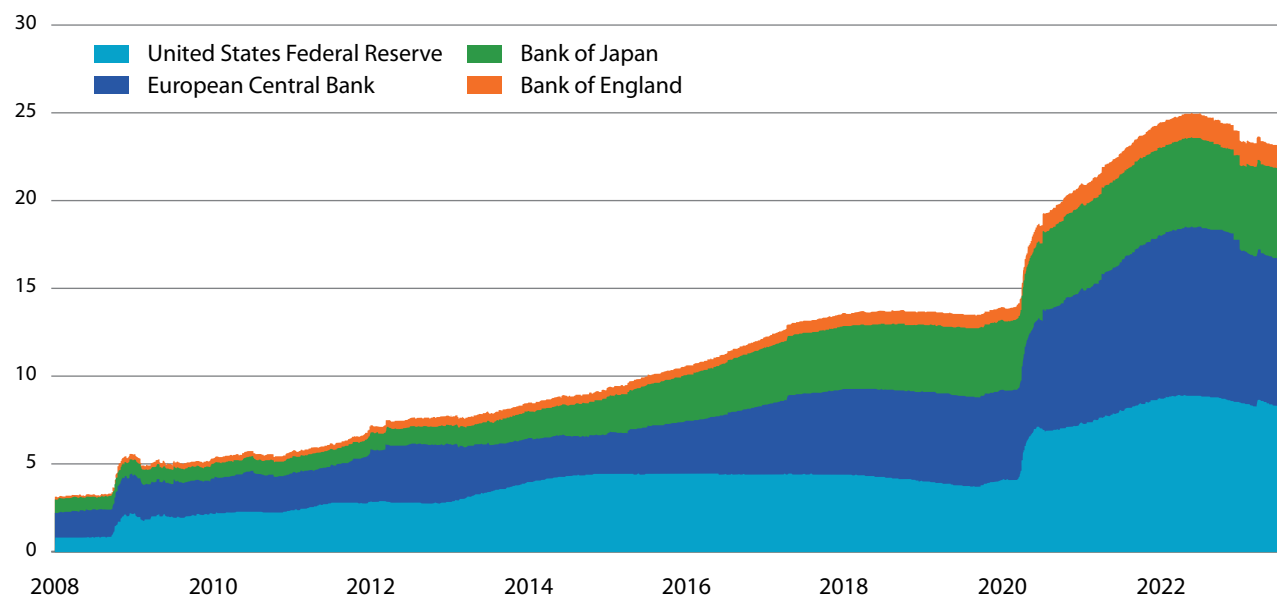
(Percentage)



Source: UN DESA calculations based on Trading Economics (accessed on 1 January 2024).

(b) Assets of central banks' balance sheets, 2008–2023

(Trillions of United States dollars)



Source: UN DESA calculations based on data from the Federal Reserve, European Central Bank, Bank of England, Bank of Japan, CEIC and Trading Economics (accessed on 30 October 2023).

Note: All assets of the Bank of England, Bank of Japan and European Central Bank are converted into United States dollars by using the exchange rates on 31 August 2023.

weakness exacerbated debt sustainability risks for many developing countries in 2022 and 2023 and are limiting monetary policy space. Higher interest rates in developed countries will continue to increase the debt-servicing burden of developing countries, particularly those with high levels of dollar- or euro-denominated public debt. And many developing country central banks may be restricted in lowering interest rates to support growth even when inflation pressures ease, as that could lead to capital outflows, currency depreciations, increased risk premia and further heightened debt sustainability risks.

5. Weak investment prospects

Investment growth—a key driver of long-term productivity—has slowed over the past two decades, particularly in developing countries. As figure II.10 shows, the growth of gross fixed capital formation in the world accelerated during the first half of the 2000s but declined thereafter, in both developed and developing countries. Amid the series of crises and shocks described above, economic uncertainties increased, which discouraged firms' investment activities. Global investment growth is projected to grow by only 2 per cent in 2024, only a marginal improvement from the 1.9 per cent estimated for 2023, and significantly below its 2011–2019 average growth rate of 4 per cent.

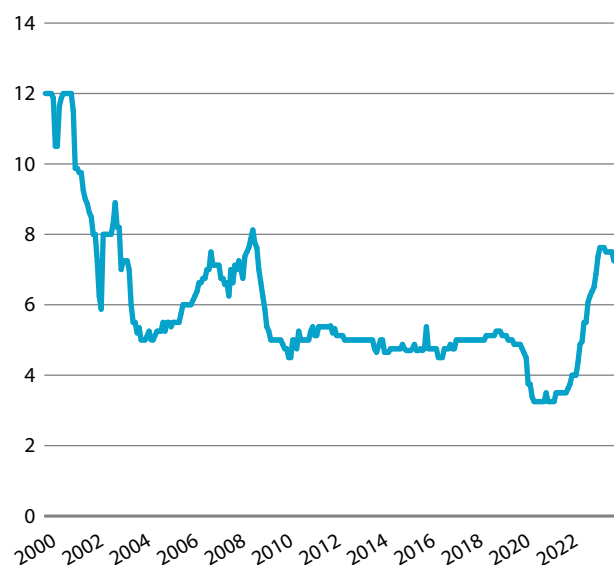
The ultra-loose monetary environment in the aftermath of the 2008 world financial and economic crisis did not successfully boost investment growth. In developed economies, commercial banks were reluctant to fund fragile businesses during uncertain economic times and, instead, kept the additional resources in their reserve accounts at

the central banks. In the United States, for instance, excess reserves of depository institutions held in the Federal Reserve surged from \$1.6 billion in January 2008 to \$2.7 trillion in August 2014.¹⁴ In developing economies, deceleration of investment growth in the decade leading up to the COVID-19 pandemic reflects the significant drop in commodity prices from 2014 to 2016 and the associated deterioration in the terms of trade, weak growth in advanced economies and high corporate leverage.¹⁵ Moreover, while loose global financial conditions in the decade after the 2008 world financial and economic crisis encouraged capital inflows, these flows predominantly came through portfolio channels, with no clear effect on investment and growth.¹⁶

Productivity growth—largely driven by productive investments—has declined considerably in developing countries in the past two decades. Annual total factor productivity (TFP) growth, a key measure of economic efficiency and productivity, fell from 1.6 per cent between 2000 and 2007 to 0.2 per cent between 2011 and 2019 in developing economies. In sub-Saharan Africa, annual TFP growth declined by an even larger margin, falling from 2.1 per cent between 2000 and 2007 to -0.2 per cent between 2011 and 2019. A multitude of factors, including constrained investment, inadequate research and development activities, limited technology spillovers, weak institutions and decelerated international trade growth, contributed to the decline in TFP growth.

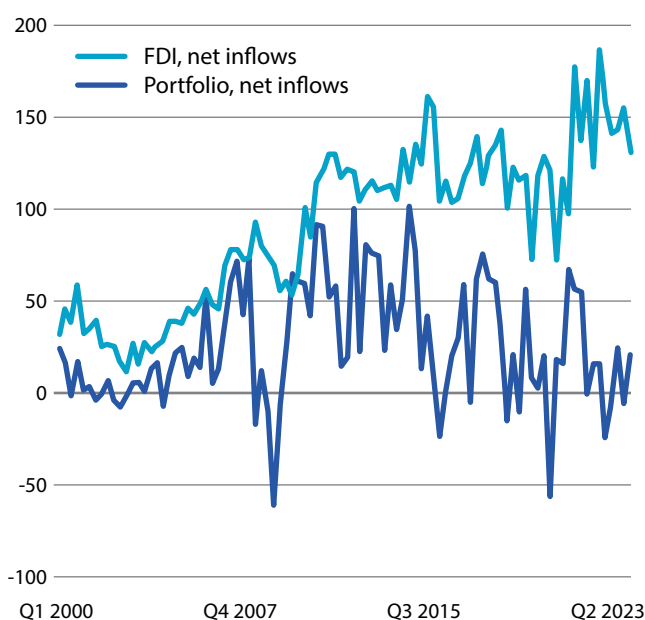
Investment is expected to remain subdued globally. In 2023, residential investment fell significantly in most developed economies amid rising mortgage interest rates and construction costs. The United States saw a particularly severe decline, with residential fixed investment in the

Figure II.8
Policy rates in developing economies (median), 2000–2023
(Percentage)



Source: UN DESA calculations based on CEIC data (accessed on 2 January 2024).
Notes: The last observation of the data is November 2023. Fifty-four developing country central banks are covered. However, country coverage may differ between years due to data availability.

Figure II.9
Capital flows to developing countries, Q1 2000–Q2 2023
(Billions of United States dollars)

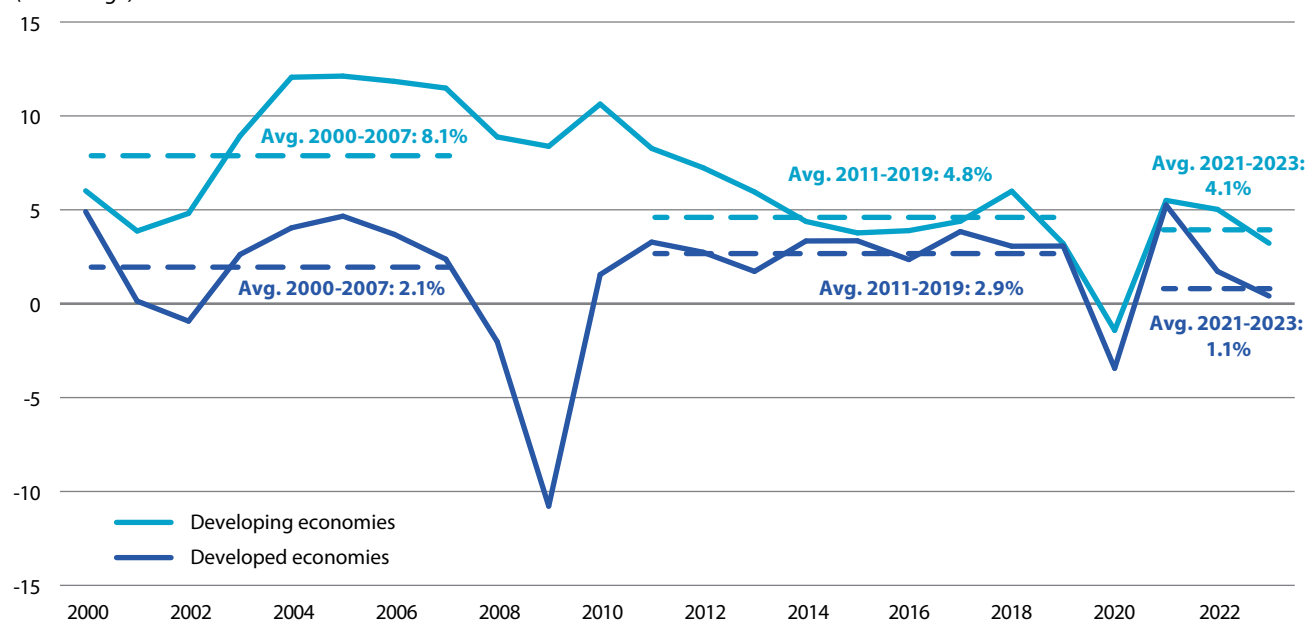


Source: UN DESA calculations based on the IMF Balance of Payments and International Investment Position Statistics (accessed on 2 January 2024).
Notes: Thirty-three developing countries are covered based on available data.

Figure II.10

Growth of gross fixed capital formation in developed and developing economies, 2000–2023

(Percentage)



Source: UN DESA calculations based on estimates and forecasts produced with the UN DESA World Economic Forecasting Model.

Note: Growth rates for 2023 are partially estimated.

first three quarters of 2023 down 14 per cent in comparison with the same period in 2022. In contrast, investment in intellectual property remained robust (figure II.11). Prospects in most developing countries are also weak due to softer external demand, volatile commodity prices, high borrowing costs and fiscal consolidation pressures. High levels of debt amid subdued growth continue to constrain fiscal space, making it harder for governments to borrow and invest. Conflicts hamper investment in parts of Africa and Western Asia. In contrast, investment in South Asia, particularly in India, remains strong. India is benefiting from growing interest from multinationals, which see the country as an alternative manufacturing base in the context of developed economies' supply chain diversification strategies.¹⁷

6. Labour markets

Recent crises have adversely affected global labour markets, with recovery uneven across regions. After reaching a peak of 6.5 per cent in 2009 during the world financial and economic crisis, the global unemployment rate moderated, falling to 5.6 per cent in 2019. In the wake of the COVID-19 pandemic, the unemployment rate increased to 6.6 per cent in 2020, with the number of people unemployed increasing from 194 million to 227 million in just one year.¹⁸ Young workers and workers with basic education were among the most affected. The post-pandemic recovery has been swift but uneven. Although the global unemployment rate dropped to an estimated 5.1 per cent in 2023, labour market recoveries diverged considerably between developed and developing countries. Key employment indicators in many developing countries have yet to return to pre-pandemic levels. In parts of Western Asia and Africa, for instance,

unemployment rates in 2023 still exceeded 2019 levels. Slowing economic growth in 2024 is expected to further weigh on employment prospects in many regions.

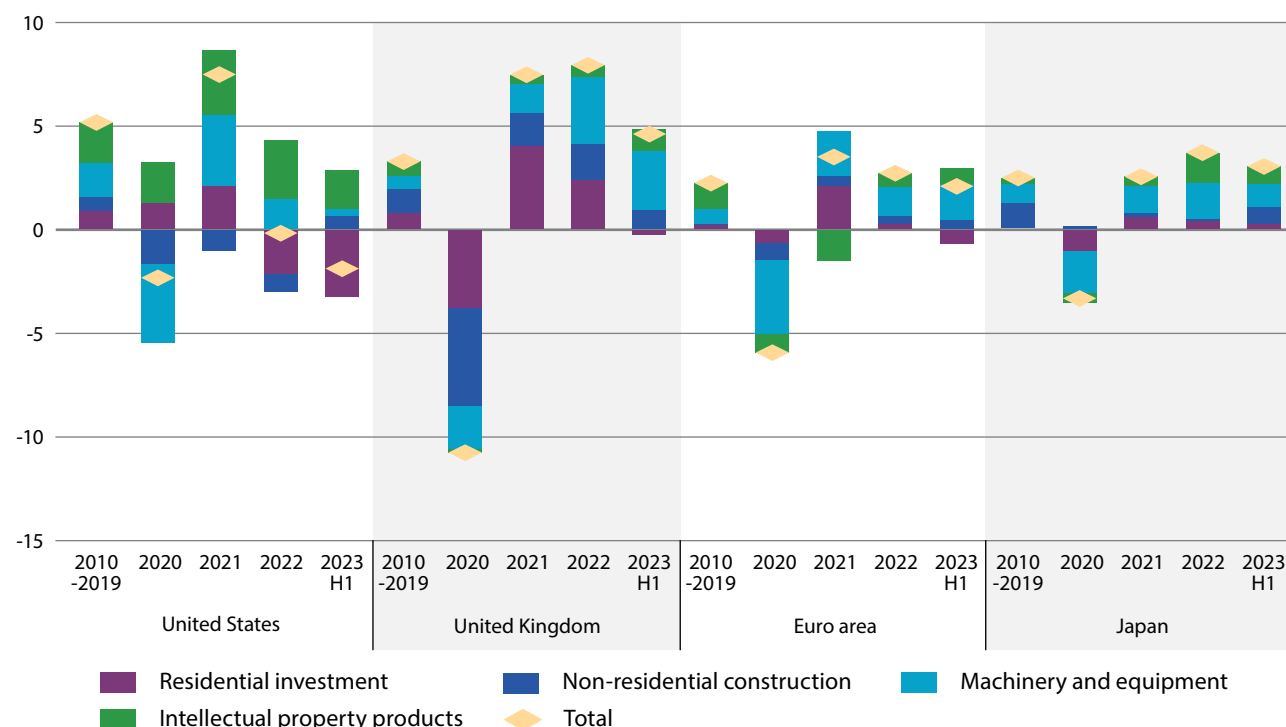
Demographic shifts, economic development patterns, technological advances as well as multiple crises are reshaping labour markets. Between 2000 and 2023, the total world population increased from 6.1 billion to 8 billion.¹⁹ While many regions, including Europe, North America and East Asia, face ageing populations, a rapidly growing youth and working-age population challenges policymakers to generate enough productive jobs, particularly in South Asia and sub-Saharan Africa. Historically, countries shifted from low-productivity agriculture to higher-productivity activities in industrial or services sectors during the process of structural transformation. More recently, in many low-income countries, the contribution of agriculture to GDP has declined faster than the share of workers in agriculture, while the manufacturing sector has not absorbed many workers²⁰ (see also chapters III.B and III.G). Labour productivity growth has been on a downward trend across country income groups (figure II.12), which can be partly attributed to weaker investment and—for many developing countries—diminishing productivity gains from allocations of labour towards more productive sectors.²¹ In addition, limited employment opportunities in the formal sector and the absence of unemployment benefits in many developing countries have contributed to widespread informal employment, which is typically associated with poor working conditions, limited access to social protection and little or no income security.

Rapid technological change could bring further disruptions while also creating new job opportunities (see also chapter III.G). When firms adopt new methods of production, workers with low-skilled jobs

Figure II.11

Annual investment growth in selected developed economies, by asset type, 2010–2023H1

(Percentage)



Source: UN DESA calculations based on data from CEIC and Eurostat.

Note: H1 = first half of the year. Figures are in constant prices. Data for the United Kingdom, euro area and Japan is total investment; data for the United States is private investment.

engaged in routine tasks are often put at risk, as these occupations are most susceptible to automation. The launch of ChatGPT in November 2022 marked the beginning of a new era for AI, which may accelerate the substitution of some lower- and medium-skilled jobs but complement and augment the work of high-skilled professions.²² The asymmetric effects of AI across the skills spectrum could increase income inequality in the labour market. Women could be particularly adversely affected since they are overrepresented in occupations with higher risks of automation, although female-dominated occupations also have more potential to be complemented by technology.²³ The net effect of AI on labour market inequality will depend on the management of this transition and whether the shift leans more towards automation or augmentation.

7. Climate risks and the global economy

The climate emergency and related extreme weather events have brought considerable economic and social costs, disproportionately affecting the most vulnerable countries and communities.

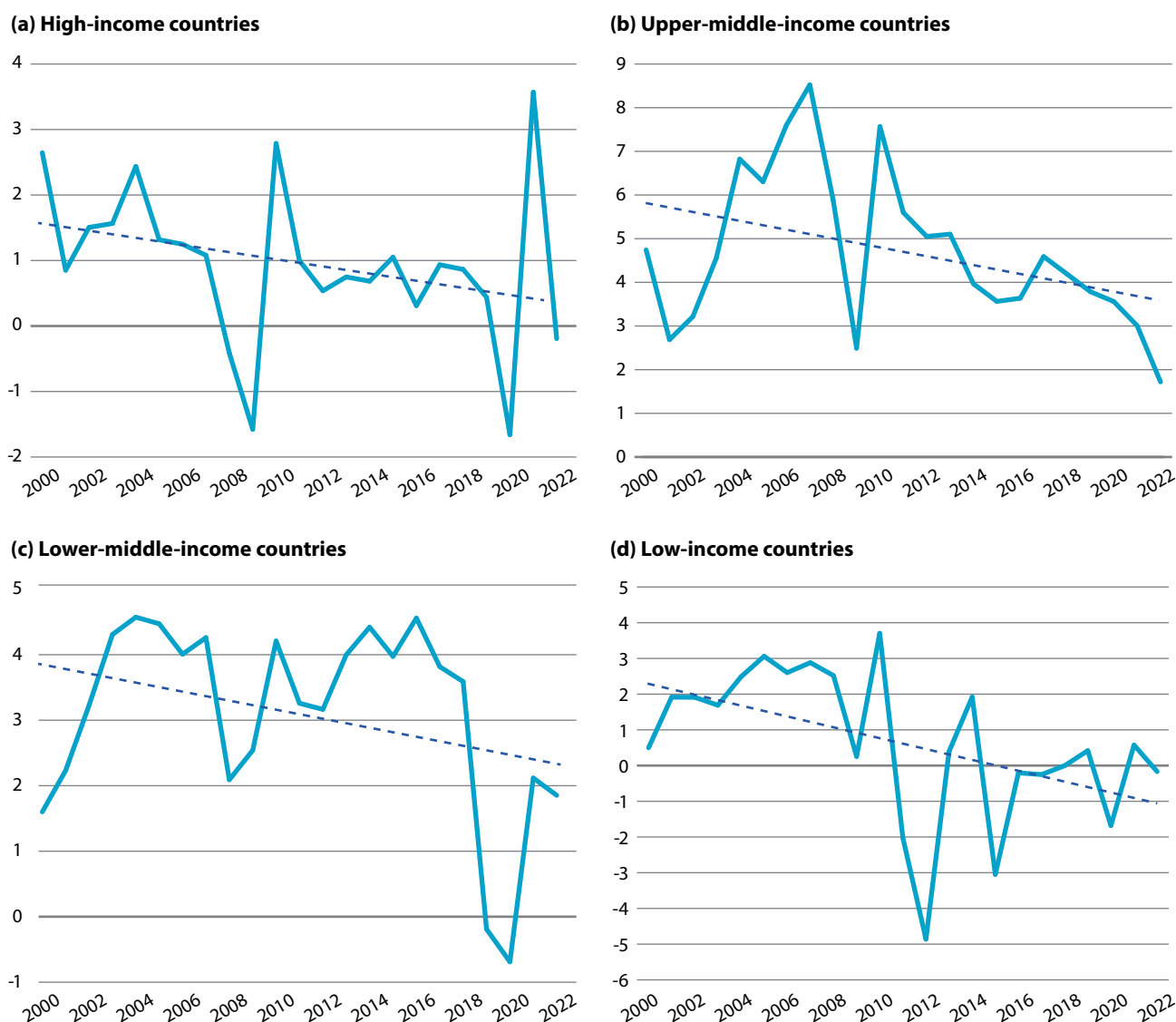
Extreme weather events have occurred more frequently over the past few decades, while their economic and social impact has become increasingly more pronounced. The number of disasters increased from an annual average of around 310 from 2000 to 2020 to over 340 between 2020 and

2023.²⁴ The year 2023 saw a surge in extreme weather events and the hottest summer since global records were first kept in 1880.²⁵ These extreme weather events exact a significant human and economic toll: Between 2000 and 2023, about 2.6 per cent of the global population lost their lives, were injured or became homeless due to climate disasters, including 3.2 per cent of the population in low-income countries, compared with 0.5 per cent in high-income countries (figure II.13a). An additional 68 million to 135 million people could be pushed into poverty by 2030 because of climate change.²⁶ Global annual economic damage from disasters amounted to over \$173 billion between 2020 and 2023, up from an annual average of \$108 billion during the first decade of the century (figure II.13b).

SIDS have been particularly vulnerable. From 2010 to 2019, SIDS suffered losses of \$94.3 billion due to weather, climate and water-related hazards, compared to total SIDS GDP of \$874 billion in 2019.²⁷ Climate vulnerability is also linked with higher borrowing costs and—when countries are hit by extreme weather events—weaker recovery (see chapter III.E). Disruption to economic activities and livelihoods and damages to infrastructures affect countries' ability to mobilize domestic and external resources and elevate creditors' perception of country risks, which translate into even higher borrowing costs and debt vulnerability.

While climate change impacts are increasingly macro-relevant, global macroeconomic conditions in turn affect the ability of countries to invest in climate mitigation and adaptation. Many

Figure II.12
Labour productivity growth, by country income group, 2000–2022
 (Percentage)



Source: UN DESA calculations based on data from ILO STAT (accessed on 30 December 2023).

Note: A linear trend line is added on each panel.

countries have increased their investment in renewable energy to reduce carbon emissions; however, these actions are not yet sufficient. In 2023, global investment in renewable power generation reached \$658 billion, almost double the investment of \$331 billion in 2015. Developed countries and China accounted for 90 per cent of this increase. China alone was responsible for 41 per cent of global investment in renewable energy in 2023, with all other developing countries accounting for only 16 per cent. Increased investment in renewables does not, however, indicate a reduction of investment in fossil fuels: Investment in fossil fuels has rebounded in recent years, surpassing pre-pandemic levels in 2022 and 2023. Global coal production has surged due to its much lower capital intensity compared to oil and gas.²⁸ High interest rates and increased capital costs discourage

investments in green transitions, as they make financing capital-heavy renewable energy projects costlier, thereby diminishing their appeal relative to more affordable, non-renewable alternatives. This can slow down the shift towards sustainable energy solutions.

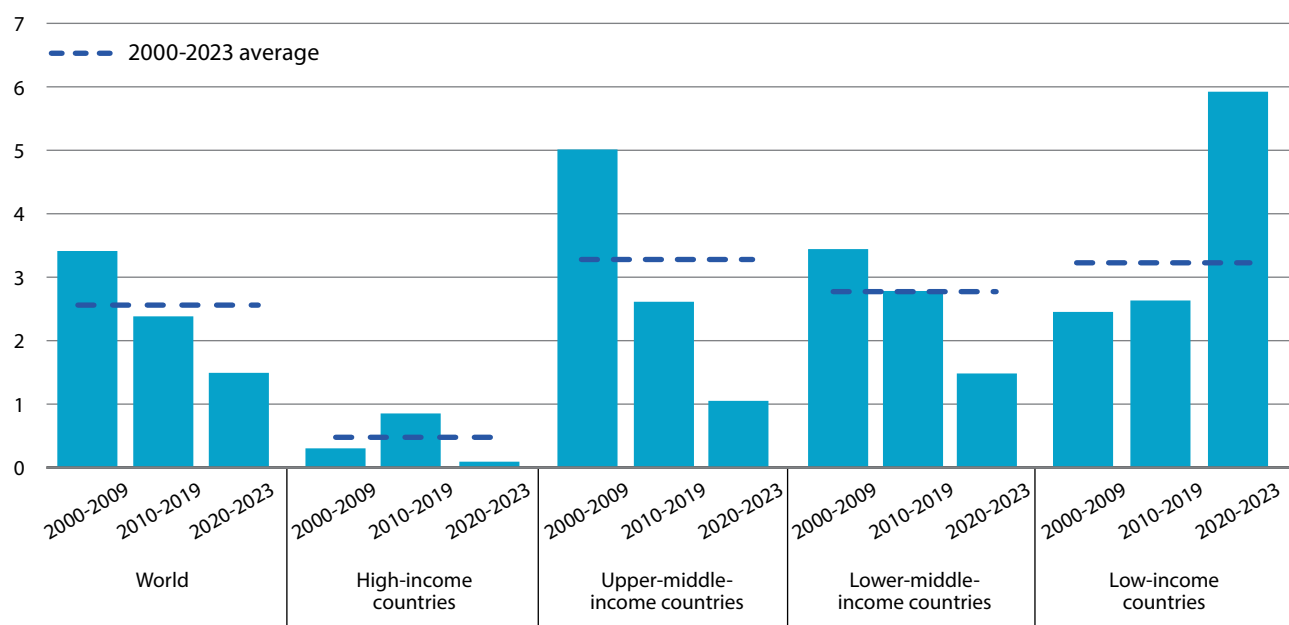
8. Conclusion

The global economy has become progressively less “enabling” for mobilizing financing and investment for development over the past 25 years. The financing for development outcomes recognized the critical role that an enabling international economic environment plays in

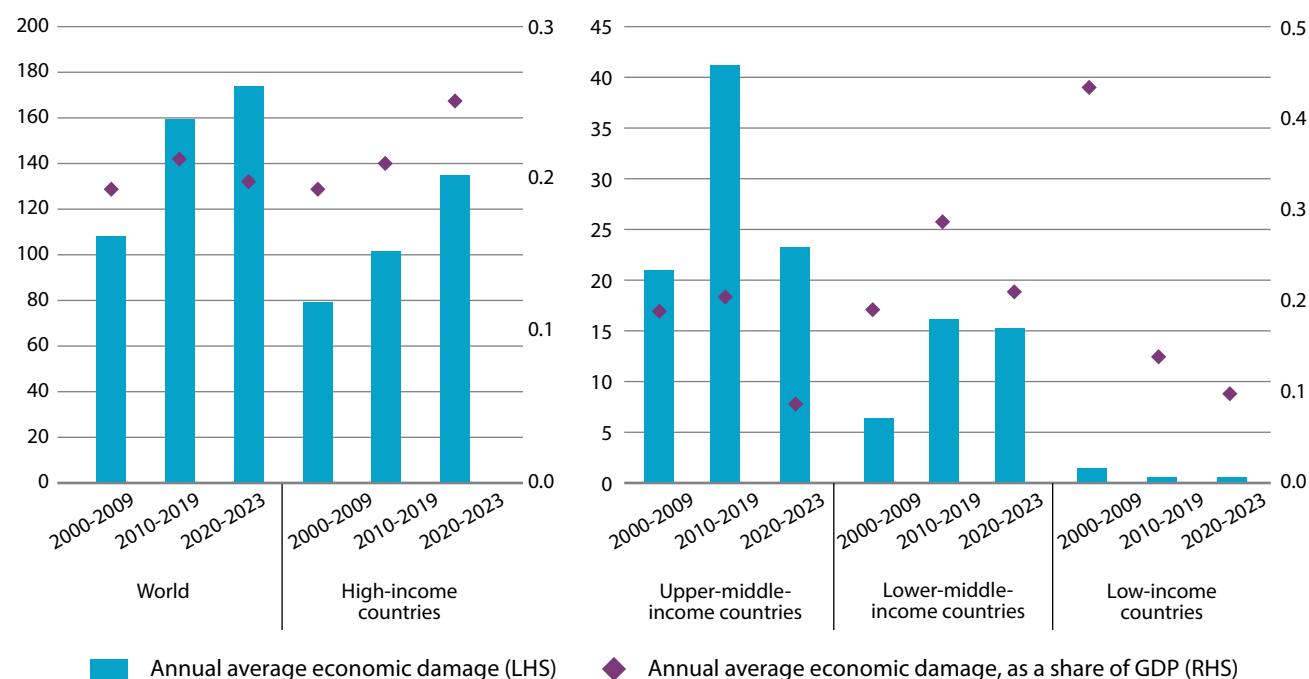
Figure II.13

Economic and social costs of natural disasters in the world, by country income groups, 2000–2023**(a) Annual average share of people affected by natural disasters**

(Percentage)

**(b) Annual average economic damage caused by natural disasters**

(Billions of United States dollars, Percentage)

**Source:** UN DESA calculations based on the International Disaster Database (accessed on 24 December 2023).**Note:** Natural disasters include drought, extreme temperature, flood, glacial lake outburst flood, storm, and wildfire.

achieving development outcomes. The subsequent chapters of this report will show how the major crises in 2008/09 and since 2020—and the broader deceleration in global growth and investment—have significantly impeded the mobilization of public and private resources. This is mirrored in less dynamic trade and cross-border investment trends, contributing to a less benign economic environment.

Improving this global enabling environment will be a central challenge in the pursuit of the SDGs and energy transitions.

Achieving the SDGs and the large-scale transitions needed to avoid catastrophic climate change will require investments at unprecedented scale. Such an investment push is not conceivable unless countries and the

international community as a whole find ways to address key macro-economic challenges and constraints, which include deteriorating public finances, fiscal constraints and debt overhangs in many developing countries, monetary and financial stability risks that impact the cost of capital, and the dearth of productive and sustainable investment that is crucial for improving longer-term growth and resilience to climate and other adverse shocks. Proposals put forward in the rest of this report aim not only to advance implementation of the respective action areas, but also to form a package of domestic reforms and reforms to the international financial architecture that together could help steer the post-COVID-19 economy towards a path of sustained, sustainable and inclusive growth.

Endnotes

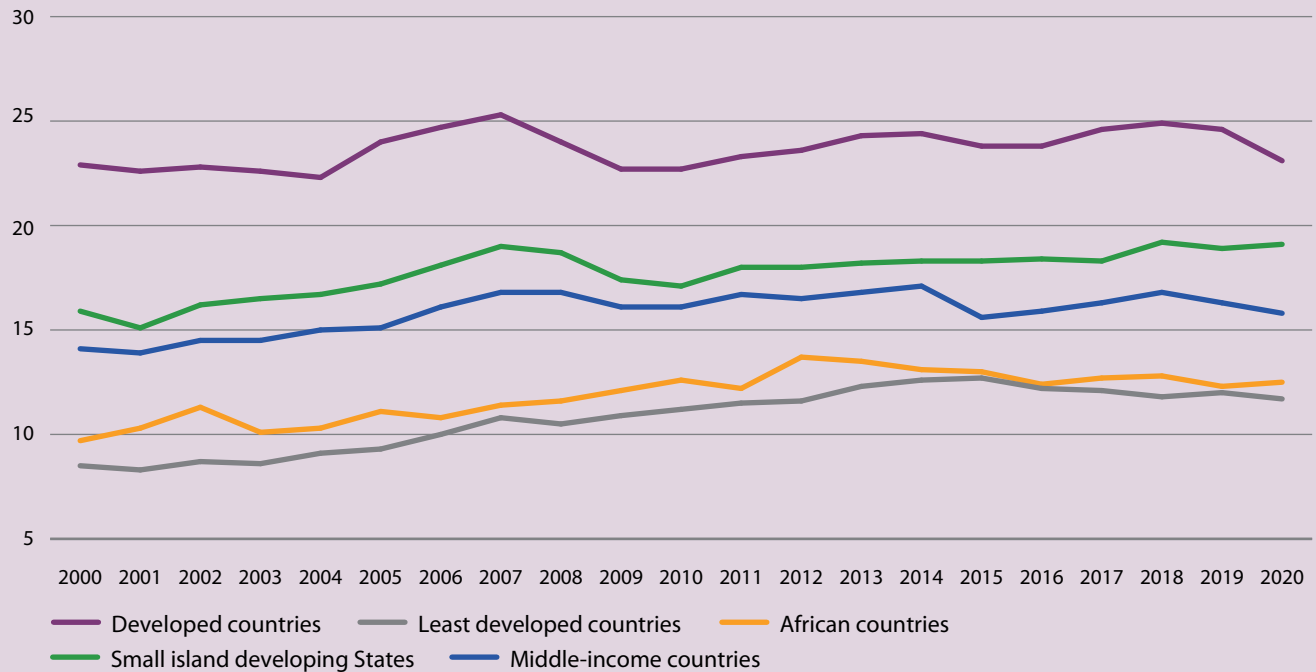
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- 3 If indirect COVID-19 induced deaths are considered, the total death toll could range between 18.2 and 33.5 million (The Economist, 2023). <https://www.economist.com/graphic-detail/coronavirus-excess-deaths-estimates>.
- 4 Bolhuis, M. A., Chen, J., & Kett, B. (2023, June). The costs of geoeconomic fragmentation. *Finance and Development*, June 2023, 35.
- 5 An important infrastructure challenge is the inadequate coverage of power grids in developing countries, including LDCs, LLDCs and SIDS. Resources are critical for developing countries to build or modernize their electricity grids, which could help expand the access of their population to ICT and reduce the digital divide within countries (e.g. rural-urban divide) and between countries.
- 6 Data source: <https://pip.worldbank.org/home>.
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- 12 Quantitative easing, also known as QE, involves central banks buying assets from the financial sector, particularly asset-backed securities, and government bonds, to inject liquidity into the banking system.
- 13 The Bank of England started hike policy rates in December 2021, while the Federal Reserve and the European Central Bank started in March and July 2022, respectively.
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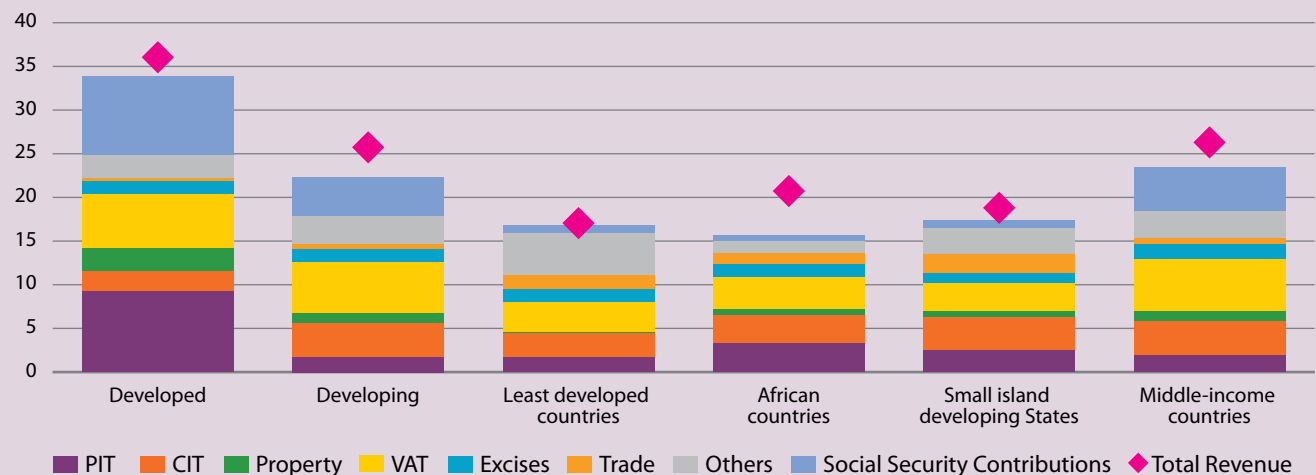


Domestic public resources *in numbers*

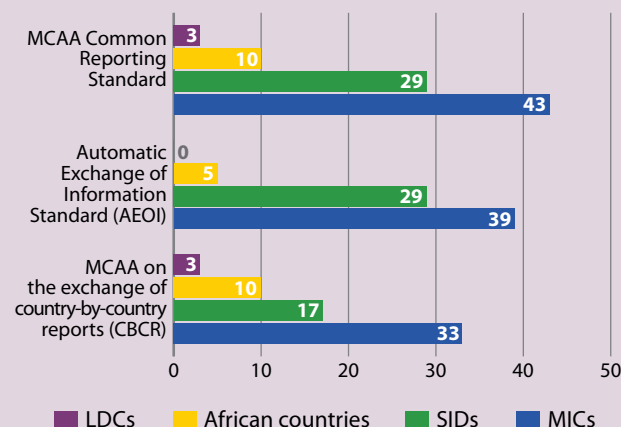
Developing countries achieved notable increases in tax revenue in the first decade of the century, but have seen stagnation and setbacks by crises.



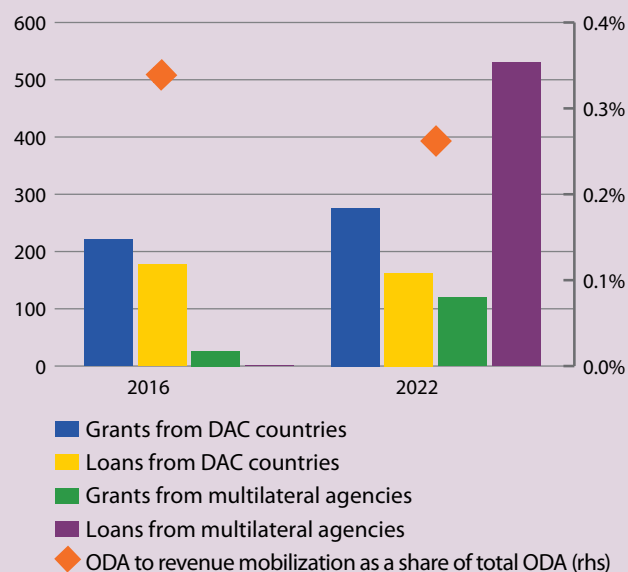
Developing countries are more dependent on consumption taxes and corporate income taxes, accounting for 5.8% of GDP and 3.9% of GDP, respectively.



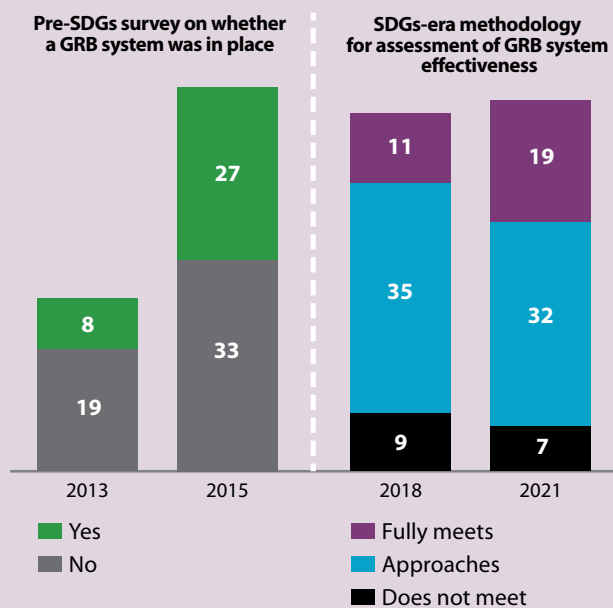
Only three LDCs have signed on to important tax information exchange agreements, and none of them are yet automatically receiving information on financial accounts.



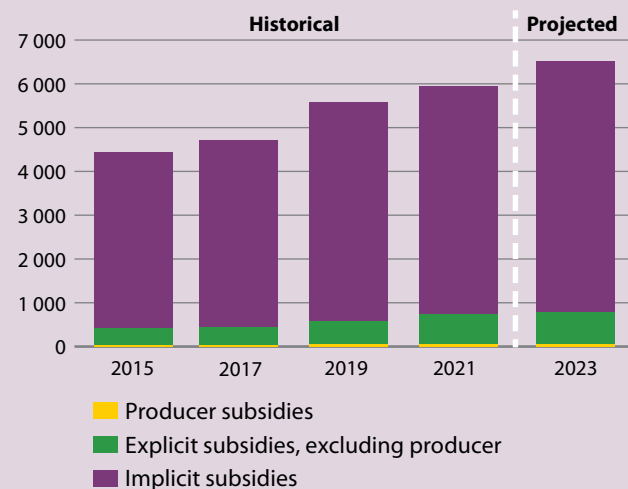
Disbursements of ODA for domestic revenue mobilization fell short of donor targets to double by 2020 but hit \$437 million in 2022.



Globally, only one in four countries currently has a comprehensive gender responsive budgeting system.



Estimated global fossil fuel subsidies were \$7 trillion in 2022, including \$1.3 trillion in explicit subsidies.





Chapter III.A



Domestic public resources

1. Key messages and recommendations

Domestic public resources—and the mobilization of additional tax revenue in particular—have become a progressively more central aspect of the deliberations by Member States on financing for development.

Domestic public finance is essential for financing the Sustainable Development Goals (SDGs), increasing equity and helping to manage macroeconomic stability. Robust and resilient fiscal systems, including both tax and expenditure, can contribute to alleviating poverty and reducing inequalities while supporting economic growth, industrial transformation and environmental sustainability. The Monterrey Consensus and Doha Declaration grouped together domestic public and private resources under the heading of “Mobilizing domestic financial resources for development”, with international tax cooperation only briefly mentioned. The Addis Ababa Action Agenda, in contrast, dedicates its first action area exclusively to domestic public finance. It endorses a whole-of-government approach that includes increasing the quantity of resources, enhancing the quality of expenditures, and ensuring that both are done fairly and sustainably. It presents extensive commitments and a discussion of international tax cooperation and measures to combat illicit financial flows (IFFs). In short, it reflects the growing understanding among Member States about the importance of building the overall capacity of the State using domestic resources, and the positive implications this has for bolstering trust in government, strengthening the social contract and delivering public goods and services critical for poverty eradication and economic transformation.

There has been a notable but uneven increase in tax revenue in developing countries since 2000, with most of the gains concentrated in the decade before the 2008 world financial and economic crisis.

A myriad of crises over the last two decades—including economic crises, pandemics, geopolitical conflicts and

disasters—has had a major effect on the mobilization of domestic resources for development. After significant increases in taxation in developing countries in the decade before 2009, the record has been mixed, with the COVID-19 pandemic halting momentum gained by the renewed attention on improving tax systems in the Addis Agenda. The setbacks from exogenous shocks are expected to increase as crises become more frequent and intense with impacts on social, economic and environment stability from the changing climate.

Despite the progress made, there remains a large unmet tax potential in developing countries and a pressing need to reform fiscal systems to tap that potential and generate resources on the scale required for achieving the SDGs. Expanding tax capacities to raise revenue for funding public goods and services is primarily a domestic challenge and will require the political will to both overcome entrenched interests that benefit from current systems and increase investment in tax capacity. There are many examples of governments that have invested in tax reforms, demonstrating the possibilities of countries realizing unmet potential. So far, however, political will has been found wanting in many countries, including developing countries not investing enough in tax system reform and administration capacity, and donors not delivering the volumes of assistance they pledged to provide for supporting revenue mobilization. The Fourth International Conference on Financing for Development should consider how to turn commitments for domestic tax reforms into actions to make tax systems more fair, transparent, efficient and effective.

Building tax capacity—the policies, institutions and technical capabilities to collect tax revenue—is indispensable and urgently needed for strengthening the ability of governments to deliver

sustainable development. To respond to SDG investment needs and external challenges, countries need to build strong and resilient fiscal systems, including diversification of revenue sources and measures to combat illicit financial flows (IFFs). Countries with weak fiscal policies and institutions, low buffers, high levels of informality and low tax capabilities will continue to find it difficult to support the investment needed to deliver on the SDGs. When taxpayers contribute to society and governments combat corruption and provide valuable public goods and services in return, a virtuous circle can be sustained: investment in tax capacity supports increased spending on public goods and improved services, which contributes to voluntary compliance by taxpayers. New digital technologies have helped tax authorities to step up their efforts to better govern revenue systems, prevent some types of tax evasion and improve relationships with taxpayers, with the lessons learned from early adopters available to help others rapidly improve their systems. By building trust through effective governance of revenue and expenditure systems, governments will also be better able to realize other public policy goals.

Globalization and digitalization have fundamentally altered the taxation landscape, motivating some of the increased focus on international taxation in the financing agenda.

Globalization and long-term changes in the structure of economies have challenged the effectiveness and efficiency of revenue mobilization systems, requiring shifts in the design of tax policy and administration. Tax systems mostly rely on combinations of taxation on labour, capital and consumption. Over the last 20 years, developing countries have been squeezed between their relatively less formalized economies and thus smaller tax bases, declining tariff revenue due to trade liberalization, and competitive pressure to lower corporate taxes to attract private investment. To mobilize sufficient revenue, many countries turned to consumption taxes, which can be regressive; some countries managed the equity implications better than others. Globalization and financial liberalization also increased the pressure on countries to decrease corporate or wealth taxation over time by making it easier for businesses and individuals to shift profits and assets to other jurisdictions, a challenge which is particularly acute for poorer countries. The efforts to constrain harmful tax competition and combat tax evasion and avoidance have prompted much of the attention paid to advancing international tax cooperation.

Since 2015, attention has shifted dramatically towards multilateral tax cooperation instruments, transforming the international tax cooperation landscape and enabling progress on combating tax avoidance and evasion, but also risking leaving a subset of countries further behind. Discussions to update international tax norms and promote international tax cooperation are an essential complement to the primarily domestic efforts to boost tax capacity. When the Addis Agenda was agreed, few multilateral tax agreements existed; bilateral relationships and agreements were the dominant form of international cooperation. Since 2015, exchange of information on request for tax purposes has blossomed, several multilateral legal agreements have been concluded, and important tax transparency instruments have been implemented through the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum). The automatic exchange of information (AEOI) on financial accounts, which began in 2017, and the country-by-country (CbC) reports of multinational enterprises (MNEs), which began in 2018, have provided an abundance of information for those tax administrations that receive them, but most developing countries lack

access to and the ability to use the information. Work to address the challenges from globalization and digitalization has been ongoing for more than a decade at multiple venues. A pioneering effort to introduce a global minimum corporate tax is being implemented, but other work has yet to yield policy results that sufficiently address tax avoidance and evasion and that have the full support of all Member States. There remain concerns about the inclusiveness and effectiveness of existing international tax cooperation mechanisms, including the suitability of new global norms for developing countries with lower capacity tax administrations. The Fourth International Conference on Financing for Development is an opportunity for the world's political leaders, in a fully inclusive forum, to confirm the future direction and governance of international tax cooperation.

Efforts to coordinate internationally to ensure adequate domestic expenditure on agreed international goals have often faltered, including due to a lack of ownership of international targets, challenges from the political economy of policies (particularly fossil fuel subsidy reform) thought to hurt the poor and middle class, and a lack of political will to change expenditure systems where powerful domestic interests may be benefiting from the current system.

Since 2000 there has been an increasing focus on carbon pricing, reforms to fossil fuel subsidies and incentives for green energy/industry. However, the commitment in the Addis Agenda to phase out harmful fossil fuel subsidies remains largely unfulfilled, with implicit and explicit subsidies growing over time. Similarly, increased spending on gender equality and women's empowerment and universal social protection floors has been routinely supported rhetorically, but implementation in practice has lagged behind. The international community could consider how a Fourth International Conference on Financing for Development can add further momentum to aligning expenditure with the SDGs and support fiscal policies to reduce inequalities.

National development banks (NDBs) are increasingly seen as a critical part of the global financial system and an important tool for ensuring financing for countries' sustainable development priorities. Coordination and networking among public development banks (PDBs) has grown enormously since the agreement on the Addis Agenda, which highlighted the role of NDBs. The international community could consider how a new international agreement could build on progress in cooperation and coordination of the entire system of PDBs to increase their impact.

This chapter provides a brief overview of revenue trends in the past two decades and discusses how countries can use tax policies and tax administration to realize greater resources for investment in the SDGs. It then presents developments in international tax cooperation and progress in combating IFFs. Lastly, the chapter looks at SDG-related expenditure and investment, including gender-responsible budgeting (GRB), fiscal responses to climate change and national development banks.

2. Domestic resource mobilization

2.1 Revenue trends

Tax-to-GDP ratios are directly related to development levels, as countries with larger economic output and stronger institutions,

with few exceptions, have been able to mobilize more tax revenue. The Addis Agenda recognizes that domestic resources are first and foremost generated by economic growth, and empirical evidence shows that the tax base naturally expands as economies grow. Both the Doha Declaration and the Addis Agenda include commitments to enhance tax revenue mobilization and the efficiency of the tax system while making it more progressive. Beyond its fiscal function, tax capacity is associated with accelerated growth and better institutions, as countries with more revenue can invest in better public service delivery, thus increasing trust in the State and strengthening the social contract which feeds back into higher capacity to mobilize revenue in the future.¹

There has been a notable but uneven increase in tax revenue in developing countries since 2000, with particularly significant increases in the first decade before the 2008 world financial and economic crisis. Median tax revenues increased steadily in most categories of countries and regions until setbacks from the 2008 crisis and the onset of the COVID-19 pandemic in 2020 (figure III.A.1). Analyses of long-term trends in revenue mobilization have shown that two thirds of countries experienced improvements of tax-to-GDP ratios in the first decade of the century.² Many of the episodes of rapid increases in tax revenue mobilization were in countries that simultaneously embarked on revenue administration and tax policy reforms in parallel.³

Revenue gains, however, have been volatile, with both year-to-year volatility and medium-term increases and declines. In some cases, macroeconomic factors created volatility, such as financial crises and the COVID-19 pandemic, although the pandemic did also motivate an acceleration in digitalization of revenue administrations which could spur long-term improvements in revenue mobilization.⁴ For countries heavily dependent on commodities-related revenue, commodity cycles have contributed to both increases but also regressions in revenue mobilization; commodity dependence may also indirectly contribute to revenue volatility because governments in these countries have lower incentives to invest in revenue administration.⁵ Only a fraction of countries saw rapid revenue gains that were sustained over time; more frequently, countries with moderate revenue gains were able to sustain reforms and further increase revenue in subsequent periods.⁶ This suggests that expectations for rapid and sustained revenue increases in a large number of countries may be over-optimistic. There is also evidence that high-level political commitment and buy-in from all stakeholders plays a role in sustaining efforts to increase revenue.⁷

2.2 Tax policies: The changing tax mix and impact on revenue levels

There has been a global shift in the tax mix over the past several decades, with implications for the ability to raise revenue, reduce inequality and enhance revenue mobilization. Each country has a unique tax mix depending on its economic, political and social structures as well as the historical development of the State and its institutions. Yet global competition and the international environment can also drive common movements. Prior to the new century, developing countries were much more reliant on trade taxes; they have since shifted to greater dependence on consumption taxes and corporate income taxes. In contrast, developed countries liberalized their trading systems much earlier, and with more formalized economic systems, rely strongly on personal income

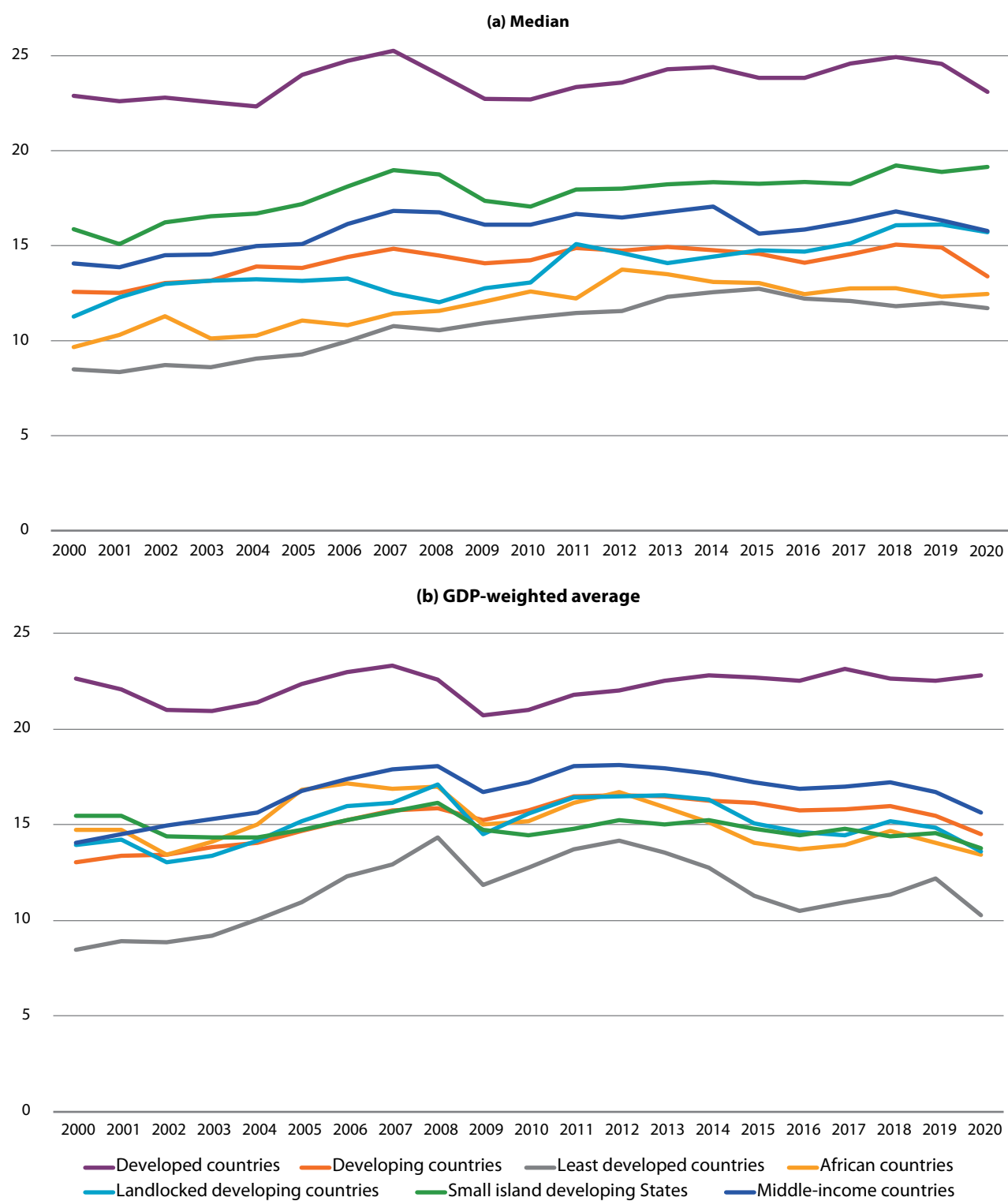
taxes and social insurance contributions to fund their public goods and services and social protection systems, respectively.

Revenue increases require strengthening the design and administration of core taxes—value added tax (VAT), excises and personal and corporate income taxes—with a focus on tax base broadening and combating tax avoidance and evasion. Core taxes make up the bulk of tax systems in all country categories (figure III.A.2). Countries can choose a tax mix that is compatible with their economic structure and also satisfies their political settlement. One perennial challenge is balancing incentives and achieving political agreement on tax base widening, which often has diffuse gains over all taxpayers but concentrated costs for those brought into the tax net or those losing the benefit of tax expenditures. Most countries also have scope for ending preferential tax rates on capital income and for better use of real property taxes.

VAT is central to revenue mobilization in developing countries, but exemptions and reduced rates erode its performance while its equity implications need to be better addressed. Taxes on consumption have spurred revenue growth in developing countries over the last few decades. A well-designed VAT is an efficient revenue instrument because its distortive effect on economic activity is minimized per dollar of revenue raised. However, VAT is regressive because of the higher share of income that is spent on consumption by poor households. In a bid to alleviate regressivity, VAT exemptions and reduced rates on essential goods are frequently used, but these measures can benefit high-income households more. Instead, the regressivity of VAT should be considered in the context of the overall tax and spending system as well as the overall tax policy mix, with increased revenue being used to finance social protection systems that support low-income households. Tax policymakers and administrators can adjust VAT design and implementation in response to changing circumstances, for example by ensuring equitable taxation on digital goods and services, including those delivered cross-border, to level the playing field with other businesses. In addition, several developing countries are collecting significant additional revenues through digital services taxes.⁸

Corporate income tax (CIT) is an important source of revenue in low-income countries, accounting for a larger share of revenue than in developed countries, where corporate tax rates have been consistently declining for many decades. Statutory CIT rates have been decreasing on average over the last two decades, although considerable variation among jurisdictions remains (figure III.A.3).⁹ The global average combined (central and subcentral government) statutory tax rate was 21.1 per cent in 2023, compared to 28.2 per cent in 2000. Of the 141 jurisdictions covered in the 2023 data, 27 had corporate tax rates equal to or above 30 per cent in 2023. At the same time, globalization and aggressive structuring of cross-border transactions have resulted in large portions of the CIT base being shifted to low- and no-tax jurisdictions. Nonetheless, CIT revenues increased from 2000 to 2020 on average, both as a share of total tax revenues and as a percentage of GDP. In some countries this reflects the rising profit share in national income while in others, it reflects the increase in the corporate tax base. Developing countries are much more reliant on CIT revenue, with average CIT revenue as a share of total revenue between 15 per cent and 20 per cent across Latin America, Africa and the Asia-Pacific region, while the average revenue share for Organisation for Economic Co-operation and Development (OECD) countries was less than 10 per cent.¹⁰

Figure III.A.1
Tax revenue, by country groups, 2000–2020
 (Percentage of GDP)



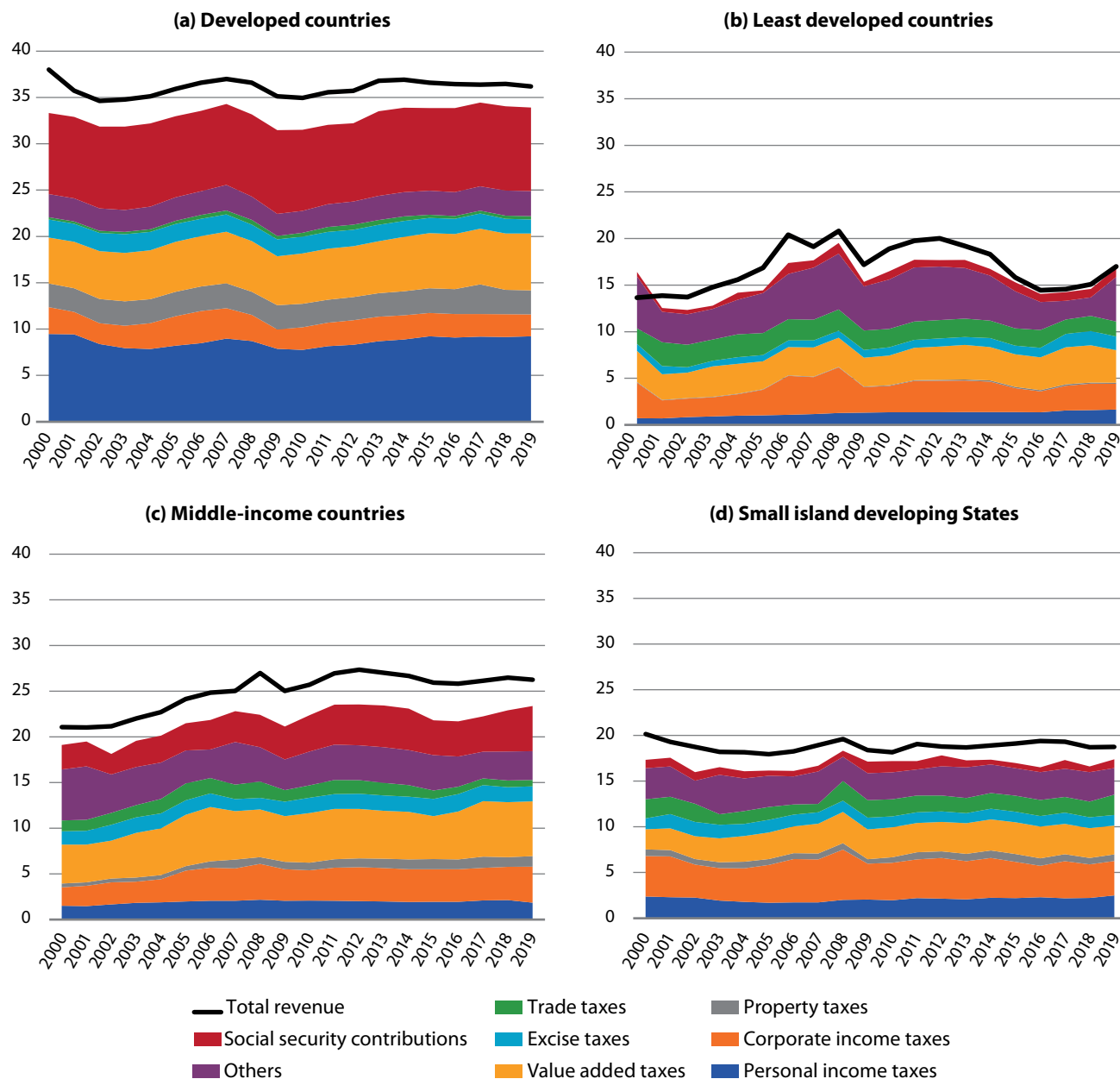
Source: UN DESA calculations based on IMF data.

Note: General government tax revenue as a percentage of GDP, M49 groupings.

Figure III.A.2

Composition of revenue systems, by country group, 2000–2019

(Percentage of GDP)

**Source:** UN DESA calculations based on IMF data.**Note:** GDP-weighted averages of revenue shares for countries with data available in the specific year.

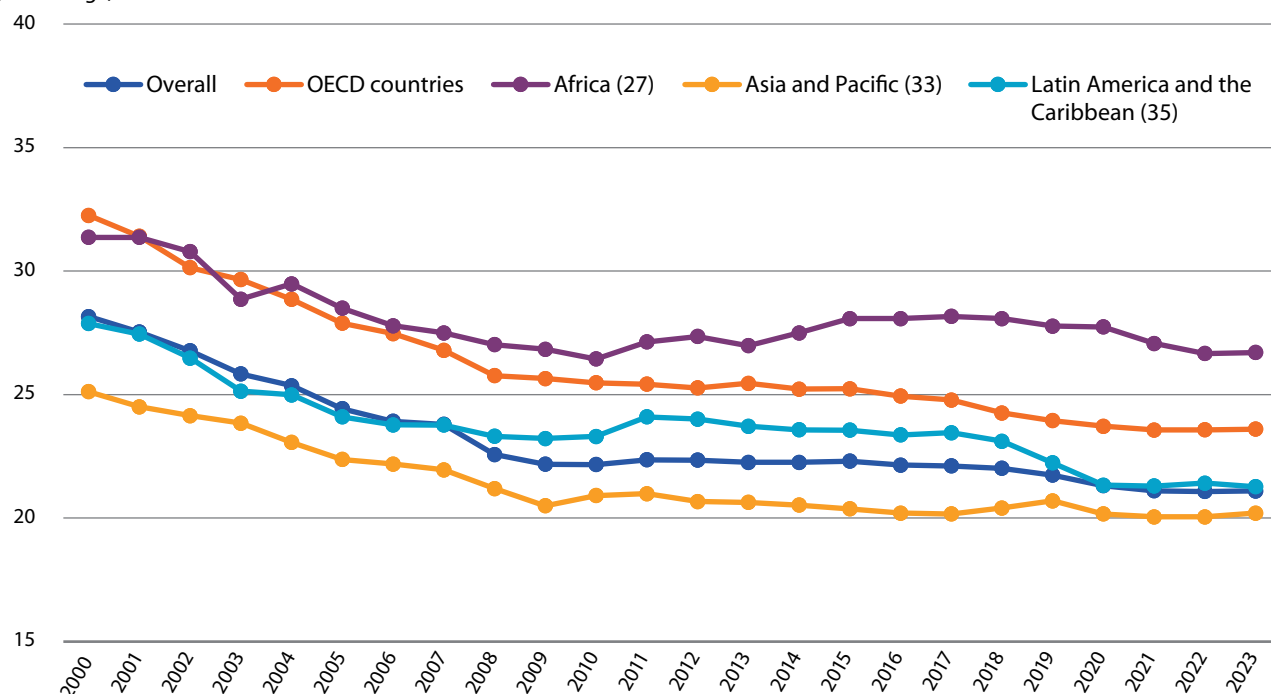
Taxing wealth and real property could generate additional revenue and be redistributive. Property taxes are widespread in developed countries and are a small but increasing source of revenue in developing countries (figure III.A.2, panel b). The immovable nature of real property makes taxes on these assets relatively easy to collect once the appropriate administrative infrastructure is in place (namely, a cadastre and property valuation systems). Because property taxes are mostly redistributive and economically efficient, they can be important elements of progressive tax systems. As they have historically been assigned to local governments,

recurrent property taxes can also be a tool to strengthen subnational fiscal capacities and their provision of infrastructure and services as well as improve their coordination with central fiscal authorities.¹¹ There is also growing discussion of net wealth taxes, which can be feasible with sufficient political will and where tax administrations have sufficient capacity and access to information. Countries may wish to start by strengthening policy on and administration of capital income taxation, including taxing capital income at the same rate as income from labour in order to reduce both inequalities and opportunities for tax avoidance.¹²

Figure III.A.3

Average statutory corporate tax rates, by region, 2000–2023

(Percentage)



Source: OECD.

Note: Numbers in brackets indicate number of countries in the sample.

Commodity exporting developing countries exhibit strong dependence on revenue related to natural resource extraction; transparency and accountability has increased over the decades but remains a challenge. On average, cross-country analysis shows that natural resource revenue exhibits an almost one-for-one trade-off with the development of other tax revenue and that countries with high resource revenue invest little in tax institutions and tax capacity.¹³ Aside from environmental risks, the sector presents concentrated risks for corruption, profit shifting and IFFs, which can be countered with effective public policies. The Doha Declaration introduced a reference to the Extractive Industries Transparency Initiative (EITI) which seeks to strengthen public and corporate governance and accountability in the sector. The EITI strengthened its monitoring of implementation by its members over 20 years, and almost all have improved compliance.¹⁴ There remains space for improving the design of natural resource fiscal regimes by using profit and rent taxes together with royalties in a progressive way.¹⁵

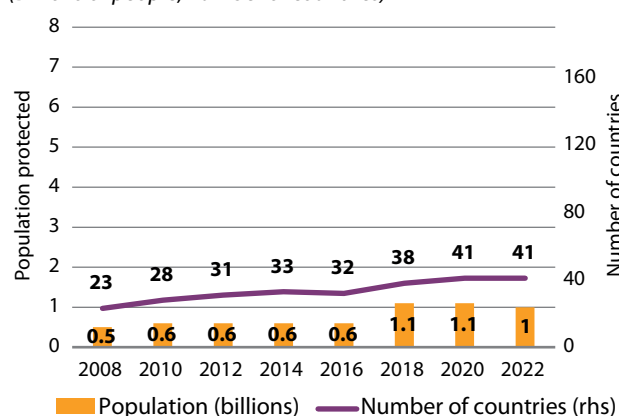
Trade taxes had been an important but declining revenue source in developing countries, while excise taxes could be used to raise revenue and change consumer behaviour in ways that promote SDG achievement. While trade taxes (tariffs) have declined in prominence as trade liberalization was pursued in the late 1990s and early 2000s, they remain important in countries in special situations (figure III.A.2 panels c and d). The shift in revenue from trade taxes to domestic taxes such as VAT has slowed over the past two decades.¹⁶ At the same time there has been an increase in the use of domestic excise taxes in developing countries, for example on fossil fuels, tobacco, alcohol,

sugar-sweetened beverages¹⁷ and plastic bags. The Addis Agenda includes specific recognition of the role of tobacco taxes, and now 41 countries have excise and other taxes on tobacco that are more than the World Health Organization (WHO) recommended level of 75 per cent of the retail price (figure III.A.4).¹⁸ There is room to increase excise revenues through better design and consistent applications across taxpayers, as well as strong potential for using them to help address climate change (see below) and other sustainable development priorities. The Fourth International Conference on Financing for Development could build on recent country experiences and provide a platform for discussion on how to use excise and other taxes to set incentives that change behaviours.

2.3 Tax administration: Digitalization, enforcement and cooperative compliance

Modern revenue administrations maximize revenue mobilization and voluntary compliance with an integrated, holistic approach combining preventive, detective and corrective actions. Strengthening the institutions tasked with collecting revenue is vital for building tax capacity. Tax administrations are a key governmental contact point, and thus shape the citizen-State relationship. Perceptions of the legitimacy of the tax administration impact on the willingness to pay tax, emphasizing the importance of the social contract and moving beyond audit to holistic tax administration that addresses trust, ease of compliance and quality of service alongside the risk of audit and enforcement.¹⁹ Digitalization can ease compliance for taxpayers and deliver high-quality service. Use of third-party data can both improve ease of compliance as

Figure III.A.4

Countries with recommended levels of tobacco taxation, 2008–2022*(Billions of people, number of countries)***Source:** WHO.**Note:** Based on number countries with total tax on cigarettes $\geq 75\%$ of the retail price.

well as strengthen risk management, and capacities in this regard will be essential for effective implementation of international tax transparency mechanisms. These approaches require capacities and resources to access and productively use data. Using data to target enforcement towards high-risk cases—so called compliance risk management—can also bolster perceptions of fairness. In addition, there should be close cooperation and exchange of information between tax and customs administrations, regardless of whether they are fully separate institutions or are part of integrated revenue administrations. Increased revenue, including from changes to international tax norms, will only flow with investment in strong capacities.

Revenue administrations need sufficient funding and autonomy to ensure adequate performance. Attracting and retaining the best staff with the highest integrity standards lies at the heart of an effective revenue administration. Sufficient funding also needs to be provided for technology usage and implementation of digitalization. Political interference in revenue administration will undermine perceptions of fairness and produce opportunities for corruption. Assessing progress in tax administration performance is challenging as there is limited long-term comparative data on investment in tax administration and its effectiveness. However, since 2016, the International Survey on Revenue Administration (ISORA) has collected annual data on tax administration operations and other characteristics, with more than 150 tax administrations now participating.²⁰ Comparisons across countries remain difficult given differences in economic structure, institutional design and decentralization.

Greater digital adoption in revenue administrations is associated with higher domestic tax revenue collection and reduced compliance gaps. ISORA data shows that developing countries have lower levels of electronic filing of tax returns, pre-filing of tax returns and online payments, but gaps with developed countries are closing (figure III.A.5). Research consistently shows that greater digital adoption in tax administration is associated with larger tax revenue collection, and especially that strategies that mandate use of digital filing can increase revenue by up to 5

percent of GDP.²¹ Large gains are much more likely when complementary factors for digital administration are present, for example reliable Internet connections, experienced tax administration staff and sufficient information and communication technology expenditure by the tax authority.

Electronic invoices are an example of a digital tax administration tool that enhances revenue mobilization.

E-invoices offer a more efficient alternative to traditional paper invoices, improving accuracy, speeding up business and providing real-time access to invoicing data to tax authorities. They enhance the efficiency of tax administration by ensuring that tax amounts are calculated and remitted correctly, while facilitating tax compliance by generating reliable data for audits. While there are multiple distinct models for the governance and operation of e-invoicing systems, examples of developing country tax authorities implementing them in partnership with the private sector show that they can handle millions of transactions, simplify tax reporting and compliance, and reduce fraud.

Tax policy units have had a positive impact on fiscal management and tax transparency.

Specialized units in finance ministries that seek to use evidence and data to drive policymaking are now common in richer countries, although less common in poorer countries.²² Working with revenue administration data and analytical staff, these units can provide technical analysis of the economic, behavioural and distributional implications of different policies, monitor and evaluate tax system performance and help inform budgeting processes.²³

2.4 Building integrated, medium-term strategies with public backing

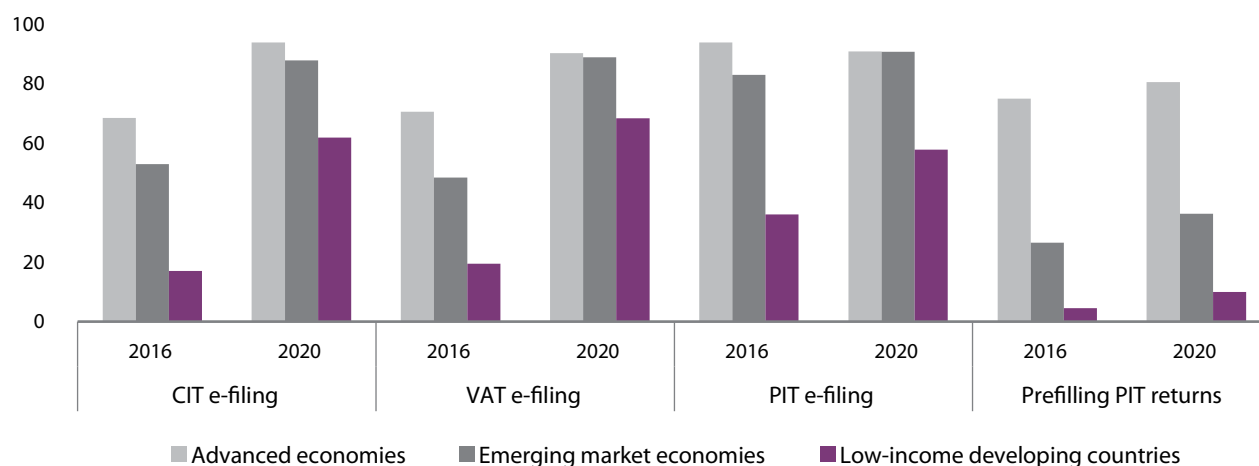
Tax system reform to increase tax revenues requires a medium-term, country-led and whole-of-government approach.

Taxation can serve as both a revenue collection tool and a policy instrument to encourage sustainable growth, influence behaviour, enhance well-being and improve governance. This Task Force has emphasized the importance of medium-term fiscal frameworks to help with planning and demonstrating political commitment to tax reform. A Medium-Term Revenue Strategy is one approach that can help to address interlinkages. Tax system reforms take time to design, implement and administer effectively, requiring a relatively longer time frame to yield significant revenue increases. This can create political challenges depending on the time horizon of decision makers.

The central challenge facing reformers lies in both identifying innovative technical strategies to strengthen revenue mobilization and improving trust to enhance compliance, build political support for reform and reinforce stronger social contracts. Reform strategies need to bring together various government agencies involved in tax policy design and implementation, taxpayers and civil society engaging with the tax system and, if relevant, external development partners supporting reforms.²⁴ Taxation is fundamentally a political decision, and political support for reforms to the tax system is essential if changes are to be sustainable and viewed as legitimate.²⁵ Social consensus for tax reforms that affect distribution and incentives are critical, as has been seen with attempts to reform fuel taxes (see below). Ultimately, the most important barriers to successful tax reform in many contexts are political rather than technical.

Figure III.A.5

Tax administrations offering electronic filing and pre-filing of PIT returns, by country groups, 2016–2020
(Percentage of ISORA respondents)



Source: IMF, Building Tax Capacity in Developing Countries.

Note: Country classification according to IMF categories.

3. International tax cooperation

At the beginning of the century, bilateral relationships and agreements were dominant, but multilateral tax agreements have now moved to the forefront.

International efforts on tax cooperation date back to the League of Nations period from the 1920s to the 1940s and continued after World War Two, first in the United Nations and then in the OECD.²⁶ These efforts focused on allocation of taxing rights and provision of double tax relief implemented through bilateral agreements. More recently, international tax cooperation has moved beyond double taxation relief to increasingly look at setting tax norms to limit tax avoidance and evasion, including by exchanging information between tax authorities. International tax cooperation can also help to build capacity in countries in need of support. While the Doha Declaration called for enhancing international tax cooperation, the Addis Agenda set principles by which this cooperation should occur. It noted that international tax cooperation should be universal in approach and scope and should fully take into account the different needs and capacities of all countries. The Addis Agenda also strengthened the work of the United Nations on international tax cooperation, doubling the meetings of the United Nations Committee of Experts on International Cooperation in Tax Matters (UN Tax Committee). Since 2009, and especially since the Addis Agenda agreement in 2015, there has been an acceleration of and participation in international cooperation on tax matters, with particular focus on tax transparency, international norms on corporate taxation and capacity-building (figure III.A.6). In December 2023, the General Assembly established an ad hoc committee, engaging all Member States, to develop draft terms of reference for a United Nations framework convention on international tax cooperation.

3.1 Tax transparency trends

International tax cooperation has advanced the furthest on transparency and information exchange, motivated by a desire to combat tax evasion. Since 2009, significant progress has been achieved

in ensuring transparency and exchange of information for tax purposes, primarily through the Global Forum. The UN Tax Committee agreed in 2009 to a code of conduct on cooperation in combating international tax evasion, setting minimum standards of conduct required of Member States regarding the exchange of information.²⁷ This was adopted by an Economic and Social Council resolution in 2017 that added endorsement for the automatic exchange of information.²⁸ Strengthened cooperation between jurisdictions has had a significant impact on domestic revenue mobilization. Over 26,600 bilateral requests for information were sent in 2022 to support ongoing tax investigations, up from less than 10,000 in 2009 (figure III.A.7). More than €126 billion of additional revenues (tax, interest, penalties) have been identified through both voluntary compliance and tax investigations. This includes over €41 billion by developing countries.²⁹

AEOI on financial accounts and the CbC reports of MNEs have provided new information for those tax administrations that receive them.

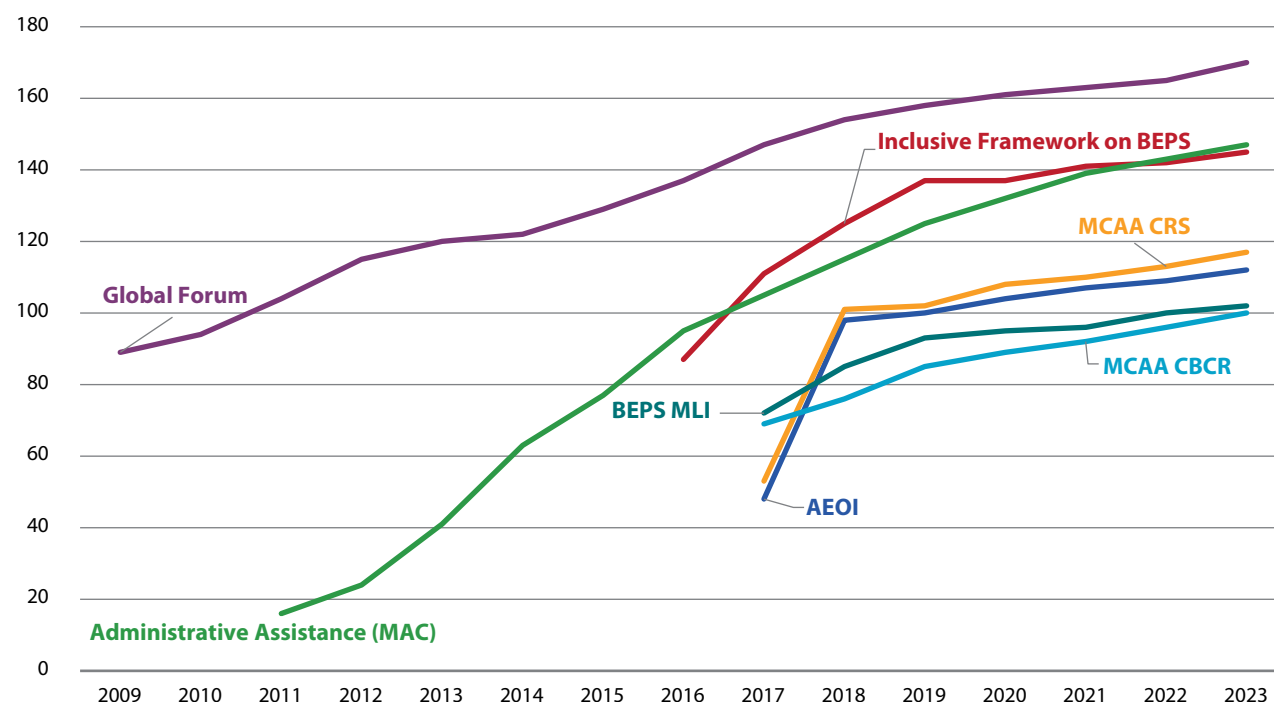
The 2014 adoption of the Standard of Automatic Exchange of Financial Account Information and its implementation represent a significant step in tackling tax evasion. Out of the 123 members of the Global Forum that by December 2023 committed to implement this Standard by a specific date, 108 jurisdictions have already exchanged information. Information on over 123 million financial accounts was exchanged automatically in 2022, covering total assets of almost €12 trillion (figure III.A.8). The Global Forum conducts peer reviews to assess the adequacy of its members' legal frameworks and the actual implementation of those frameworks. The vast majority of Global Forum jurisdictions (94 per cent) are assessed to have legal frameworks for implementing the AEOI Standard that satisfy the requirements. A significant majority of Global Forum jurisdictions (66 per cent) have been rated as "On Track" with ensuring the effective implementation of the AEOI Standard in practice.

Significant challenges remain in developing countries in regard to accessing and using information for tax enforcement. Developing countries have much lower levels of access to information on tax matters. To begin with only some of them are members of the Global Forum or the

Figure III.A.6

Participation in international tax cooperation instruments and forums, 2009–2023

(Number of jurisdictions)



Source: OECD, Global Forum.

Note: Includes both jurisdictions which are not sovereign countries and non-UN Member States.

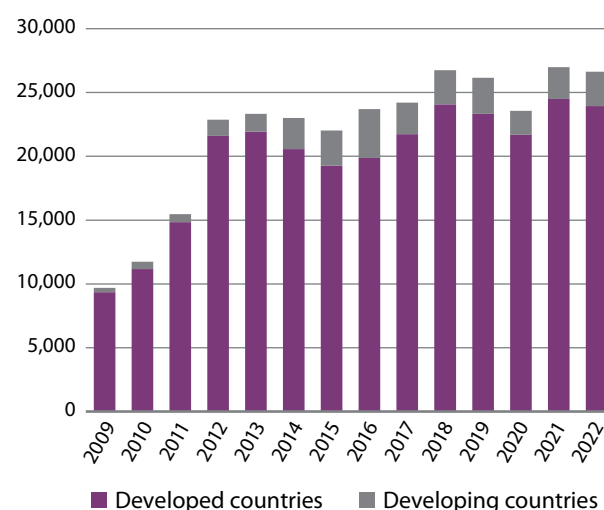
OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), which host the multilateral systems for, respectively, AEOI on financial accounts, and automatic exchange of CbC reports of MNEs. A lower number of least developed countries (LDCs) have signed the agreements, with only three LDCs signed on to each common reporting standard which allows AEOI, and to the instrument for CbC reports (figure III.A.9). Furthermore, countries must meet legal, administrative and technical infrastructure requirements before commencing exchanges. Countries must then bilaterally match with expressions of interest to share information from other countries and are expected to exchange information with all “interested appropriate partners”.³⁰ In 2023, 104 implementing jurisdictions sent financial account information to 84 recipient jurisdictions creating over 8,736 exchange relationships (with each direction of information flow counted separately). However, no LDCs are currently receiving information. Only five African countries were sending and receiving information as of November 2023, accounting for fewer than 400 of the relationships.³¹ Seven African countries (including three LDCs) committed to implementation by 2026. For developing countries that are members of the Global Forum the challenges to receiving information include insufficient capacities, lack of the appropriate legal framework, and confidentiality and data safeguards.³²

To improve the incentives for taxpayers and bolster trust in tax systems, more countries are moving towards public transparency for tax-related information. Information allows authorities to better enforce the law, and tax-related information needs to be more

Figure III.A.7

Exchange of information requests made by Global Forum member jurisdictions, 2009–2022

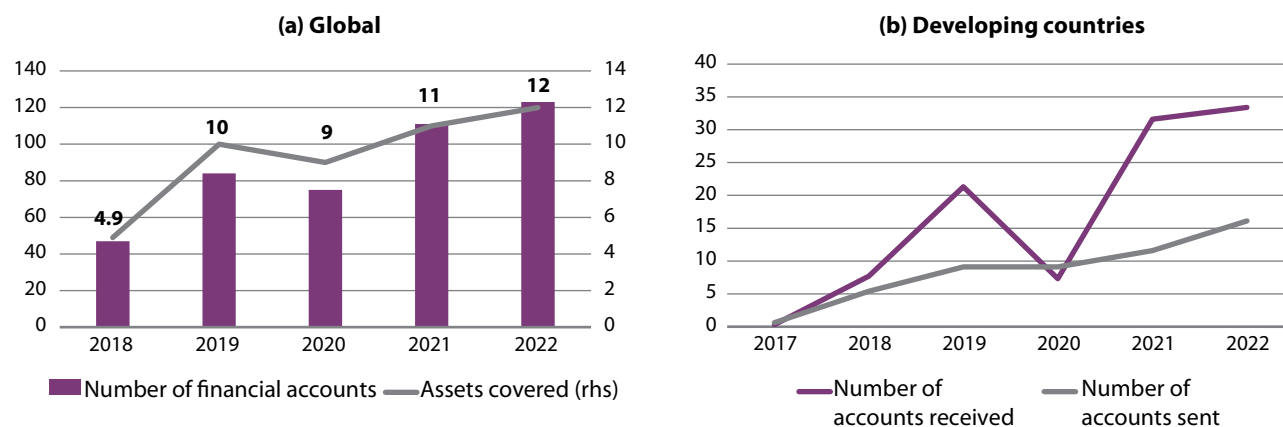
(Number of requests)



Source: Global Forum.

Note: Classification according to Global Forum definition of developing country.

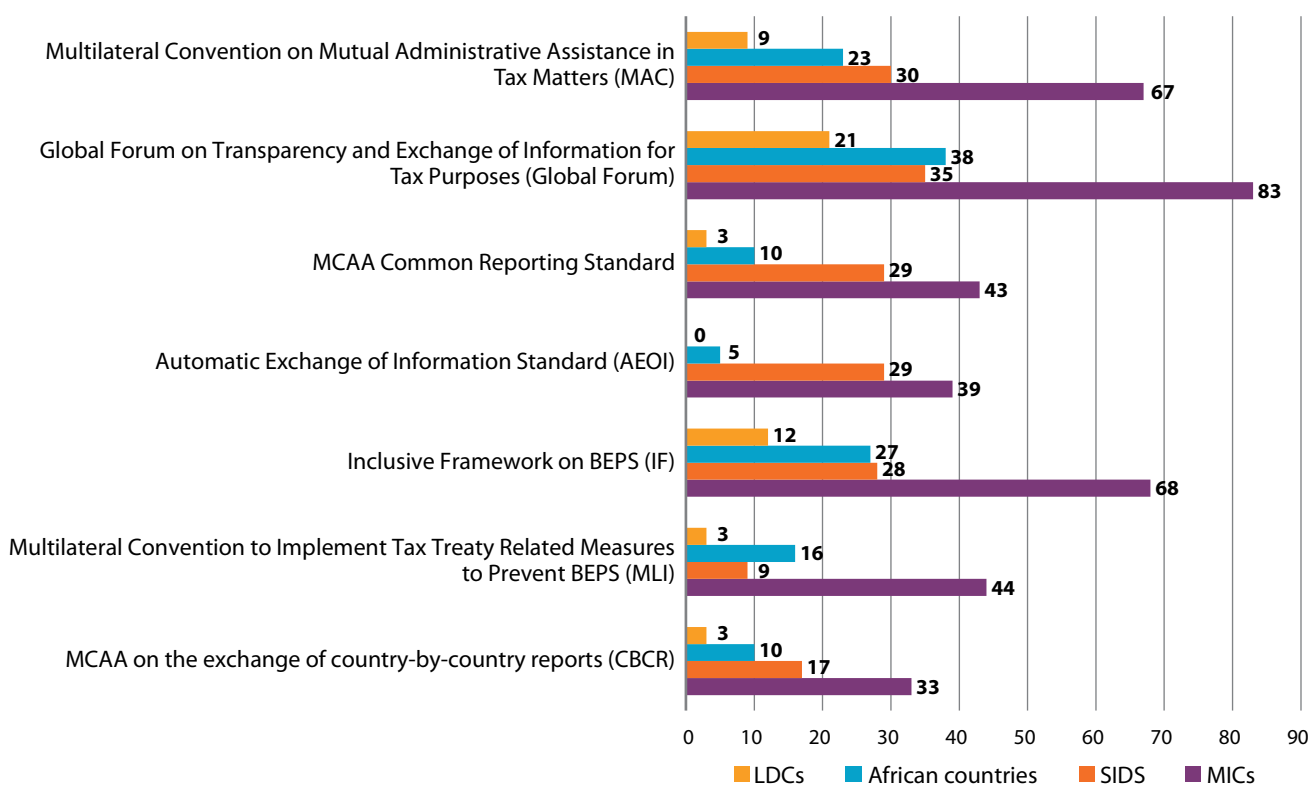
Figure III.A.8

Automatic exchange of financial account information, 2018–2022*(Millions of accounts, trillions of euros)*

Source: Global Forum.

Note: Difference between sent and received accounts is due to not all countries responding to the Global Forum survey. 2020 experienced a drop in countries responding to the survey due to the COVID-19 pandemic. Classification according to Global Forum definition of developing country.

Figure III.A.9

Participation of countries in special situations in international tax instruments and forums, 2023*(Number of jurisdictions)*

Source: OECD, Global Forum.

Note: This figure includes categories referenced in paragraph 8 of the Addis Agenda, including countries in special situations as well as middle-income countries. It includes jurisdictions which are not sovereign countries, non-UN Member State jurisdictions, and small islands that are associate members of regional economic commissions.

widely available. Public transparency can also boost trust more broadly and contribute to strengthening the social contract. A growing number of countries across regions are creating systems to publish their beneficial ownership registries for public access (see below). Public transparency of CbC reports is also on the table in some locations. Some countries and regions have already moved towards publication of a limited form of CbC reports. This follows the experience of more than 30 countries that required extractive industry MNEs (including both logging and mining industries) to publish additional corporate information in CbC format. Some companies are also voluntarily publishing CbC data. Better access to information can also empower journalists to report on fiscal systems, allowing for more effective accountability.

3.2 International norms on corporate taxation

The fundamental principles of taxation of MNEs were developed a century ago and have not yet been sufficiently updated to fully combat tax base erosion and profit shifting (BEPS). Despite the efforts of governments to tax revenue where economic activity occurs and value is created, existing data shows continued misalignment between the location where profits are reported and the location where economic activities occur. Data is scarce due to the inherent limitations in understanding the internal structures of MNEs and the lack of systematic global reporting. The best evidence comes from the anonymized and aggregated statistics based on the CbC reports, an innovation that arose in 2016. The CbC reports data is limited by aggregation levels, lack of reporting by some countries and lack of global coverage, but the most recent data from 2020 covers almost 7,600 MNE groups, with more than 929,000 legal entities and reports filed with 52 jurisdictions.³³ The data shows continuing differences in the distribution of employees, tangible assets and profits, with profits and related-party revenue much higher in investment hubs which have a low share of employees and assets.³⁴

Increased attention since 2008 has led to significant enhancements of the OECD rules designed to prevent BEPS, but enterprises continue to exploit gaps and mismatches in tax rules to artificially shift profits to low-tax or no-tax locations. Prior to the 2008 world financial and economic crisis, OECD countries agreed on international tax norms through processes that were closed to non-OECD countries. With the elevation of the Group of Twenty (G20) as an important tax decision-making forum in 2009, political sign-off shifted to all G20 countries alongside OECD members, while the OECD Secretariat continued to support the technical norm-setting work. This grouping produced an important set of agreements to combat corporate tax avoidance and evasion in 2015, the so-called BEPS Action Plan, alongside a new intergovernmental forum to monitor implementation of these actions, the OECD-housed Inclusive Framework on BEPS. Of the 15 actions set forth in the BEPS Action Plan, four are considered minimum standards that must be adopted by all Inclusive Framework member jurisdictions: Action 5 on harmful tax practices, Action 6 on prevention of tax treaty abuse, Action 13 on CbC reports, and Action 14 on mutual agreement procedures. As of end-December 2023 the number of CbC report exchange relationships globally had grown to 3,876—of which 1,976 involved a middle-income country. However, there are concerns that developing countries lack access to this data given that currently, access to the reports is usually predicated on membership of the Inclusive Framework. Only 22 developing countries have implemented the

requirements to receive the reports, with the multiplicity of requirements, including on legislation and confidentiality, cited by countries as preventing progress.³⁵ Only five African countries are receiving such reports and only 59 exchange relationships involve an LDC.

While international policy discussions on updating international corporate income tax norms to address digitalization and globalization have been ongoing for more than a decade, they have yet to yield an agreement that sufficiently addresses allocation of taxing rights, tax avoidance and evasion, and that has the full support of all Member States. Work to address digitalization and globalization is ongoing at the United Nations Committee of Experts on International Cooperation in Tax Matters, and in the OECD/G20 Inclusive Framework Two Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy. The UN Tax Committee is developing a fast-track instrument for speedier adoption of key provisions regarding taxing the digitalized and globalized economy from the United Nations Model Double Taxation Convention between Developed and Developing Countries. These provisions include Article 12B of the UN Model, agreed in 2021, which when added to bilateral treaties would preserve within the treaty relationship the right of source countries to tax income from automated digital services delivered by companies based in the treaty partner. At the Inclusive Framework, work continues on Pillar One, which aims to allow market jurisdictions to tax some of the profits of the largest and most profitable MNEs without reference to the existing arm's length standard for attributing profits to different jurisdictions, an important conceptual change in international tax norms. However, for the majority of profits and most MNEs, the rules for profit attribution and allocation of taxing rights would not change.³⁶ Countries agreeing to implement Pillar One will also need to remove any digital services taxes as defined by the Multilateral Convention to Implement Amount A of Pillar One (MLC). The draft text of the MLC was published in October 2023, although it remains to be finalized and entry into force would require the convention to be ratified by at least 30 jurisdictions, one of which must be the United States of America.³⁷ Rules to standardize the application of the arm's length principle in some specific cases of marketing and distribution activities (so-called Amount B) were released in February 2024.

The proposed global minimum tax aims to ensure minimum levels of corporate taxation and limit international tax competition, including by modifying some of the premises for taxing rights on corporate income; it is an opportunity for developing countries to redesign their investment tax incentives. The rules for implementing a global minimum tax of 15 per cent, so called global anti-base erosion rules, under Pillar Two of the Inclusive Framework are complete and are being implemented as part of a common approach. More than 30 jurisdictions had implemented the global minimum tax as of the start of 2024 and more have announced plans to implement it by 2025. Jurisdictions where profits are declared under current tax norms have the option of collecting tax on low-taxed profits first, including through Qualified Domestic Minimum Top-Up Taxes (QDMTTs), before other jurisdictions get a chance to tax any profits that are taxed less than the minimum. Low-taxed profits are present in all country groups, but the highest share (41 per cent) are declared in investment hubs.³⁸ The global minimum tax is designed to reduce the incentive for the largest MNEs to engage in profit shifting. By also putting a floor under some tax competition, the global minimum tax

provides an opportunity for developing countries to re-evaluate their tax incentives, particularly tax holidays, and eliminate those that are ineffective and not aligned with sustainable development. The Platform for the Collaboration on Tax plans to update its toolkit on tax incentives³⁹ in light of international tax developments.

Subject-to-tax rules also allow countries to protect their tax base.

In March 2023, the UN Tax Committee approved the addition of a subject-to-tax rule (STTR) to the UN Model Convention, which can be incorporated into bilateral tax treaties. This provision applies to any payments, whether between related or unrelated parties, when such payments are subject to tax below an agreed-upon rate. At the OECD, the Pillar Two STTR would allow source countries to tax a more limited set of outbound intra-group payments—including interest, royalties and all payments for services—when they are taxed below the specified rate of 9 per cent in the destination country. A multilateral convention to facilitate implementation of the Pillar Two STTR was opened for signature in October 2023.⁴⁰ Inclusive Framework members with low taxes on the covered payments have committed to incorporate it into their treaties with developing countries, if requested.

3.3 Capacity-building for domestic revenue mobilization

The Addis Agenda recognized the need to increase capacity-building and prompted efforts to strengthen and better

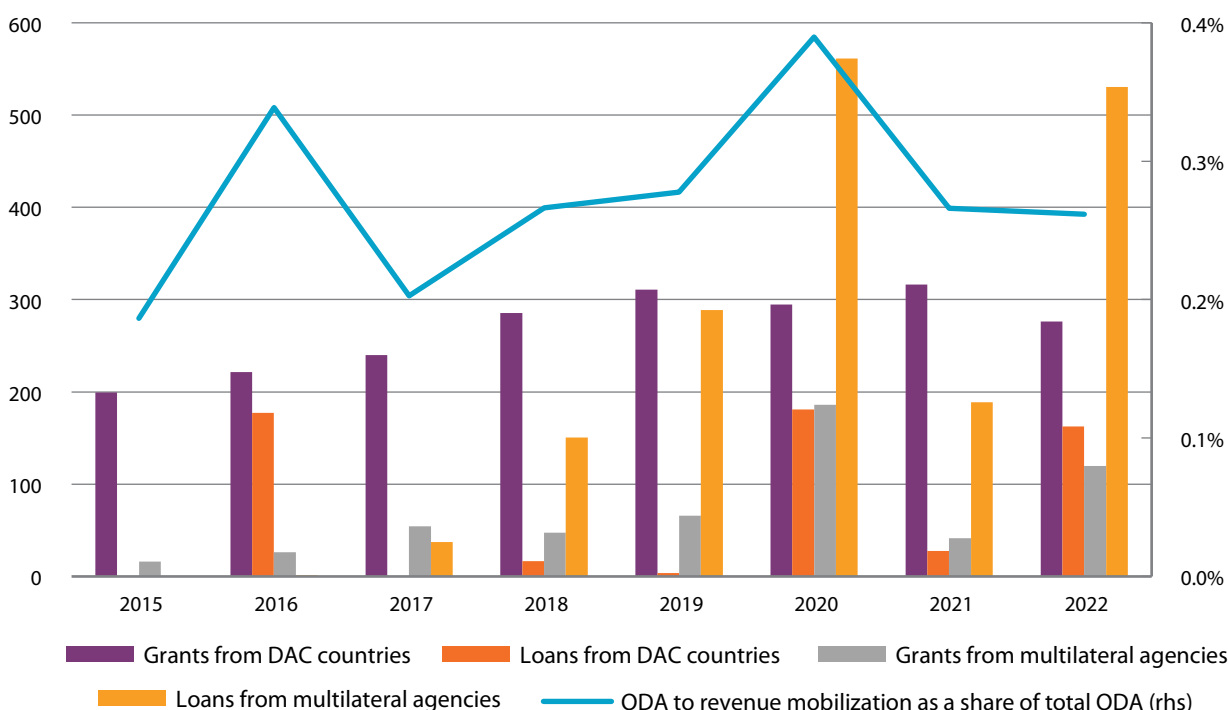
measure the funding for domestic resource mobilization. While intergovernmental organizations such as the United Nations, the IMF, the World Bank Group and the OECD have long held training and capacity programmes to build tax capacity and support tax reforms, donor funding for this support and for bilateral programmes was not systematically tracked prior to 2015. New efforts, such as the joint OECD/UNDP Tax Inspectors Without Borders initiative and the Addis Tax Initiative, were launched at the Third International Conference on Financing for Development in Addis Ababa. In 2016, the OECD Development Assistance Committee (DAC) adopted a new monitoring code for its Creditor Reporting System to better track the provision of official development assistance (ODA) for domestic resource mobilization. This change enabled voluntary efforts to increase capacity-building such as the Addis Tax Initiative to better measure and track progress.

Donor-funded capacity-building related to domestic public revenue mobilization has increased dramatically since 2015 but has levelled off in recent years just as new international tax norms will require increased administrative capacity. The measured donor-funded capacity-building related to domestic public revenue mobilization has increased since the \$200 million reported in 2015 but it has fallen short of voluntary commitments to double it by 2020.⁴¹ Disbursements of ODA by OECD donor countries coded as being for the purpose of domestic revenue mobilization fluctuated between \$300 million and \$475 million from 2018 to 2022, ending the period as 0.26 per cent of total ODA to developing countries (figure III.A.10).

Figure III.A.10

Official development assistance disbursements for domestic revenue mobilisation, 2015–2022

(Millions of United States dollars, percentage)



Source: OECD.

Note: Constant 2022 United States dollar disbursements from Development Assistance Committee (DAC) countries.

International organizations have significantly increased capacity-building, with stronger coordination and an increase in regional work. The data on ODA disbursements in this area shows a marked increase in both grants and lending from multilateral agencies such as the World Bank and IMF, especially in 2020 and 2022 (figure III.A.10). This does not include the significant efforts in international coordination spurred by the increased attention on tax capacity-building. Already in 2014, the Global Forum launched an Africa Initiative, and this model was subsequently reproduced in other regions. The Platform for Collaboration on Tax was launched in 2016. The United Nations system has also expanded its capacity-building work both in international tax cooperation and in enhancing domestic resource mobilization in ways that promote sustainable development. Additionally, regional tax organizations have stepped up their efforts by forming a global platform called the Network of Tax Organisations (NTO) in May 2018, comprising 10 regional and international tax administration forums. Most recently, a new Regional Tax Cooperation Platform for Latin America and the Caribbean was created in July 2023.

4. Illicit financial flows

The study of IFFs has combined and built on earlier work on capital flight, corruption and the proceeds of crime. The Monterrey Consensus referenced the need to reduce capital flight and fight corruption. While the Doha Declaration introduced the term “illicit financial flows”, it provided sparse coverage of this topic. Attention to IFFs greatly increased in the 2010s, especially with the 2011 mandate from the African Union and Economic Commission of Africa to establish a High Level Panel on Illicit Financial Flows from Africa, which issued a report in 2015 before the Third International Conference on Financing for Development in Addis Ababa. The Addis Agenda and 2030 Agenda on Sustainable Development then provided global agreement on the need to substantially reduce and eventually eliminate IFFs.

Combating IFFs is a key strategy to combat organized crime, support domestic resource mobilization and provide resources for sustainable development. Addressing corruption can also support increased voluntary tax compliance.⁴² Member States have recognized combating IFFs as a key development challenge that requires a whole-of-government approach.⁴³ Emphasis should be placed on information exchange and national cooperation mechanisms among tax authorities, anti-corruption bodies, financial intelligence units, law enforcement and other relevant national institutions.

4.1 Beneficial ownership transparency

The availability of beneficial ownership information on legal persons and arrangements, and on financial accounts, helps to fight against tax evasion and other financial and serious crimes such as corruption, money laundering and terrorist financing. Although the original purpose of beneficial ownership laws and regulations was to fight money laundering and financial crime, the beneficial ownership transparency agenda has significantly expanded in the past few years, contributing to multiple policy goals, including fighting corruption and financial crimes, public accountability, promoting business integrity, improving investment climates and protecting national security. Understanding who is the

natural person who owns and controls legal entities and arrangements (beneficial owner) can prevent the misuse of corporate structures. Financial Action Task Force (FATF) Recommendations require the availability of reliable, accurate and up-to-date beneficial ownership information.⁴⁴ The Global Forum has also introduced complementary beneficial ownership rules to combat tax evasion.

Since the first beneficial ownership standard was introduced in 2003, a growing amount of beneficial ownership information has become available to both governments and the wider public, but effective implementation is a challenge. The FATF strengthened its recommendations related to beneficial ownership transparency in 2022 and released a new suite of guidance in 2023.⁴⁵ While countries have generally amended their legal frameworks to comply with these international obligations, and many have even adopted registries, implementation has proven to be challenging, especially around the verification of beneficial ownership information. At its tenth session held in December 2023, the Conference of State Parties to the United Nations Convention Against Corruption (UNCAC) considered a report on good practices for beneficial ownership information⁴⁶ and adopted a resolution on enhancing the use of beneficial ownership information to strengthen asset recovery, which included recommendations on the sharing of good practices, the need to maintain searchable historical records of beneficial owners, including of legal persons and legal arrangements, and verification.⁴⁷

4.2 Asset recovery and return

International commitments for asset recovery and return were first made with the ratification of the United Nations Convention on Transnational Organized Crime (UNTOC) and UNCAC in the early 2000s. UNTOC was the first universal legal instrument to set forth a framework for financial asset return⁴⁸ when it was adopted in 2000. It opened the possibility for asset return but did not mandate it, only requiring the State that recovers assets to “give priority consideration to returning the confiscated proceeds of crime or property to the requesting State Party”.⁴⁹ In 2003, UNCAC Chapter V introduced the obligation to return the proceeds of corruption, requiring countries that ratify the convention to adopt laws to enable asset return and to return confiscated property that has been seized as result of requests made in accordance with the convention.⁵⁰ Within the financing for development process, the first call on States to assist in the recovery and return of stolen assets was in the 2008 Doha Declaration. Following agreement on the Addis Agenda, significant inter-governmental discussions focused on how improving asset recovery and return can contribute to the financing of sustainable development.

With increasing data availability, it is clear that the volume of asset recovery and return is increasing, with the growing use and central importance of non-conviction-based asset recovery. The Stolen Asset Recovery Initiative (StAR) contributed to an analysis of international returns of proceeds of corruption that took place between 2010 and 2023 (figure III.A.11). The survey-based data, which is not comprehensive, shows that \$4.3 billion in corruption proceeds have been returned to countries since 2010, with volumes of returns higher after 2017.⁵¹ Conviction-based criminal forfeiture remained the most frequently cited legal mechanism for cross-border asset recovery efforts, used in just over half of all reported cases (51 per cent), followed by non-conviction-based confiscation (30 per cent) and settlements (22 per cent).⁵² There is no data

available on the volume of assets frozen due to a request from another country, nor comprehensive estimates on the total amounts lost to corruption, but some have claimed these total hundreds of billions of dollars over a span of decades.⁵³

The asset return process, however, remains time-consuming and resource-intensive and is still too frequently blocked. States identified two major barriers to successful international asset recovery under UNCAC: (1) perceived non-responsive or overly broad mutual legal assistance refusals by the country of asset location and (2) difficulties in identifying, and verifying the beneficial ownership of suspected corruption proceeds. Responses further emphasized the growing use and central importance of non-conviction-based asset forfeiture in cross-border asset recovery cases involving corruption proceeds. In addition, October 2023 revisions to the FATF Recommendations bolster the powers and ability of law enforcement and other authorities to identify and trace criminal property for the purposes of asset recovery.⁵⁴ UNODC, including through its Global Operational Network of Anti-Corruption Law Enforcement Authorities (GlobE Network) and its joint StAR Initiative with the World Bank, continues to support countries with their asset recovery efforts.

There remains no international provision for asset recovery and return for non-corruption related IFFs. UNCAC is the only universal instrument that mandates asset recovery and return, but its provisions are limited to the proceeds of corruption. The Multilateral Convention on Mutual Administrative Assistance in Tax Matters contains provisions for assistance in the recovery of tax claims, although most signatories have a partial or complete reservation on the provision. FATF standards now include tax crimes as a predicate offence to money laundering, providing another avenue for international cooperation on asset recovery. In 2020, African Union countries adopted the Common African Position on Asset Recovery, which expresses a desire to go beyond the proceeds of corruption to also address tracing and repatriation of other types of IFFs, including abusive transfer pricing, trade misinvoicing and tax evasion.⁵⁵ Member States could examine the development of a more holistic approach to asset recovery, building on the provisions in UNCAC but encompassing all sources

and channels of IFFs. Such a holistic framework could create an effective, more efficient and more impactful asset recovery infrastructure.⁵⁶

4.3 Measurement of progress

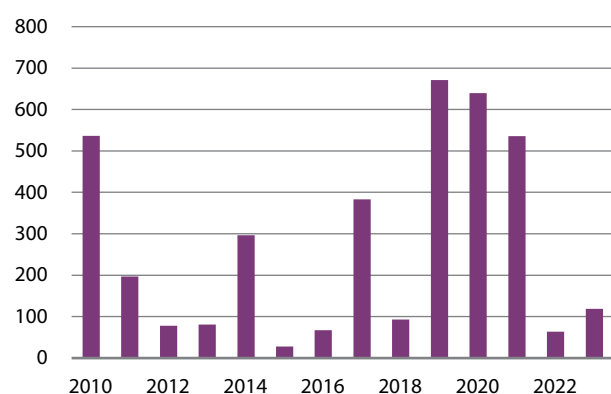
Comparable and reliable statistics on IFFs can help to shed light on the activities, sectors and channels most prone to illicit finance, pointing to priorities for enforcement resources. As co-custodians of SDG Indicator 16.4.1 on IFFs, UNODC and the United Nations Conference on Trade and Development (UNCTAD) defined globally agreed statistical concepts and a statistical definition of IFFs in the *Conceptual Framework for the Statistical Measurement of Illicit Financial Flows*,⁵⁷ endorsed by the United Nations Statistical Commission in March 2022.⁵⁸

Agreement on the statistical definition of IFFs resulted in the publication of the first official estimates of IFFs in the SDG indicators database in early 2023. The first estimates reported by nine different countries reveal that IFFs related to criminal activities are substantial, with estimates comparable to the value of exports of licit markets in some countries.⁵⁹ Several countries also prepared preliminary unofficial estimates of IFFs from trade misinvoicing, by analysing asymmetries in customs reporting between countries or abnormal prices in transaction-level customs data, using UNCTAD methodological guidelines.⁶⁰ Pilot testing in 22 countries, supported by the custodian agencies with United Nations Regional Commissions, will continue, with a new global project focused on nine countries until 2026.⁶¹

Based on lessons learned in pilot testing countries, international organizations are continuing to improve methods to measure IFFs but at the current pace, only a handful of countries will have made estimates before 2030. New IFF estimates are enabling countries to develop tailored policies to curb these flows more effectively. UNCTAD has refined methodological guidelines for measurement and is conducting pioneering work on the aggregation of estimates from multiple IFF types into one number.⁶² UNODC has developed a draft *Statistical Framework to Measure Corruption* to make progress on these measurement challenges. It was presented to the 54th session of the United Nations Statistical Commission and reviewed through two global consultations.⁶³ While most countries have the necessary data, they need support to organize the inter-agency work, develop skills, apply the guidance, enhance information systems and create the necessary tools.

Figure III.A.11

Value of global asset returns, 2010–2023
(Millions of United States dollars)



Source: UNODC.

Note: Based on survey responses from 98 Member States.

5. SDG-related expenditure and investment

Public spending is a powerful instrument to incentivize, support and deliver sustainable development, and all countries have scope to better align public expenditure with the SDGs. Expenditure policy is a key mechanism for investing in SDG achievement, including redistribution and risk reduction.⁶⁴ Effective public financial management (PFM) systems allow countries to implement those policies efficiently. The Monterrey Consensus called for efficient, transparent and accountable systems for managing the use of public resources as well as improvements in public spending. The Doha Declaration called for Member States to continue to improve budgetary processes and enhance the transparency of

PFM and the quality of expenditures. The Addis Agenda committed to further strengthening the effective use of domestic resources and covered in detail subjects such as gender, social protection, infrastructure, ecosystem protection, subnational finance and fossil fuel subsidies.

5.1 Public financial management

Increasing the effectiveness of PFM can allow the State to more efficiently deliver public goods and services and reduce the losses to corruption.

Countries can generate positive feedback loops by using revenue for efficient public goods and services delivery, which boosts trust in government and generates incentives for paying tax and further improving accountability of the public sector for good financial management. This may require more effective fiscal coordination with subnational entities that struggle to deliver mandated services without sufficient or timely disbursement of resources by central authorities. Budget systems can also be adapted to allow better tracking of spending on sustainable development, including for climate adaptation and disaster risk reduction,⁶⁵ in ways that are comparable across countries (see chapter IV box IV.3). There are indications that country PFM systems are improving over time. Countries that assessed their PFM systems multiple times using the PEFA framework, on average, improved their scores from their first PEFA assessment to their last. There are several examples, however, of deteriorations in average scores after first assessments, which can often be attributed to external shocks, political economy factors or changes in governance.

PFM reforms are often technocratic changes but have had greater impact where there is a genuinely new political settlement that underpins sustainable reforms. Well-developed PFM systems can help to track the effectiveness of spending and provide the information needed for decision-making on resource allocation. They can also provide ongoing information on overspending, underspending and challenges in delivering public goods and services.⁶⁶ However, even seemingly small reforms that seek to prevent leakage and introduce better accounting can create entrenched opposition from vested interests that are opposed to reforms.⁶⁷ Many reforms over the last two decades have proceeded technically, with new systems implemented, but political economy considerations help to explain why they did not achieve their full intended impact. A better PFM reform agenda will build on a political economy analysis of the country, its current systems and practices, and bring more voices into the conversation. Improving the transparency of budget processes and instituting participatory budgeting can contribute to public ownership of PFM reforms.

5.2 Gender-responsive budgeting

Strengthening the alignment of domestic expenditure with gender equality goals is imperative, and gender responsive budgeting (GRB) can enhance the effectiveness of public finance's contributions to gender equality.

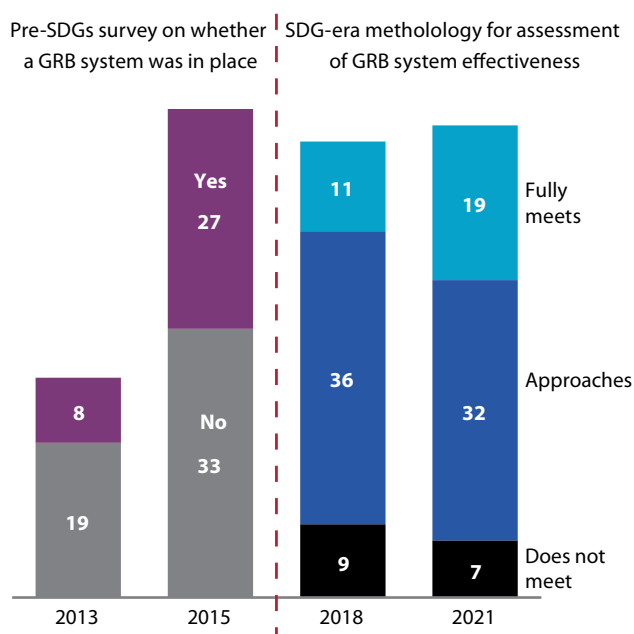
GRB is a public policy tool that analyses central and local administrative budgets to assess gender financing gaps, identify actions to close them and ensure that national and local commitments to gender equality and women's empowerment are resourced. The introduction of GRB can help to focus political attention on matching the delivery of public resources for gender equality and women's empowerment with a country's stated gender equality objectives. For example, it can enable greater expenditure on alleviating

unpaid care burdens which fall disproportionately on women. Globally, however, only one in four countries currently has a comprehensive GRB system (figure III.A.12). Where these systems do exist, they support efforts to cost, allocate and spend resources to effectively implement national gender-responsive laws and policies, including those with indirect impacts on gender equality.

Over time, GRB has been introduced in more countries globally and tracking systems have become increasingly comprehensive and effective, but gaps remain.

Analysis of GRB practices indicates the importance of strengthening gender integration in PFM systems, while also enhancing transparency and accountability. This can support better targeting of public resources for the implementation of gender equality laws and policies, while also building trust that public resources are allocated and spent to respond to the needs and demands of people.⁶⁸ GRB should encompass all spending, including on public services, infrastructure and social protection; and include analysis of taxation and other revenue-raising measures and a review of spending outcomes.⁶⁹ GRB implementation can improve with legislative requirements and/or mandates, combined with clear guidelines. Further, strong linkages between policy design and budget decisions are important, coupled with robust gender analysis at each stage of the budget cycle. Providing training and capacity-building to legislators can improve the understanding and uptake of GRB.

Figure III.A.12
Existence and comprehensiveness of gender-responsive budgeting systems, 2013–2021
(Number of countries)



Source: UN WOMEN calculations based in part on GPEDC survey.

Note: Data for 60 countries that reported data in 2015 and at least one datapoint in 2018 or 2021. 2013 and 2015 data based on Global Partnership for Effective Development Cooperation survey with four binary Yes/No questions. 2018 and 2021 data based on a revised methodology comprising 13 questions allowing for more granular analysis of systems, as approved by the Statistical Commission for SDG indicator 5.c.1. The SDG indicator methodology focuses on linkages between legislative/policy commitments and budget resources.

It is important to improve data quality and strengthen capacities and skills to conduct comprehensive gender assessments of all budget policies and evaluate the corresponding impacts of these on different groups. Increasing timely and accessible public data on gender budget allocations and expenditures is central to these efforts, so that governments and other stakeholders can follow public resource flows and evaluate the extent to which public investments address the needs and priorities of women living in poverty.⁷⁰ Active engagement of civil society organizations, parliaments and audit institutions can strengthen the evaluation of impacts and the accountability loop.

5.3 Fiscal responses to climate change

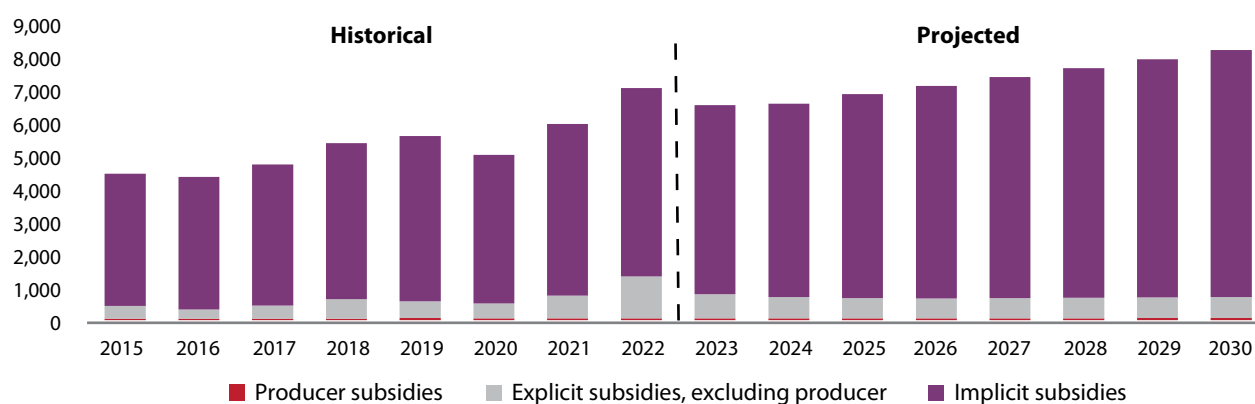
Fiscal systems and regulatory policies matter for climate action: they can either encourage and subsidize emissions of change-inducing pollutants or incentivize climate change mitigation and adaptation. In the Addis Agenda, Member States committed to rationalize inefficient fossil fuel subsidies that encourage wasteful consumption. The Addis Agenda also explicitly encouraged the exploration of carbon pricing as a form of innovative financing for development. Indeed, climate change action requires a fundamental transformation of consumption, production and investment by all, and fiscal policies must play a central role in setting the incentives that encourage decarbonization and climate adaptation.⁷¹ Yet, fiscal systems remain rife with measures that actually encourage inefficient or unsustainable investment, particularly in fossil fuels and associated infrastructure. Agricultural subsidies that induce climate change are linked to both fuel and fertilizer use and land use changes.⁷² Standard economic literature emphasizes that setting a price on carbon is the best way to incorporate the environmental and social costs of pollution into market economies, but there has been a widespread rejection of pursuing the transformation through carbon pricing alone.⁷³ Climate change action may need a combination of instruments (including taxes, user fees, carbon markets, regulations and subsidies) to be politically feasible, administratively practical and effective.

Global fuel prices do not reflect the full economic and environmental costs of their use, including both climate change and local pollution impacts; both implicit and explicit subsidies have risen over time. Fossil fuel subsidy estimates, which look at both implicit and explicit subsidies, provide summary information that points to the substantial and pervasive underpricing of fossil fuels.⁷⁴ Estimated global fossil fuel subsidies were \$7 trillion in 2022, including \$1.3 trillion in explicit subsidies (figure III.A.13). Both implicit and explicit subsidies have grown over time, with noticeable increases in 2022 at the time of significant energy price volatility. Potential revenues from subsidy reform are lower than the subsidies themselves given that reform would reduce fuel consumption. Recent surges in international fossil fuel prices reinforce the case for rapidly transitioning away from fossil fuels—not only to address the climate crisis and reduce air pollution deaths but also to decrease dependence on insecure sources of energy.⁷⁵

Carbon pricing can be used to incorporate social costs into economic decision-making and to help address climate change.

Carbon pricing's primary goal lies in the implementation of the polluter pays principle, anchored in Principle 16 of the Rio Declaration on Environment and Development (1992), which advocates that the costs of pollution and its mitigation should be borne by the emitters. In addition to creating an incentive to reduce emissions, carbon pricing can help to raise revenues. Carbon pricing can be implemented through a range of instruments with various policy designs, which can be tailored to best meet domestic objectives and circumstances. This includes direct (or explicit) carbon pricing mechanisms such as emissions trading systems and carbon taxes, which impose a cost expressed as a monetary unit per ton of carbon dioxide equivalent (CO₂e). Indirect ways of placing a price on carbon emissions include fuel and energy taxes. By changing the relative price of the carbon-emitting and no-carbon technologies, green subsidies and tax incentives can achieve similar results, but potentially at high fiscal cost. Rarely is a single carbon price applied across an economy; tax codes often give preferential treatment for fossil fuel consumption⁷⁶ and many direct carbon pricing instruments target specific sectors or even fuels,

Figure III.A.13
Global fossil fuel subsidies, 2015–2030
(Billions of United States dollars)



Source: IMF.

Note: Figures after 2019 and 2022 use projections for fuel use and fuel prices, respectively.

much like indirect taxes on fossil fuels; and carbon and fuel taxes can be substituted one for another.⁷⁷ Carbon pricing policies can be accompanied by compensating assistance for low-income households to address distributional concerns.

Carbon pricing has been shown to be an effective fiscal tool—raising revenue in ways that are less distortionary than other policies—with global coverage of direct carbon pricing policies continuing to expand. Almost a quarter of global greenhouse gas emissions are currently subject to a carbon tax or emissions trading system, with 73 instruments currently in operation (figure III.A.14 panel a). In the past year, only a few instances occurred where governments relaxed direct carbon pricing in response to the energy crisis. Revenues from carbon taxes and emissions trading systems increased almost five-fold in the past decade to a record high of almost \$100 billion in 2022 (figure III.A.14 panel b)⁷⁸ as policies have evolved and diversified to reflect increased ambition. These revenues can help to finance decarbonization, improve government balance sheets, support resilient and sustainable development, and finance a just transition. While the uptake of direct carbon pricing is on the rise in developing countries, existing instruments are predominantly implemented in developed countries. Additional revenues from carbon pricing could be on the order of several percentage points of GDP.⁷⁹ Carbon taxes are also straightforward administratively as an extension of fuel taxes.⁸⁰

5.4 Social protection financing

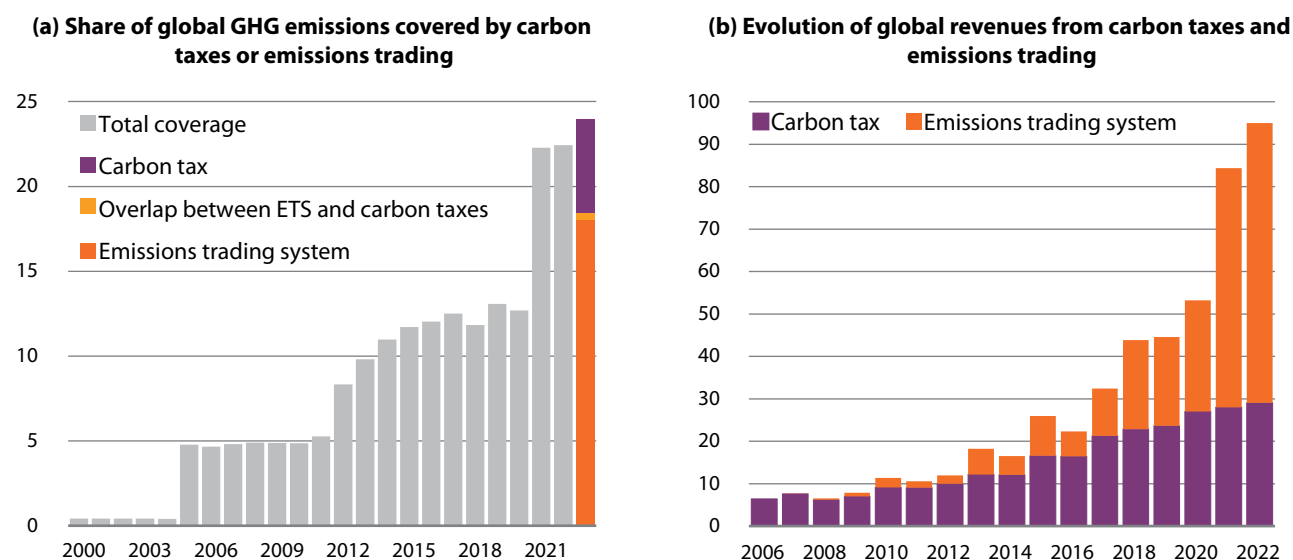
Enormous progress has been made on delivering the human right to social security, but social protection benefits are still not a reality for most of the world's population. The development of social protection systems over the past century has been remarkable (figure III.A.15). Today, most countries have schemes in place, anchored in national legislation, that cover all or most areas of social protection, although in

some cases these cover only a minority of the population. While national legal frameworks are essential for a rights-based approach to social protection, they do not on their own ensure effective coverage of the population nor the adequacy of benefits. Large gaps still remain, especially in Africa and Asia. Only 46.9 per cent of the global population is effectively covered by at least one social protection benefit (excluding health care and sickness benefits).⁸¹ As countries develop their systems to deliver on the mandate in the Addis Agenda for universal social protection, they need to consider the adequacy, efficiency and sustainability of their policies.

Higher social protection expenditure is associated with lower income inequality. The largest reductions in income inequality are observed for contributory pensions, which in many countries capture the largest share of social protection expenditure. Evidence from the International Labour Organization shows that in 17 out of 35 countries with available data, such pensions reduce income inequality, as measured by the Gini coefficient, by more than 15 per cent and in three countries by at least 30 per cent. On average, countries that spend a larger percentage of GDP on a given social protection benefit are also those that obtain a larger reduction in income inequality for paying such benefit.⁸² Building synergies between the social protection and tax systems can strengthen the social contract between citizen and State, as expansion of the tax base can coincide with or even follow the provision of benefits. The efficient operation of a social protection system also helps to maintain public confidence in the effectiveness of the programme and trust in the State as a whole.

Solid and sustainable financing frameworks are essential for social protection systems to function effectively and have positive impacts. Financing social protection generally comes from the budget, thus tax revenues and social contributions are the basis of financing. Universal social protection systems also have some unique features, notably that necessary expenditures tend to rise during economic slowdowns—precisely when available resources are falling. The financing mix for social

Figure III.A.14
Carbon pricing and associated revenue, 2000–2023
(Percentage, billions of United States dollars)

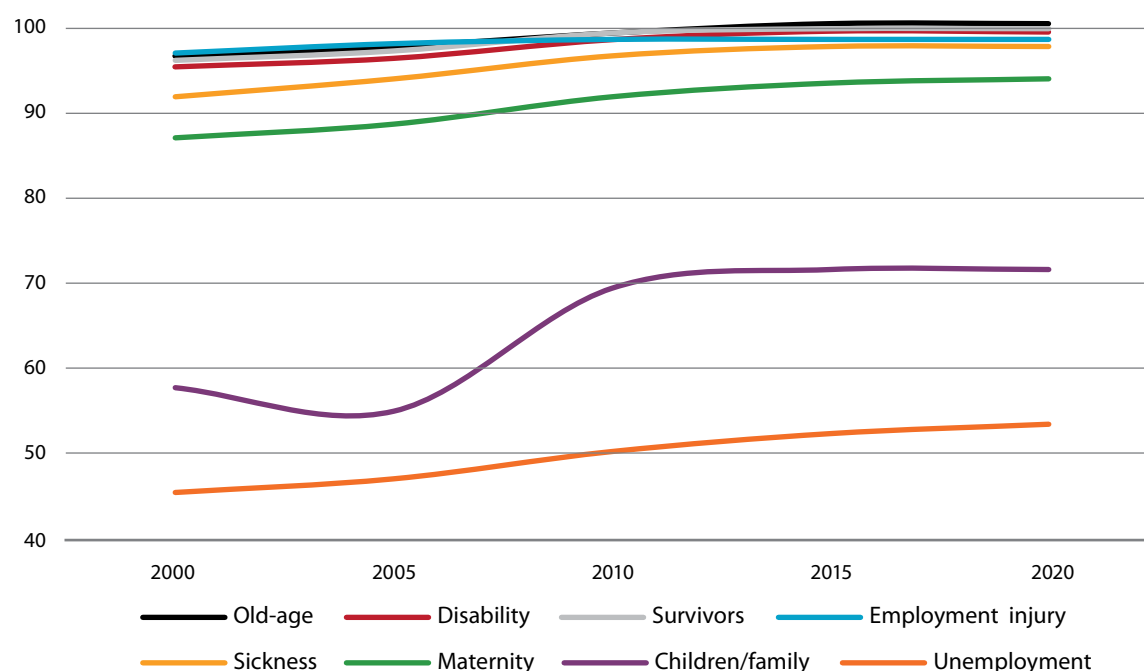


Source: World Bank, State and Trends of Carbon Pricing 2023.

Figure III.A.15

Coverage of social protection systems anchored in national legislation, by policy area, 2000–2020

(Percent of countries)



Source: ILO.

Note: Countries with social security schemes anchored in national legislation, by policy area (branch).

protection thus needs to be effective for countercyclical expenditure. Some countries have successfully used dedicated fiscal reserve funds to create countercyclical financing, which is a popular choice for commodity exporting countries.

The financing gap to achieve SDG targets in social protection and essential health care is still sizeable and has increased by approximately 30 per cent since the onset of the COVID-19 pandemic. The financing gap for extending a social protection floor to all was estimated to be \$1.2 trillion per year or 3.8 per cent of world GDP in 2020. This is the average additional investment required to achieve universal coverage of basic benefits to all children, mothers of newborns, those who are severely disabled and all persons in old age, as well as universal essential health care. The annual financing gap is higher for lower-middle-income and low-income countries, reaching 5.1 per cent of GDP and 15.9 per cent of GDP, respectively.⁸³

Options to increase fiscal space for social protection exist, even in low-income countries. Countries have to manage budget constraints, but increasing the size of universal transfers can be feasible and redistributive if financed by reforms to make the tax system more efficient and progressive.⁸⁴ The primary avenue to expand the fiscal space is to gradually increase domestic resources for social protection in line with the economic and fiscal capacity of each country. Countries can reprioritize expenditure, for example away from fossil fuel subsidies (see above). Another key channel to increase domestic resources is to extend social insurance coverage. Social security contributions as a source of financing for social protection have been subject to some debate, but evidence has shown that

there are no significant employment or formalization gains in reducing contribution rates.⁸⁵

5.5 National development banks

PDBs are numerous and financially powerful, with mandates that enable them to finance SDG investments in ways that are different from private banks. The June 2023 commitment of 530 multilateral, regional and national PDBs to work as a system and cooperate to align their activities with sustainable development is a milestone in strengthening the potential contributions of NDBs.⁸⁶ According to a recently compiled database, there are more than 500 PDBs in the world distributed across every region, operating at local, national, regional or international levels, including national and multilateral institutions.⁸⁷ PDBs combine three attributes: (i) they are owned, controlled or supported by governments; (ii) they execute a public, development-oriented mandate, addressing market inconsistencies; and (iii) they enjoy an independent legal status and financial autonomy. Operational independence in investment and credit decisions can help to insulate PDBs from political corruption risks. The accumulated assets of PDBs totalled around \$23 trillion in 2021 (figure III.A.16). This includes 10 mega banks that hold 70 per cent of the total—roughly the equivalent of the assets of the entire United States banking sector. The formation of new national PDBs has followed trends in geopolitics and macroeconomics, with surges of bank creation in the 1990s and after 2008.⁸⁸ However, the lack of consistent data on PDBs makes it difficult to assess trends in lending, assets managed and the impact of financing (see chapter IV box IV.4).

NDBs are crucial for mobilizing the required financing, including from private sources, to reach countries' climate and environmental objectives.

Governments have long used NDBs as important financing tools to implement their national economic and social policies, especially to directly finance large infrastructure projects, foster economic growth, reduce poverty and, more recently, address climate change. Today, many NDBs strive to crowd in private investment (domestic and international) to increase the scale and development impacts of private financial flows and to foster capital market development through blended finance and other forms of alternative financing. NDBs can overcome market failures and other barriers to investment in sustainable development, particularly for projects to combat climate change, reduce disaster risk and pursue other environmental objectives. This is due to their greater appetite and ability to bear perceived high risks and long payback periods.⁸⁹ A survey of the largest NDBs shows that more than 80 per cent have adopted green goals. The majority have excluded financing of unsustainable projects and are

leading players in public climate finance, but the share of green assets in their portfolios remains low, with average levels at just 14 per cent.⁹⁰

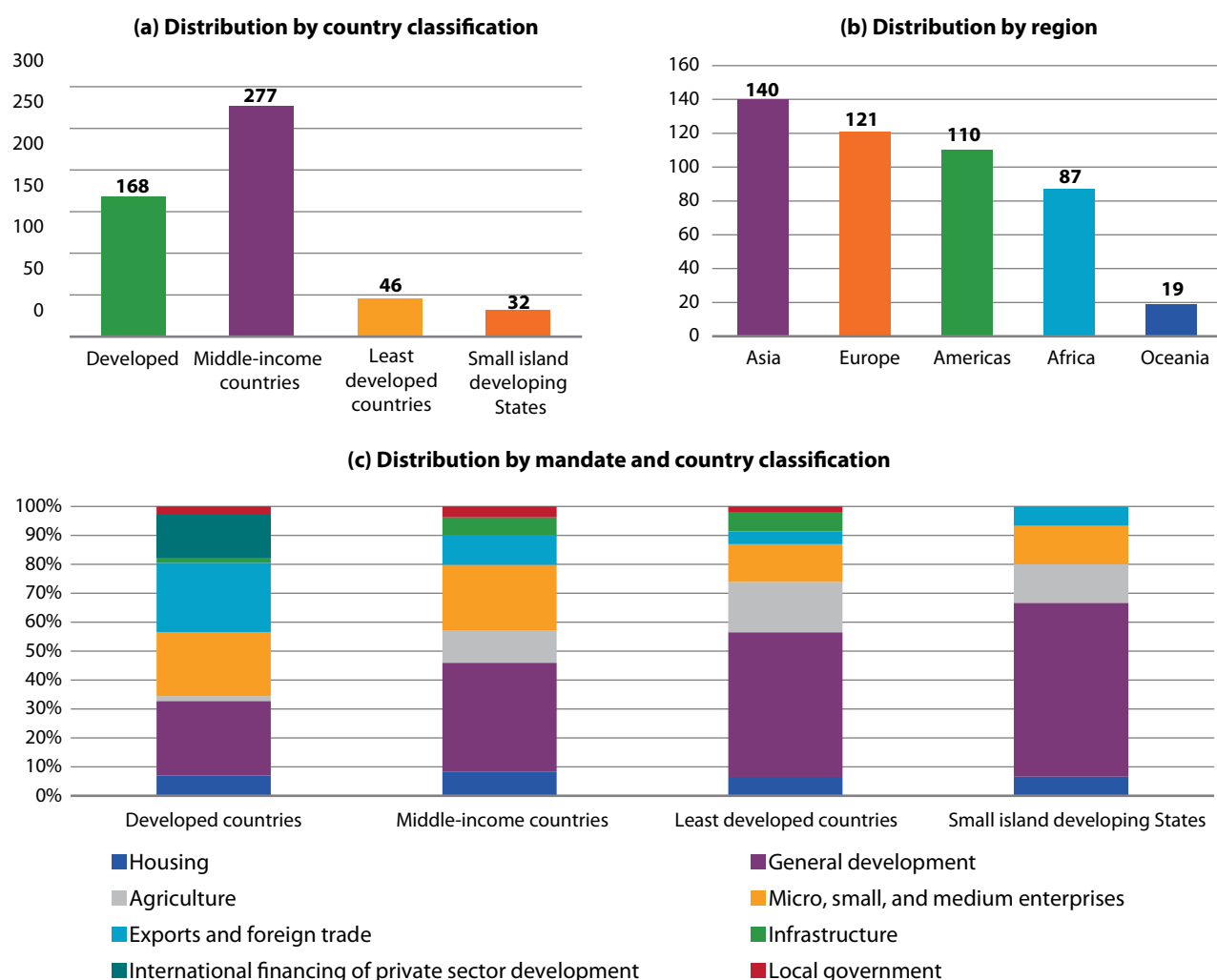
NDBs can also shape markets and raise the standards for all investors.

NDBs usually provide longer-term funding than commercial banks, thus lengthening investor time horizons and better aligning the financial durations of all lending with social and environmental sustainability. In most countries, NDBs play a role in financing small- and medium-sized enterprises, thus influencing the credit worthiness of parts of the private sector (figure III.A.16 panel c). By providing early funding to renewables, they can promote sustainable alternatives to fossil fuel investments. Public banks can also reduce exposure and vulnerability to financial crisis and alleviate their negative impacts by providing countercyclical responses during crises, addressing the drying up of private financing and tax revenue.⁹¹ For example, these institutions played a pivotal role in channelling resources to counter the economic upheaval caused by the COVID-19 pandemic through a countercyclical increase in their operations.

Figure III.A.16

Distribution of national and subnational development finance institutions, 2000–2023

(Number of institutions, percentage)



Source: UN DESA calculations based on Finance in Common data.

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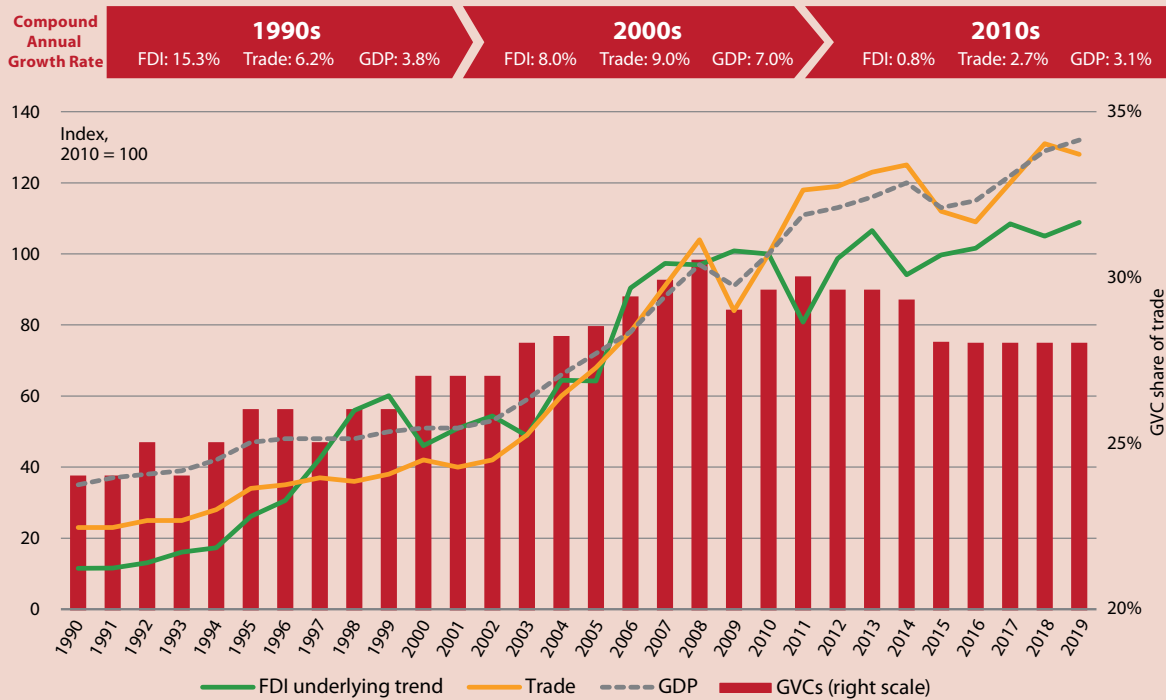
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- 90 Dalhuijsen et al.
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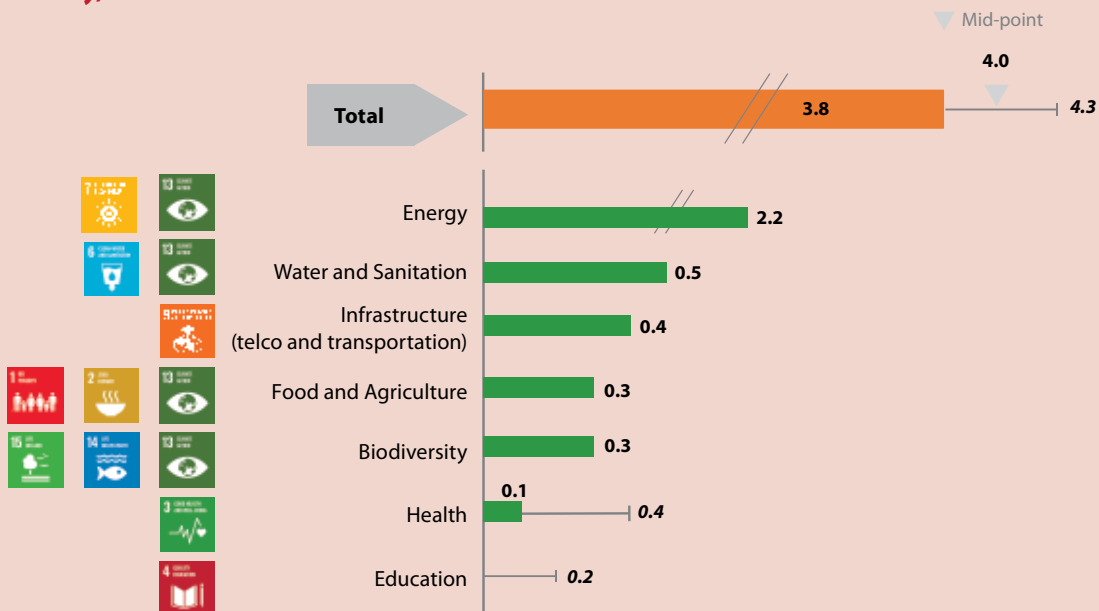


Domestic and international private business and finance in numbers

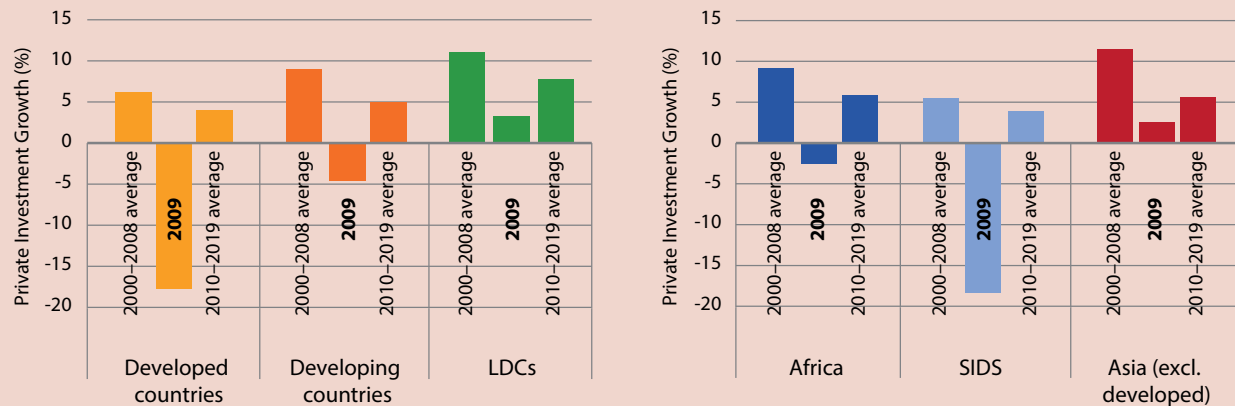
FDI growth slowed significantly after the 2008 world financial and economic crisis, in line with the broader deceleration of global economic growth and trade.



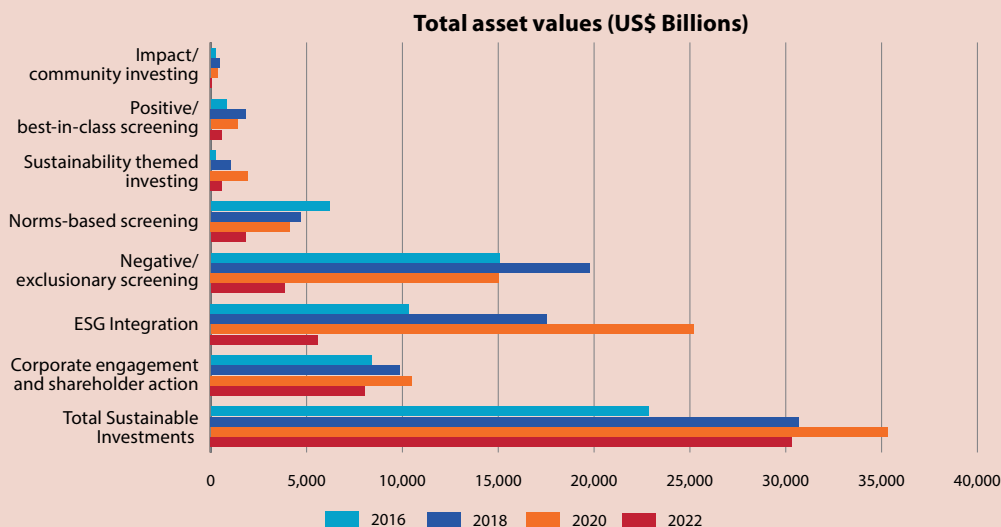
Annual investment gaps across all SDG sectors increased from \$2.5 trillion in 2015 to more than \$4 trillion today, due to underinvestment and additional needs.



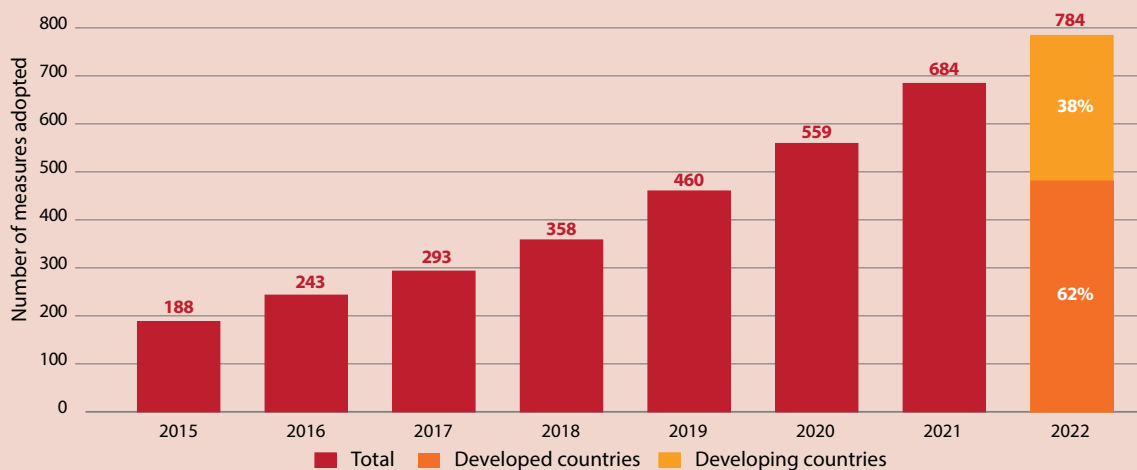
The private sector is at the heart of sustainable growth and development, but its dynamism slowed after the 2008/09 crisis.



Investments in sustainable assets have surged over the past three decades but remain limited in scale and primarily tied to risk mitigation, with impact investing seeing relatively lower adoption rates despite growing interest.



Sustainable finance legislation is increasingly being adopted at the regional and national levels, with a greater number of measures in developed countries.





Chapter III.B



Domestic and international private business and finance

1. Key messages and recommendations

Private business and finance is an important driver of sustainable growth and development. As noted in the Addis Ababa Action Agenda, “private business activity, investment and innovation are major drivers of productivity, inclusive economic growth and job creation”. To deliver on these promises, business activity and investment (both foreign and domestic), need to be dynamic, inclusive, risk-informed and sustainable. However, private sector dynamism slowed after the 2008 world financial and economic crisis, in parallel with the broader macroeconomic growth slow-down, which also led to a widening Sustainable Development Goal (SDG) investment gap. Revitalizing private sector development that is fully aligned with sustainable development will be a core task of the upcoming Fourth International Conference on Financing for Development.

Along with a broader slow-down in global growth, foreign direct investment (FDI) flows have decelerated, revealing disparities in both geographical and sectoral distribution. Investment trends have been highly uneven since Member States convened in Monterrey, Mexico, in 2002. Following rapid acceleration in the 1990s and 2000s, the past 15 years have seen a slowdown in foreign investment, driven largely by shifts from capital intensive activities towards digital business models, “asset-light” forms of production and a servicification of economies. These trends in turn are making “traditional” models of development based on exports of manufactured goods increasingly difficult to pursue. At the same time, the investment gap is continuing to grow across all SDG sectors, reflecting both underinvestment and additional needs, particularly in energy and infrastructure. While investment in these sectors has grown rapidly since 2015, growth has been highly uneven, with much of it concentrated in developed countries and China as well as some large developing countries. Least developed countries (LDCs)

have seen only marginal investment growth over the past two decades and will require dedicated assistance. The Fourth International Conference on Financing for Development will provide an opportunity to agree on ambitious measures to support LDCs and other developing countries to mobilize long-term financing and investment for the SDGs. This could include efforts to tackle the high costs of capital and risk premia, which are thwarting efforts in many developing countries to finance projects across SDG sectors, as well as an Investment Support Centre for LDCs as mandated in the Doha Programme of Action.

Significant structural changes in the global economy are reshaping private investment and developing countries’ ability to integrate productively in the global economy, necessitating a search for new growth and development strategies. Changes have included the geographical concentration of manufacturing in several large developing countries, technological change – most notably digitalization – and unequal gains from global value chains (GVCs). These have contributed to very uneven growth in manufacturing activities, which have traditionally been a “development escalator”, with some regions experiencing “premature deindustrialization”. Nonetheless, some economies have leapfrogged certain stages, developing in non-linear ways, influenced by factors like digitization, global economic shifts, and domestic policy and institutional frameworks.

Today, smaller firms and modern service providers can play a more central role in connecting companies with international supply chains and boosting countries’ industrial transformation. However, relying on services as a basis for economic growth can prove challenging for those developing countries (including LDCs) where energy supply, information and communication technology (ICT) infrastructure and human capital

remain limited. Services also tend to create fewer jobs. As new growth and development strategies – suitable for an age of climate change, rapid technological change and a changing global economy – emerge, there has been renewed interest in sustainable industrial policies to support sustainable and inclusive transformations. The Fourth International Conference on Financing for Development can help to enable the alignment of financing frameworks and actions (across all action areas of the Addis Ababa Action Agenda, at both national and international levels) to facilitate such transformations, taking into account the great diversity and complexity of economic contexts across different developing countries.

Transformation strategies can build on and must complement growing interest and efforts by the private sector to integrate sustainability considerations. While significant progress has been noted in corporate sustainability over the past 30 years, risks of misalignment with sustainability goals persist. On the one hand, companies have actively engaged in voluntary sustainability initiatives to address risks and capitalize on opportunities tied to emerging macro trends and stakeholder expectations. On the other hand, however, short-term-oriented decision-making, particularly evident in moments of crisis, reveals the ongoing need to redefine the broader “rules of the game” via policy frameworks. This includes shifting focus from minimizing the negative consequences of shocks when risks are realized, to preventing the creation of risks and reducing existing risks before these manifest as shocks.

A more dynamic and sustainable business sector will only arise with more inclusive and sustainable financial markets. Lack of access to affordable finance and financial incentives misaligned with sustainability are often among the most binding constraints for sustainable private sector development. While important progress was made towards financial inclusion, with more than half a billion people gaining access to financial services between 2017 and 2021 alone, the availability of long-term financing continues to be a challenge for small- and medium-sized enterprises (SMEs) and individuals, particularly in developing countries. Short-term incentives and decision making also often stand in the way of more sustainability – with longer-term investors more inclined to incorporate sustainability risks into their decision making, and to seek companies that prioritize long-term business fundamentals over short-term targets. Efforts to extend investors’ time horizons, such as those being proposed by Global Investors for Sustainable Development in preparation for the Fourth International Conference on Financing for Development, are imperative to align private actions with long-term sustainable development trends; stability, sustainability and greater access to financing are mutually reinforcing.

Following the rapid emergence of sustainable finance over the past 25 years, the current moment offers a chance to accelerate progress. Investor interest in sustainable finance has grown steadily since the 1990s, with a net expansion from 2015. Sustainable fund flows have remained relatively resilient, consistently surpassing 2016 levels since then despite year-on-year fluctuations following the COVID-19 pandemic. But sustainable fund assets still make up a small percentage of total global assets under management today, estimated at less than 5 per cent of the global fund market in 2023. Furthermore, impact investing, designed to contribute to real-world solutions in line with the SDGs, represents only a small portion of sustainable assets. Weaknesses related to the field’s information infrastructure that have given rise to greenwashing concerns, are

compounded by an enabling environment that still incentivizes traditional investment strategies. Growing political polarization of the field has also led to a backlash in some countries. Against this challenging backdrop, the field has commenced a journey towards maturation, marked by the refinement and consolidation of voluntary standards and the enactment of legislation at the national and regional levels. The upcoming Fourth International Conference offers an opportunity to continue collaborating towards (i) the interoperability of sustainable finance legislation across regions to prevent uneven progress and heavy compliance burdens, while accounting for regional and local specificities; (ii) the adoption of mandatory national disclosure standards with a double materiality vision; (iii) frameworks and carefully crafted incentives for impact investing at scale to align capital markets with real-world impact; and (iv) a broader set of macroeconomic policies that create enabling conditions for sustainable transformations.

This chapter will give a brief overview of investment trends in the past two decades, including investment trends in sustainable transformations. It will then discuss developments in aligning business activity with sustainable development, including efforts to strengthen the business environment and private sector development in a changing global economy. Lastly, the chapter discusses trends and progress in achieving a financial sector that is both inclusive and sustainable.

2. Investment trends in an evolving global economy: The long view

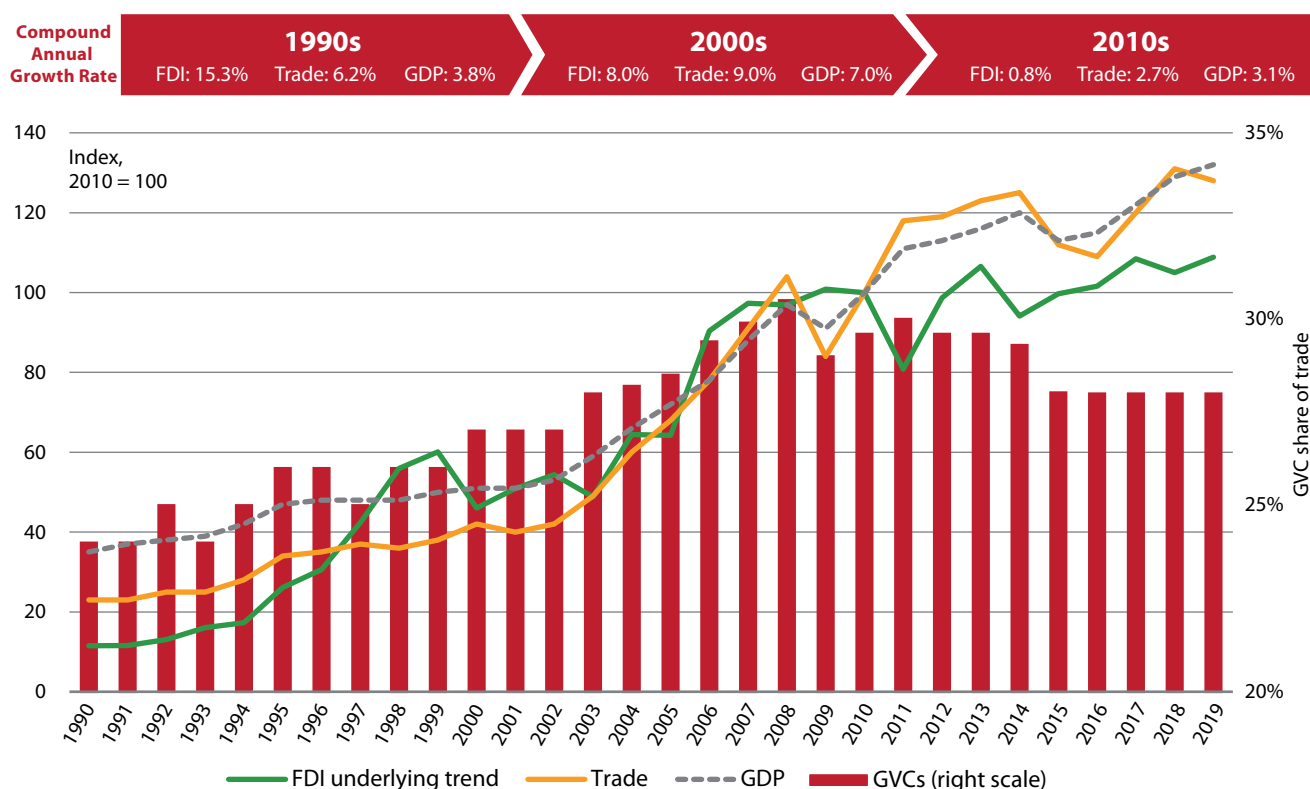
2.1 Foreign direct investment trends since Monterrey

Since Member States convened in Monterrey in 2002, global foreign investment patterns have changed dramatically, with the 2008 world financial and economic crisis proving to be an inflection point. In the context of massive changes in the global division of labour and rapid technological change, including the shift towards digital business models and asset-light forms of production, increased geopolitical fragmentation and accelerating climate change, FDI trends have shifted over the past decades, evolving in terms of volume, direction and sectoral breakdown. A number of crises, including the 2008 world financial and economic crisis and the COVID-19 pandemic, have proved to be inflection points, accelerating trends driven by structural rather than transitory factors. Amid changing investment patterns, growing efforts to align foreign investment trends with sustainable development have thus far fallen short of what is needed to achieve the 2030 Agenda for Sustainable Development. Changing FDI patterns have also cast doubts on the viability of “traditional” models of economic development based on attracting FDI and exports of manufactured goods.

The first International Conference on Financing for Development in Monterrey took place against the backdrop of a decade of FDI expansion – a trend that has since slowed and, more recently, stalled. Enabled by an acceleration of technological progress and fuelled by the quest for low labour costs and increased productivity, the 1990s and early 2000s saw a rapid growth in global FDI stocks, along with a rapid expansion of global trade (figure III.B.1). This trend slowed markedly following the 2008 world financial and economic crisis. FDI growth slowed

Figure III.B.1

Foreign direct investment and trade trends, 1990–2019



Source: UNCTAD.

Note: Trade is global exports of goods and services. GVC share of trade is proxied by foreign value added in exports, based on the UNCTAD-Eora GVC database (see Casella et al., “Improving the analysis of global value chains: the UNCTAD-Eora database”). The underlying FDI trend is an UNCTAD indicator capturing the long-term dynamics of FDI by netting out fluctuations driven by one-off transactions and volatile financial flows. CAGR: Compound annual growth rate.

dramatically compared to average growth rates in the 2000s, increasing only 0.8 per cent on average in the 2010s along with decelerating trade growth and a stagnation in GVCs. The shift towards digital business models and asset-light forms of production, a rise in protectionism and policy uncertainty as well as the COVID-19 pandemic have contributed to this slowdown. In 2023, global FDI marginally increased to US\$1.37 trillion, following a decline in 2022.¹

The growth and integration of developing countries into the global economy has been a major driver of FDI trends. Against the backdrop of a changing global economic landscape outlined in chapter I, developing countries have accounted for increasing shares in both inward and outward FDI. As shown in figure III.B.2a, in 2018, developing countries eclipsed developed countries for the first time as a destination for FDI flows, gradually doubling their share from around one third to two thirds of global FDI. While developing countries as a group have increased their share, including due to the rise of China as major recipient of inward FDI, LDCs continue to trail behind. Over recent years, LDCs have seen only a 0.5 percentage point higher inflow of FDI than over a comparable time frame between 2002 and 2004. Developing countries have also increased their share of outward FDI, which rose significantly from 7 per cent in 2002 to around one third of all FDI (31 per cent) in 2022. As shown in figure III.B.2b,

China has played an increasingly important role as a source country of FDI since the mid-2000s.

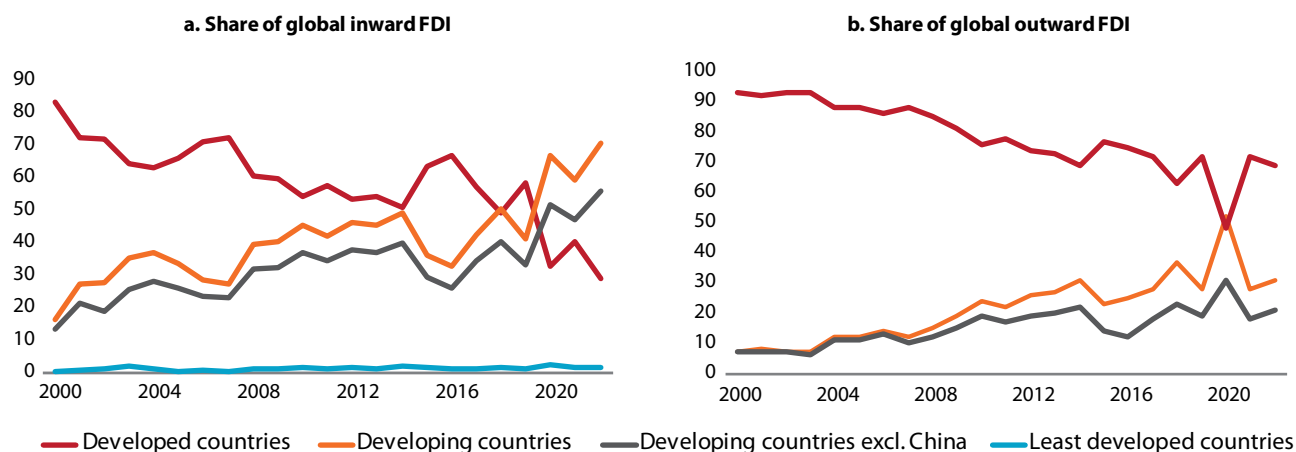
In addition to changes in volume and direction, FDI flows have also seen a transformation in composition. FDI flows into services sectors have expanded significantly, fuelled by an increased internationalization of services and a servicification of manufacturing. These trends, together with accelerating digitalization, have contributed to a slowdown of cross-border investment in physical assets, as international investment has been increasingly directed towards more intangible and asset-light modes of production. Accordingly, greenfield investment in manufacturing has dropped by up to a quarter, making it harder for countries to pursue export-based development models contingent upon inward greenfield FDI for capital formation. In addition, as figure III.B.3 suggests, the share of developing countries in global greenfield investment by value has declined below its long-run average of around 56 per cent and below the respective share of developed countries.

2.2 Investment trends in sustainable transformations

Have investment trends facilitated sustainable transformations for the 2030 Agenda for Sustainable Development? Despite some

Figure III.B.2

Share of global inward and outward FDI, 2000–2022 (Percentage)



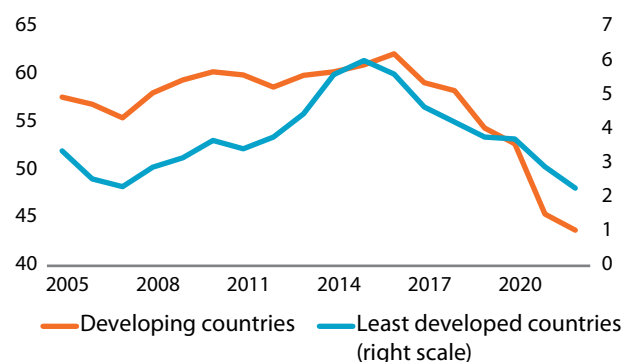
Source: UN DESA calculations based on UNCTAD data.

progress, the answer thus far is no, or rather not yet. A review of investment needs suggests that the investment gap across all SDG sectors has increased from \$2.5 trillion in 2015 to more than \$4 trillion per year today, due to both underinvestment and additional needs² (see also chapter I). Investment needs continue to be particularly large in the area of energy and infrastructure (figure III.B.4). While international investment in the renewable energy sector has nearly tripled since the adoption of the SDGs and the Paris Agreement, this growth has been unbalanced, with much of it concentrated in developed countries and China. Installed capacity and new investments still fall far short of what is needed to meet the Paris goals, with an additional 578 GW of installed capacity in emerging renewable technologies required by 2030. The largest gaps are in Africa and the Middle East, where capacity needs to grow more than tenfold by 2030, requiring cumulative investment of \$1.36 trillion (figure III.B.5).

Figure III.B.3

Share of global greenfield investment by developing countries and LDCs, 2005–2022 (Percentage)

Three-year moving average



Source: UN DESA calculations based on UNCTAD data.

Achieving energy transitions for sustainable development requires significantly scaled-up investment in a number of sectors, but the high cost of capital in developing countries remains a significant obstacle. A number of factors have hampered the channelling of sufficient investment in necessary infrastructure, the entire renewable energy value chain, alternative technologies and energy efficiency. FDI flows have largely been directed towards renewable energy generation, but much less so to related critical industries or to those developing countries where investment needs are greatest. Project financing continues to be hampered by the high cost of capital in developing countries, which is driven more by macroeconomic risk perceptions than by project risk. Indeed, the cost of capital for comparable projects is significantly higher in developing countries than in developed countries; perceived macroeconomic risks play a much larger role in explaining risk premia than project-specific/micro risks (table III.B.1). Such a high cost of capital is a significant impediment to investment in both renewable infrastructures and other necessary long-term investments in the SDGs. Overall, the high cost of capital, particularly in countries in debt distress or with high-risk ratings, is a strong disincentive for investors to shift towards renewable energy assets.³

Table III.B.1

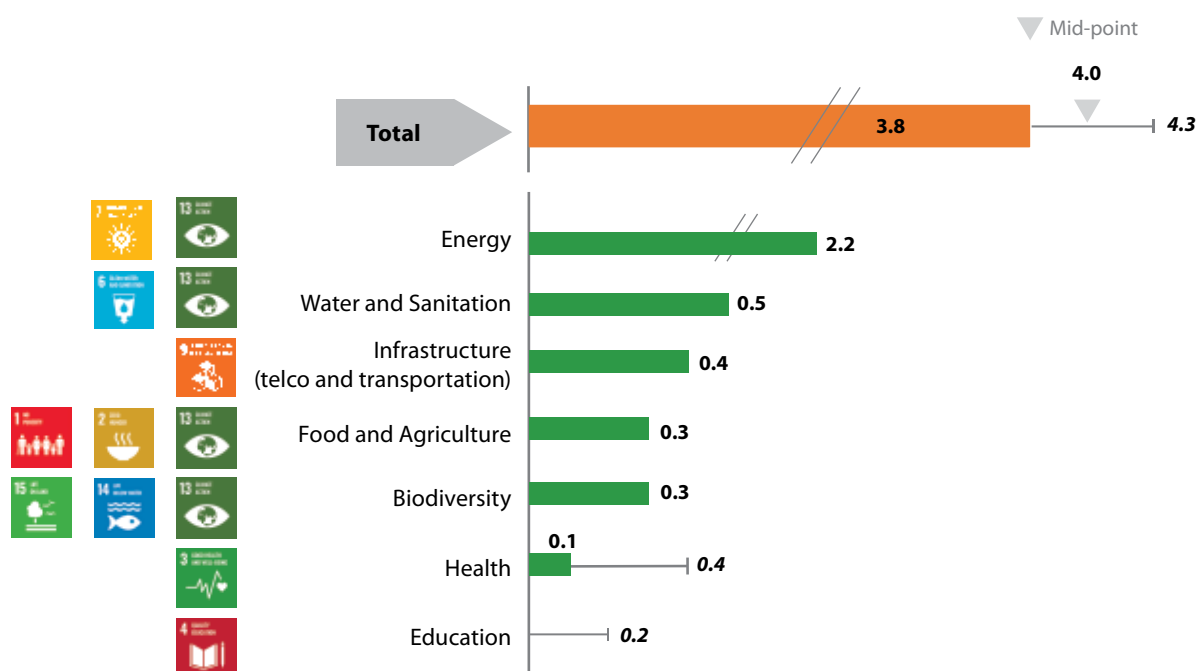
Comparative project risks and weighted cost of capital for developed and selected developing countries

Country category	Weighted cost of capital	Government cost of borrowing	Project risk
Developed countries	4.0%	-0.3%	4.3%
Industrializing developing countries	10.6%	7.7%	2.9%

Source: Persaud, "Unlocking the green transformation in developing countries with a partial foreign exchange guarantee", based on IEA and Bloomberg data.

Note: The sample of industrializing developing countries comprises Brazil, India, Indonesia, Mexico and South Africa. Cost of government borrowing reflects ten-year government bond rates for 2021.

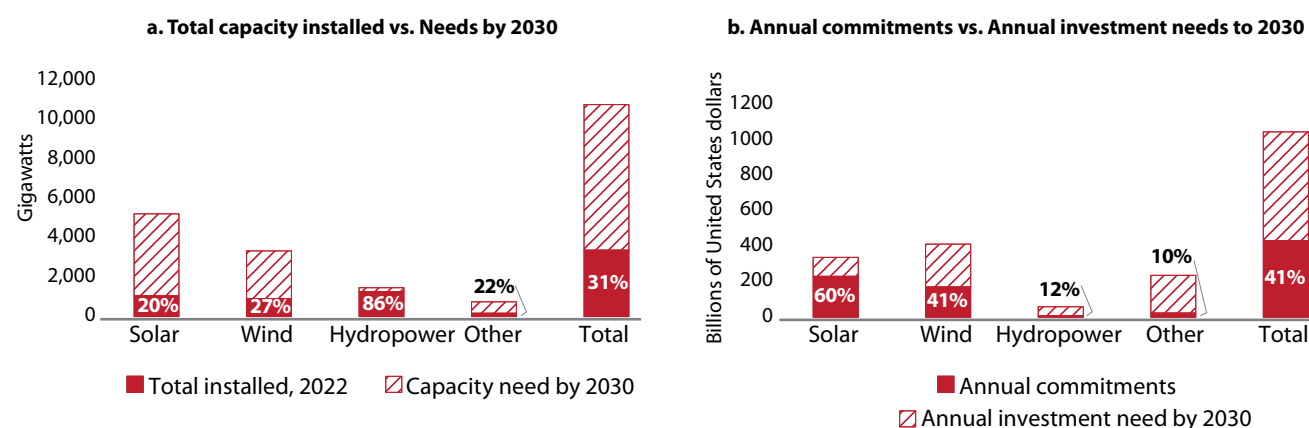
Figure III.B.4

Estimated annual investment gap (public and private) in key SDG sectors
 (Trillions of United States dollars)


Source: UNCTAD, SDG Investment Trends Monitor (Issue 4).

Note: Figures are rounded at the first decimal (\$100 billion). Investment refers to capital expenditure (capex). The range reflects the uncertainty about the size of the capex component investment gap for two sectors (Health and Education) for which the operational expenditure component is substantial.

Figure III.B.5

Renewable energy: Global total installed capacity and investment needs


Source: UNCTAD.

As investment in manufacturing capacity is stagnating and investment trends are aligning with asset-light and digital business models, new investment strategies and development pathways need to be found. These could include investment promotion and facilitating strategies aimed at attracting investment in areas such as digital infrastructures and innovation, as well as infrastructures that can act as enabling environments for thriving service sectors. This is likely to prove particularly challenging for LDCs, which will require significant support. It also highlights the role of international development cooperation (see chapter III.C) and of multilateral development banks in facilitating and investing in this shift towards new development pathways (see box III.B.1 regarding the World Bank's Private Sector Investment Lab and box III.B.2 on the Global Emerging Markets Risk Database Consortium). Blended concessional finance for private sector projects is one of the most valuable tools that development finance institutions (DFIs) can use, in cooperation with donors and other development partners, to help address the SDGs, increase finance and mobilize private capital (see chapter III.C). Initiatives like the ECOSOC SDG Investment Fair hosted by UN DESA provide a platform for connecting governments, investors, DFIs, and the UN SDG investment ecosystem. This initiative helps to devise solutions that enable the mobilization of private investment for projects that significantly contribute to the achievement of the SDGs. Since its launch in 2018, 23 countries have participated and over 130 projects have been presented, amounting to over \$50 billion in SDG-aligned investment opportunities.

Box III.B.1.

World Bank-led Private Sector Investment Lab

The Private Sector Investment Lab, launched in 2023, is composed of a group of 15 chief executive officers (CEOs) of leading global institutions who have agreed to provide their insights, expertise and experience to help the World Bank Group scale up the mobilization of private capital for financing climate and other development priorities in emerging economies. The Lab has identified five areas as critical to private capital mobilization on which its work is currently focused. These are: guarantees; foreign exchange (FX) risk solutions; scaling capital markets and securitization solutions to distribute assets; country level approaches to

3. Aligning business with sustainable development

3.1 Private sector development in a changing global economy

Private sector development is at the heart of sustainable growth and development; yet private sector dynamism slowed following the 2008 world financial and economic crisis, in parallel with the broader macroeconomic growth and FDI slow-downs discussed above. As noted in the Addis Ababa Action Agenda, “private business activity, investment and innovation are major drivers of productivity, inclusive economic growth and job creation”. The private sector contributes 84 per cent to GDP and 90 per cent to job creation in developing countries.⁴ It is private sector development that creates technological and organizational capabilities at scale, the resource base for revenue mobilization, and the vast majority of decent jobs in most countries. Yet, private sector dynamism stuttered after the 2008 world financial and economic crisis, following a period of very high rates of private investment growth, during the first decade of this century, particularly in developing regions such as Africa and Asia. Many economies witnessed a strong contraction in private investment in 2009 and only a partial subsequent recovery, with

improve enabling environments and support bankable project pipelines; and mobilizing early-stage capital for high impact projects. The aim is to turn the Lab's ideas into action through the development of new instruments of intervention and delivery mechanisms, some of which will be tested through pilot projects. The Lab will continue to work towards developing and scaling new and existing innovative solutions for private capital mobilization in partnership with all relevant stakeholders. Specific projects that can serve as pilots for testing and, if successful, scaling up, are already being discussed, with new solutions to be developed pursuant to Lab recommendations.

Source: World Bank.

Box III.B.2.

Global Emerging Markets Risk Database Consortium

The Global Emerging Markets Risk Database (GEMs) Consortium is one of the world's largest credit risk databases for the emerging markets operations of multilateral development banks and development finance institutions that are members of the initiative. GEMs pools data on credit defaults on the loans extended by members, the migrations of their clients' credit rating and the recoveries on defaulted projects. GEMs was established in 2009 as a joint initiative between the European Investment Bank (EIB) and the International Finance Corporation (IFC) and has now grown to 25 members. Consortium members contribute anonymized data on their projects' credit events notably in emerging markets and developing economies. The GEMs Consortium has been publicly disseminating statistics through its website since 2020 to address the

need for greater volumes of private investment tackling sustainable development goals in the most challenging markets. This was initially done through annual reports focusing on default rates for private/sub-sovereign lending. Starting in 2022, the reports have also covered sovereign and sovereign-guaranteed lending. The latest default statistics were published in November 2023 on the GEMs website. For both lending universes, statistics are disaggregated across regions, income groups, sectors, and counterpart types. The publication on private/sub-sovereign lending also showcases specific statistics for infrastructure. In the first quarter of 2024, the GEMs Consortium will publish for the first time recovery statistics for private and sub-sovereign lending from 1994 to 2022, building on more than ten years of successful cooperation among GEMs members.

Source: World Bank.

growth rates substantially below pre-2008 levels (figure III.B.6). The recent COVID-19 pandemic has further slowed – if not reversed – gains from private sector development in many developing countries and LDCs.

Private sector development has traditionally been associated with industrialization and diversification, which in turn facilitated sustained economic development and improvements in living standards. Such structural transformations involve the reallocation of capital and human resources from low- to high-productivity activities and sectors through economic diversification and strengthening productive linkages in the economy (see the *Financing for Sustainable Development Report 2023*). Historically, a thriving manufacturing sector has often been at the heart of such transformations, because of several unique properties: technological advances often originate in the manufacturing sector, and developing countries were able to import these and achieve rapid productivity growth even when broader institutional capabilities and skills were still comparatively scarce. Many low-skilled workers found employment in manufacturing; and its products are tradeable, hence growth was not limited by the small size of domestic markets in many developing countries.⁵ Overall, more diversified economies tend to have higher per capita incomes and better long-term growth prospects, are less volatile and do better on poverty reduction.⁶ Since 2000, less diversified economies – usually commodity exporting developing countries – have tended to experience higher volatility and have been less likely to experience stable growth rates (see chapter III.D).

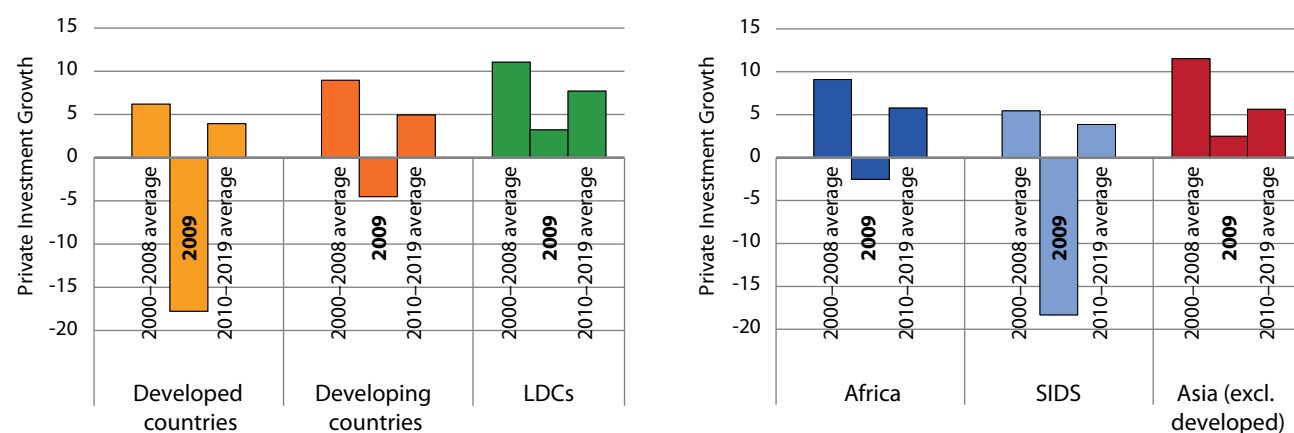
Manufacturing has become less effective as a development escalator. At the current pace of progress, the world will not achieve SDG 9 and its industry-related targets. Developing countries face significant challenges, notably African LDCs, which have seen manufacturing value-added mostly stagnate as a share of GDP over the past 20 years (figure III.B.7). This phenomenon has been described as “premature deindustrialization”: as economies grow and per capita income rises, the share of labour employed in manufacturing tends to first rise and then fall. Since the 1980s,

this turning point has arrived at increasingly lower levels of per capita income, with workers moving from agriculture to services such as trade and hospitality rather than manufacturing or modern services. Productivity growth has declined, with working conditions often characterized by widespread informality in countries where this premature deindustrialization is taking place, particularly in Africa and Latin America. Where jobs are being created, it is usually by small, less productive, and often informal manufacturing companies. Moreover, where natural resource exports or capital inflows provide external fuel to growth, growth dynamics tend to be fragile and exposed to global market shocks.⁷ Several factors are responsible:

- The **geographic concentration** of manufacturing activities in a few large economies and regions. This trend results from the streamlining of supply chains and the search for price competitiveness by producers. For example, China has emerged as the preeminent global manufacturing hub, producing 28.7 per cent of global manufacturing output in 2019, up from only 8 per cent of the global total in 2004;
- Productivity-enhancing **technological change**, primarily in advanced economies. While the emergence and diffusion of advanced digital production technologies is creating new opportunities for developing countries, they have also “raised the bar” for these same countries to develop a modern manufacturing sector and may limit employment creation opportunities, particularly considering the lack of affordability of some advanced technologies. New technologies facilitate small-scale manufacturing, and additive manufacturing allows firms to cut down on production by reducing the cost of customization while enabling creative firms to compete thanks to their knowledge of local needs. New business models based on the collaborative economy allow small firms to take advantage of under-utilized resources to reach scale, become more competitive, and improve the efficiency of environmental resource use. New communication technologies can also help firms to participate in global trade. Companies can reach

Figure III.B.6

Private investment growth slowed in most regions during the 2010s
(Percentage)



Source: UN DESA calculations based on IMF data.

Note: Private investment is defined as private gross fixed capital formation in constant 2017 dollars. LDCs: Least developed countries; SIDS: Small island developing States.

markets beyond their geographical location with an online presence. Yet, there is a need to better understand and manage the risks associated with rapid technological change. Technological changes and digitalization can decrease the demand for low-cost labour in manufacturing and increase the need for skills. As a result, it may reduce the incentive for multinational companies to offshore production to countries with low-cost labour.⁸

- The **rise in GVCs**, which has created opportunities for firms in developing countries but with a very unequal distribution of gains. Between 2002 and 2022, global trade in intermediate goods (a proxy for GVC trade) more than tripled, with Asia and Europe accounting for 40 per cent and 34 per cent of GVC trade, respectively, even with the more recent slowdown of their expansion (see chapter III.D). Elsewhere, firms have found it more challenging to integrate into GVCs. Lead firms have seen increasing mark-ups and profits, suggesting that a growing share of cost reductions from GVC participation is not being passed on. Large firms in developing countries have adopted more capital-intensive technologies, similar to their peers in advanced markets. At the same time, mark-ups for producers in developing countries are declining and gains from GVC participation can be lost if a country's private sector is unable to continue upgrading its activities.⁹ Countries can industrialize through GVCs thanks to the possibility of specializing in certain tasks. However, investing in the wrong combination of skills and production patterns could limit the opportunity to upgrade, innovate and break into more sophisticated value chains – effectively trapping firms in stagnating segments and low value added activities and “hollowing out” the domestic manufacturing sector.¹⁰ More broadly, GVCs can exacerbate the unequal distribution of gains, skills and wages within the labour market and across country groups. It is also crucial to identify and address vulnerabilities in GVCs, especially more sophisticated ones, as this increases the potential for risk exposure. Making production decisions based on risk assessment can also facilitate moving away from cost-based competition, safeguard against disruptions and promote more sustainable and resilient industries.

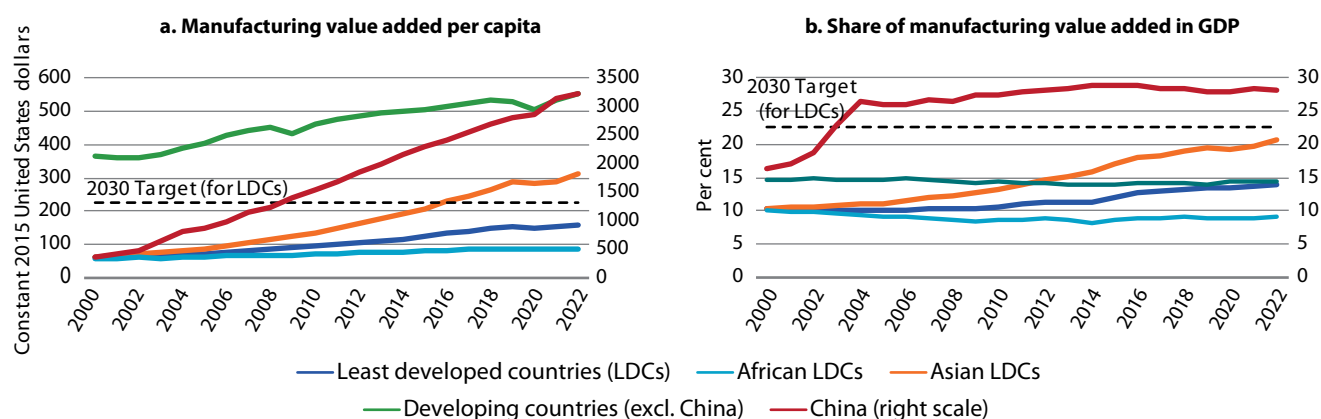
Today, modern services can play a more central role in connecting firms with international supply chains and boosting the industrial transformation of countries. Together with digital technologies, international supply chains rely on four services sectors – financial services, ICT, transport and logistics, and business and professional services – for their functioning. These service sectors have also become major sources of employment creation, exports, FDI, and innovation. Through linkages to other sectors, their presence also enhances the competitiveness of firms in other fields. For example, in regions with high-quality connected services, 44 per cent of all companies are engaged in export, compared with 19 per cent of firms where such services are weaker.¹¹ The services sector can allow firms to tap into value chains for manufacturing products that would otherwise be beyond their capability. Modern communications technology and the fall in transport costs have created opportunities for developing countries to export ancillary services such as back-office processing (e.g., customer care or data handling).¹² However, relying on services can prove challenging for those developing countries (including LDCs) where energy supply, ICT infrastructure, and human capital remain limited. In this case, policy makers can play a major role in helping their countries and firms become competitive in high-productivity manufacturing-related services (see section 3.3 and chapter III.B of the *Financing for Sustainable Development Report 2023*).

Private sector development, decent jobs and gender equality

Private firms account for the vast majority of employment creation in most countries; in a challenging global context the creation of sufficient and decent jobs remains a major challenge in many developing countries. Global employment growth has slowed down significantly since the 2008 world financial and economic crisis along with the broader deceleration of growth, trade and investment. While employment growth averaged 0.9 per cent per year between 2000 and 2008, it has fallen to only 0.1 per cent annually since then. Countries that have successfully transformed their economies, such as Bangladesh, China and Thailand, have also created good jobs on a large scale. For example,

Figure III.B.7

Prospects of least developed and developing countries achieving SDG target 9.2



Source: UN DESA calculations based on UNIDO data.

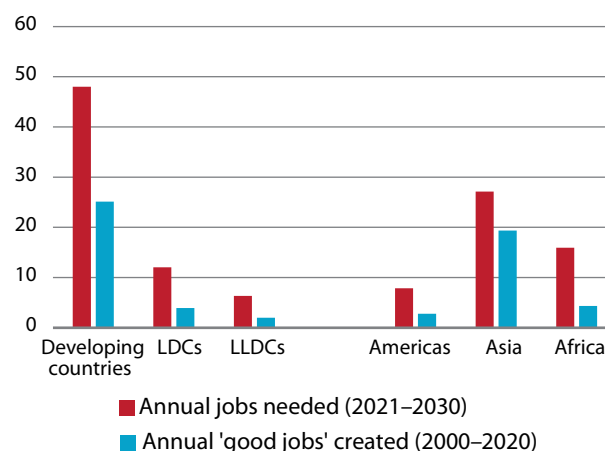
Note: 2022 per capita manufacturing value added levels for Developing countries (excl. China) are based on 2021 population figures.

between 2003 and 2016, Bangladesh experienced an almost 10 percentage point shift in the share of employment towards manufacturing and services. Waged jobs grew by almost 6 per cent annually, almost three times faster than the increase in the workforce. Moreover, 70 per cent of all new jobs created went to women.¹³ As manufacturing-based and labour-intensive transformations become more challenging, closing the “decent jobs”¹⁴ gap is emerging as a major challenge (figure III.B.8).

The quality of employment also remains a critical challenge. High levels of informality still prevalent in many developing countries result in gaps in social protection coverage and limit revenue mobilization, holding back socio-economic development. This

includes the negative effects of informality on labour productivity and human capital accumulation. Fifty-eight per cent of jobs globally, or around 2 billion people, remain in the informal sector, mostly but not exclusively in developing countries. Around 90 per cent of total employment in LDCs and low-income countries can be considered informal, compared to 67 per cent in middle-income countries and 18 per cent in advanced economies.¹⁵ A great majority of workers in the informal economy and their families do not have access to adequate healthcare and income security, and as a result are particularly vulnerable to economic shocks.¹⁶ Most workers in the informal economy are not affiliated with contributory

Figure III.B.8
Annual jobs needed and quality jobs created
(Millions)

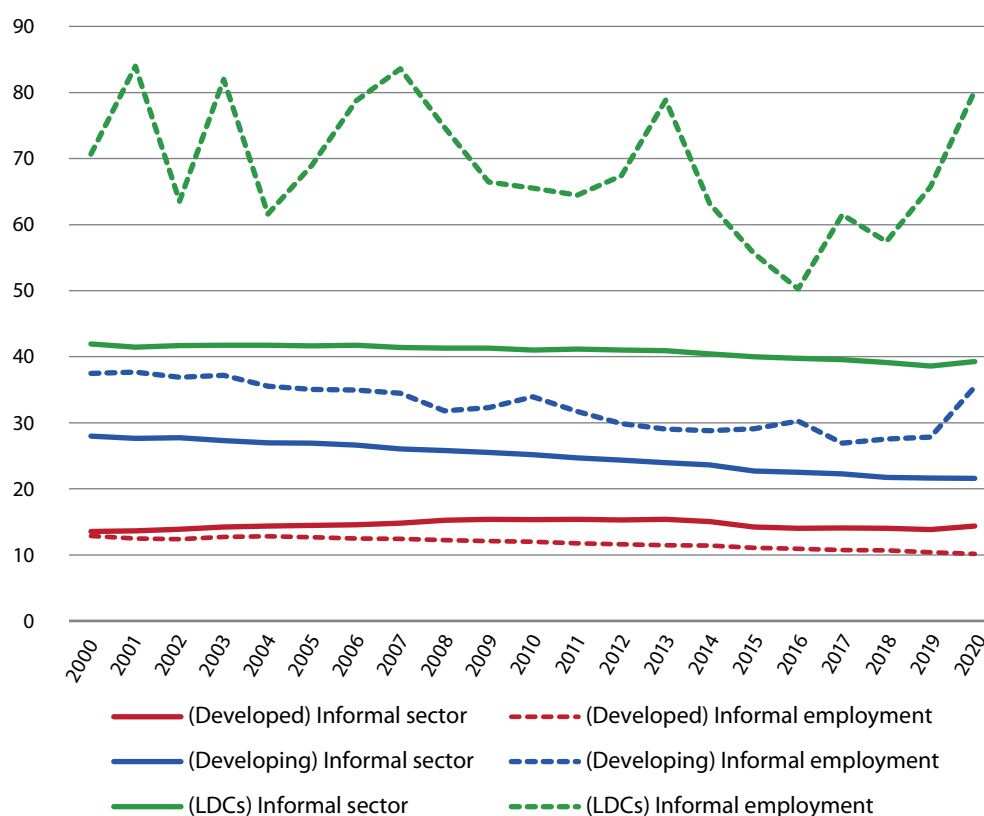


Source: UN DESA calculations based on World Bank data.

Note: LDCs: Least developed countries; LLDCs Landlocked developing countries.

Figure III.B.9

Informal activity (share of GDP) and self-employment rates (share of employment), 2000–2020
(Percentage rates)



Source: UN DESA calculations based on Elgin et al. and World Bank data.

Note: LDCs: Least developed countries.

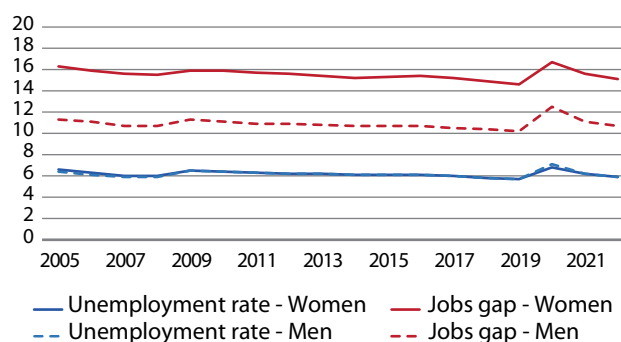
schemes, nor are they reached by narrowly targeted “safety nets”, as they are not considered “poor enough” to qualify for these. Many countries have introduced forms of mandatory coverage, while others have opened social insurance to informal economy workers and micro-entrepreneurs with mixed results.¹⁷

High levels of informality and a dearth of decent jobs are related to younger and smaller firms accounting for a large proportion of economic activity and job creation in many developing countries. Many jobs created by young, small or informal firms are in low-productivity sectors, with unequal employment opportunities, lower wages and limited access to social protection. In 2019, more than 630 million workers worldwide (19 per cent of all those employed) did not earn enough to lift themselves and their families out of poverty.¹⁸ Moreover, and in the event of shocks and crises, economies relying on smaller firms tend to take a bigger hit, as micro-, small- and medium-sized enterprises (MSMEs) tend to have fewer assets and limited cash reserves to cushion against slowing demand and liquidity shortages. An example of this are SMEs in the agrifood sector, which are often scattered, small to very small, informal and family-based and lack economies of scale – with jobs in these tending to be highly insecure.¹⁹ In the case of the COVID-19 crisis, MSMEs, particularly in developing countries, were severely impacted and faced a higher risk of permanent closure. In August 2020, 22 per cent of MSMEs surveyed reported that they risked shutting down permanently within three months, compared to 9 per cent for large firms and 34 per cent for companies operating in LDCs.²⁰ While SMEs can occupy niches of digital success, it is large firms that are typically associated with frontier innovation. These companies can usually afford higher levels of research and development expenditure, have more experience and can more easily form partnerships or prompt government intervention.²¹

Gender inequality remains pervasive and persistent in the labour market. Gender inequality in employment access has remained a major challenge with no improvement registered since 2005. Worldwide, the labour force participation rate of women stands at 47 per cent, compared to 73 per cent for men. The gender gap remains a major concern across all regions, ranging from 11 percentage points in Europe to 30 percentage points in Asia.²² Improved educational attainment among women has done little to shift deeply entrenched occupational segregation in both developed and developing countries. As a result, the global gender pay gap persists, with women earning 51 cents to every dollar earned by men.²³ Part of this is attributable to the time women dedicate to unpaid care and domestic work, which was 3.3 times more than men in 2014 and has decreased to 2.6 times more in 2023.²⁴ The smallest jobs gaps are found in high-income countries, with men registering an unemployment rate of 7.4 per cent and women 9.6 per cent. However, as national income decreases, the jobs gap between women and men increases, reaching 24.9 per cent and 17.4 per cent in low-income and lower-middle-income groups, respectively.²⁵ This points to persistent and structural problems worldwide. Women additionally face challenges in more competitive and open sectors: firms integrated into GVCs may offer jobs to more women, but such firms seem to have even lower glass ceilings. Women are generally found in the lower value added segments, and it is hard to find women owners and managers. The share of women in informal employment exceeds that of men in 56 per cent of countries, especially in low- and lower-middle-income countries.²⁶

Figure III.B.10

Unemployment and jobs gap rate by gender, 2005–2022 (Percentage)



Source: Gomis et al., “New Data Shine Light on Gender Gaps in the Labour Market”.
Note: The jobs gap rate measures the share of persons who would like to work but do not have a job.

3.2 Sustainability in business

In the past 30 years, businesses have increasingly factored in sustainability considerations driven by the recognition of their long-term benefits, but risks of misalignment or backtracking underscore the need to redefine the “rules of the game”. In efforts to try to fill remaining gaps (e.g. see aforementioned gender disparities), companies today are routinely integrating sustainability issues in their decision-making. Yet, despite much greater awareness of environmental, social and governance (ESG) factors, many business activities and investments remain misaligned with sustainable development due to short-term incentives and the absence of enabling environments for long-term decision-making. To fully align business models with sustainable development will require redefining the rules of the game, including through legislation or regulations, coupled with incentivizing financial markets to be a catalyst for change (see section 4.2).

A longstanding relationship between business and society

Modern interpretations of corporate responsibilities to society evolved with globalization and the internationalization of sustainable development. The first notions of the contribution of business to society have been traced back to as early as ancient Mesopotamia and ancient Rome.²⁷ Modern interpretations of what has been termed “corporate social responsibility” (CSR) arose in the 1950s²⁸ and broadened with the rise of an international approach to sustainable development. In 1999, the concept of “triple bottom line” provided a sustainability framework that aims to balance a company’s social, environmental and economic impact. In the same year, in Davos, Switzerland, United Nations Secretary-General Kofi Annan proposed what subsequently became the UN Global Compact. Twenty years later, the Business Roundtable codified the new purpose of corporations as stakeholder capitalism, extending beyond solely serving shareholders.

Driven by globalization and other systemically significant trends, alongside stakeholder pressures, companies have increasingly acknowledged the importance of addressing sustainability risks and opportunities. Globalization expanded the reach of multinational

corporations into diverse business environments, often with weak regulatory frameworks, introducing new reputational, legal and operational risks. In response, companies adopted voluntary internal sustainability policies to ensure uniform management across territories (e.g. transparent supply chains to avoid human rights risks). Moreover, the emergence of new systemic risks (e.g. climate change) and environmental, social, or economic crises (e.g. the 1989 Exxon Valdez oil spill, the 2008 world financial and economic crisis, COVID-19) contributed to reshaping perceptions of the role of business in society and companies' own risk assessments. Evolving stakeholder expectations further influenced companies' cost/benefit analyses on the integration of sustainability issues. Among these expectations are investors' pursuit of more sustainable investment options and the update of their policy frameworks which encourages more attention to sustainability risks and opportunities (see section 4.2), the growing preference of consumers for ethical products, a modern workforce leaning towards purpose-driven employers, as well as the heightened regulatory focus of policymakers on corporate duties. Regulation, at the international level at first, and more recently also at the national level, has focused on both corporate operations and supply chains. Prominent examples of the latter including the United States' 2010 Dodd-Frank Act (which regulates conflict minerals), the United Kingdom's 2015 Modern Slavery Act (which includes a clause on transparency in supply chains), France's 2017 Duty of Vigilance law, Germany's 2021 new Supply Chain Due Diligence Act, and, more recently the European Union's Corporate Sustainability Due Diligence Directive.

Sustainability integration in modern corporate practices

Many companies have implemented voluntary actions on sustainability, independent of legislative requirements. CEOs are broadening their roles, with 91 per cent acknowledging a duty to protect local communities and 70 per cent recognizing the need to address public concerns.²⁹ Companies' sustainability impacts can stem both from (i) their products, services and activities, and (ii) their operational practices. Initially, business' approach to sustainability was primarily centered around the latter, via the risk-oriented consideration of externalities. This vision gradually expanded with the realization of the importance of aligning core business activities with real value creation (see, for example, the recent discourse around the B Corporation or the "regenerative company" that not only avoid externalities, but also actively contribute to solutions). Businesses have embraced voluntary commitments, such as pledges and standards to standardize their approaches in line with peers, and to adopt a common language for communicating alignment to shareholders and stakeholders. Bottom-up initiatives have also emerged to help companies align with international agreements (see, for example, the Science Based Targets Initiative helping companies to align with the goals of the Paris Agreement), as well as to respond to increasing ESG demands from investors (see section 4.2).

Remaining barriers

Despite increasing commitments, SDG-aligned companies remain in the minority. In 2020, 62 per cent of MSCI SDG Alignment dataset companies (over 8,500 companies) displayed neutral alignment or misalignment across the SDGs for their products, services and activities.³⁰ Beyond business models, business practices also remain deficient from a sustainability perspective. Echoing the aforementioned challenges in the global labour market, gender equality has not yet been achieved in

corporate leadership. Despite the growing number of exchanges that promote gender equality, the number of women in high-level positions within companies remains low in many markets. Women were holding only 23 per cent of the board seats at the top-listed companies on 22 major G20 stock exchanges in 2022.³¹ Disclosure is another telling example of the misalignment of corporate practices with sustainable development. While 98 per cent of S&P 500 companies engaged in corporate sustainability disclosure in 2022 – up from only 20 per cent in 2011³² – the quality of data remains weak and greenwashing risks abound (see section 4.2).

Reversals and short-term-oriented decisions in moments of crisis reveal the limitations of voluntary and bottom-up approaches. A recent survey identified ESG as the primary investment focus for chief financial officers, but also indicated that this area is most likely to face near-term budget cuts.³³ While sustainability investments or programmes enable companies to mitigate long-term risks, crises tend to shorten time horizons and reveal an enduring misalignment between long-term non-financial considerations and prevailing incentives in markets, exacerbated by the mispricing of externalities. This is particularly evident in the current context characterized by high inflation, high interest rates and geopolitical divides. For example, the surge in oil prices following the COVID-19 pandemic led to renewed interest in brown investments along the fossil fuel value chain, underlining the need to change incentives and permanently alter the rules of the game through policies.

3.3 Strengthening the business environment

Changing business practices must be a core element of sustainable transformations, yet the private sector will not be able to systemically change behaviour unless profitability and sustainability are aligned. The rules of the game (i.e., the environment in which companies evolve) must change to enable sustainable practices. Policymakers have various tools at their disposal to align sustainability and profitability, including the pricing externalities (e.g. through carbon pricing mechanisms), the phasing out harmful subsidies, the prohibition of activities with negative impacts (such as single use plastics), or mandating certain corporate practices such as sustainability reporting (see section 4.2). Further options include the promotion of business models and opportunities with a positive impact on sustainable development, for example through subsidies, as well as public investments and other efforts through fiscal tools, regulations and laws to overcome coordination challenges that abound in economy-wide transformations (e.g. in the decarbonization of the transport sector).

Efforts to create an enabling environment for the private sector and the provision of relevant public goods should thus be aligned with sustainable development objectives. The rule of law, the absence of corruption and the quality of institutions are important determinants of private sector growth prospects. Investments in public infrastructure, education and health, stable and growth-oriented macro policies and exchange rates, and regulatory frameworks (including competition policies) all contribute to reducing uncertainty and risks for firms and thus to creating a better business environment and a lower cost of borrowing. But to achieve sustainable transformations, even these "horizontal" policies should be informed by broader sustainable development objectives. This includes: sequencing and prioritization of public investments, where governments are "doomed to choose", particularly in

an environment of tight fiscal constraints; setting the “right” incentives through fiscal and tax policies; ensuring that regulatory frameworks reflect appropriate labour, environmental and health standards; and aligning investment and trade facilitation policies with sustainability. For example, policymakers can use land-use procedures and building codes to ensure that infrastructure is not constructed in disaster-prone areas and meets appropriate design and construction standards.

Ensuring that gender equality is enshrined in law and implemented effectively is another key aspect. Currently, laws in 93 economies do not mandate equal pay between men and women for work of equal value. Women’s property rights are still restricted in 76 countries, and women cannot run a business the same way as men in 101 countries. As a result, women are less likely to become entrepreneurs, with 68 women entrepreneurs for every 100 men entrepreneurs active globally.³⁴

Easing financial constraints for firms, particularly for long-term investments, requires addressing multiple financial sector bottlenecks. The latest data for SDG indicator 9.3.2 (“Proportion of small-scale industries with a loan or line of credit”) show that nearly one third of small manufacturing firms have a loan or line of credit. Yet, access to credit remains uneven across countries and regions. For example, only 15.7 per cent of firms in sub-Saharan African countries and 17 per cent in LDCs have access to financial services, well below the global average and far from the rates in Latin America and the Caribbean, and Oceania (44.2 per cent and 45 per cent, respectively). For SMEs in manufacturing and services activities, policy-makers will have to develop and implement programmes to make formal lines of credit more accessible, increase financial literacy among entrepreneurs and introduce targeted lending in underserved areas. Constraints are most prevalent for long-term financing. Accessing financing on such terms can be a particular challenge, with lenders reluctant to provide long-term credit to borrowers about whom they have very limited information (e.g. SMEs) or for activities regarding which they are uncertain about future returns (e.g. investments in innovation; see section 4 of this chapter and box II.8 of the *Financing for Sustainable Development Report 2023*). Well-managed public development banks can play a role in filling such gaps (see chapter III.A).

A new generation of sustainable industrial policies

In response to the need for sustainable transformations, industrial policies have once again become more prevalent. Unlike policies aimed at improving the broader enabling environment for private business and investment, industrial policies and strategies are targeted in nature. They typically connect policy making with long-term visions and development priorities, help to overcome information and coordination problems, and can reduce the uncertainty that necessarily accompanies investments in new sectors, activities and technologies. Industrial policies³⁵ have been resurgent since the 2008 world financial and economic crisis, with the revival driven by several factors: the decline of decent jobs tied to the decline in manufacturing sectors in some countries; vulnerabilities in supply chains revealed by the COVID-19 pandemic and inflation driven by other supply shocks; rising geopolitical tensions that have created an additional geostrategic impetus to “avoiding external dependencies”, particularly in sectors that are deemed strategically important such as semiconductors, other high-tech sectors and energy; and finally the need to accelerate the development and deployment of low-carbon technologies and the

energy transition, which has led many countries to adopt “green industrial policies”.³⁶ Industrial policy measures more than doubled between 2009 and 2019, with the revival particularly pronounced in developed countries: four out of the five countries with the largest number of industrial policies are developed countries.³⁷

This new generation of industrial policies has to respond to a changing and challenging global environment. Developing countries must harness new opportunities in the context of stagnating trade and investment growth and a slow-down in GVCs, the geographic concentration of manufacturing activities in a few large countries and rapid technological change and digitalization – and doing so under global rules that have made industrial transformation more challenging in recent decades. The objective of such sustainable and inclusive industrial policies is also broader, and more ambitious. It is not just to spur sustained economic growth and build capabilities in the domestic private sector to innovate and enhance productivity, but also to “shape” growth, ensuring that it creates decent jobs and provides opportunities for all, is environmentally sustainable, and is aligned with the SDGs more broadly. Chapter II of the *Financing for Sustainable Development Report 2023* laid out a set of recommendations for such a strategic approach.

4. Aligning finance with sustainable development

A more dynamic, inclusive and sustainable business sector depends also on the emergence of a financial sector that is both inclusive and sustainable. Lack of access to finance, the excessive costs of finance and other financial constraints are often among the most binding constraints for private sector development. Access to financial services also remains a concern for households and individuals, particularly in LDCs, despite the significant progress achieved in this area. There has also been an enormous increase in interest in “sustainable finance” – the alignment of the financial sector with sustainability.

4.1 Inclusive finance

Over the past two decades, significant progress has been made in financial inclusion for businesses and individuals alike, driven in particular by innovations in digital finance and financial technology (fin-tech). Yet, despite the progress, significant challenges remain, particularly with regards to access to long-term finance, highlighting the sustained need for financial sector development. Moreover, gender, age and geographical location continue to be critical factors in determining access to financial resources. At the same time, the financing gap between MSMEs and large companies is widening, as MSMEs face greater difficulties in navigating the post-COVID-19 economic landscape and adapting to the shift from a low to a high interest rate environment. MSMEs from developing countries and those in the informal economy lack the capacity to navigate and hedge against various forms of risks, including exchange rate risks. These challenges need to be urgently addressed to ensure that both MSMEs and individuals have access to affordable, quality financial services. Financing costs have increased globally following a tightening of monetary policy. Inflationary pressures have also risen, increasing living expenses and impacting firms with lower elasticity in product pricing.

Access to finance for firms

Developing domestic financial sectors that are aligned with the SDGs and provide long-term financing for sustainable development in developing countries continues to be a key challenge.

Well-developed local financial markets can facilitate risk-sharing and improve the availability of long-term finance beyond a small number of large firms that can tap global financial markets. Despite efforts to promote long-term finance in domestic markets and an increase in bank lending to the private sector over the past 20 years, financial and capital markets remain underdeveloped in terms of size, liquidity and maturity in many developing countries, and long-term credit continues to be scarce, both for sovereigns and for corporates (figure III.B.11). To avoid maturity mismatches, banks require longer-term funding options in order to provide long-term lending. Studies have shown that despite improvements in financial depth, characterized by higher lending from banks to the private sector, developing countries have generally seen smaller increases in long-term finance.³⁸ The recent tightening of global financial conditions has also made long-term finance scarcer in both developed and developing countries.

Domestic efforts to extend maturity structures towards longer-term finance have been hampered by a number of factors, including market inefficiencies, an absence of local currency financing and institutional gaps, as well as macroeconomic volatility. Despite progress in promoting domestic capital markets, these markets have stagnated in many developing countries, not (yet) reaching sufficient scale to provide sufficient amounts of long-term and local currency-denominated finance.³⁹ Policies that can support the development of capital markets include strengthening institutional and legal frameworks as well as fostering financial infrastructure. At the same time, building local capital markets is an inherently gradual process that depends on the local needs and context, including the country's size.⁴⁰

Long-term credit in developing countries also continues to be highly skewed towards a small number of very large firms. Faced

with significant hurdles to access long-term finance, smaller firms are reliant on short-term loans and exposed to rollover risks that may preclude them from investing in long-term projects. Unlocking greater long-term investment in the SDGs will require financial sector development through policies that promote macroeconomic stability, strengthen regulation and supervision of banking systems as well as facilitate the long-term development of capital markets and institutional investors. In this regard, national development banks can play an important role given their ability to extend longer-term financing due to their policy mandates and funding structures (see chapter III.A).

Access to finance continues to be a critical challenge for SMEs in particular. In response to tightening financial conditions and the unwinding of COVID-19 support measures, the outstanding value of commercial bank loans extended to SMEs relative to GDP has declined. Seventy-five per cent of economies saw a drop in lending to SMEs in 2022.⁴¹ Data suggests that COVID-19 relief was directed to entities within the digital ecosystem, which left those not registered as businesses unable to access relief funds. In addition, there continues to be a gender gap in access to SME financing with women-owned businesses facing a disproportionate gap in funding. Informality continues to be a key factor determining access to finance and vice versa. Given this interplay between informality and access to finance, policy action is needed that recognizes that formalization and financial access need to be advanced in tandem.

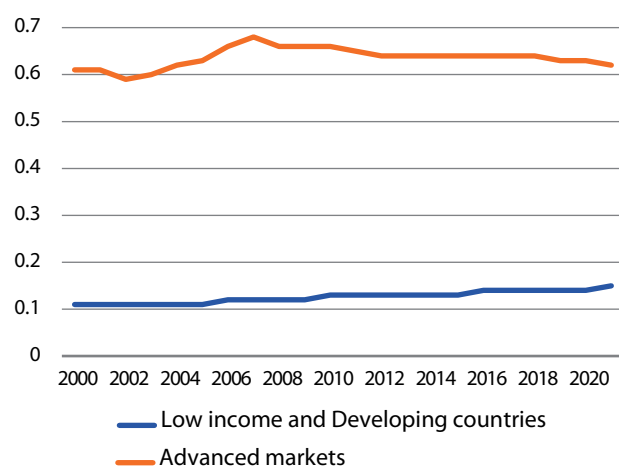
Access to finance for individuals and remittances

Enhancing access to finance for all individuals, including women, has been a Financing for Development priority from the outset. It featured prominently in the Monterrey Consensus and subsequent Financing for Development outcomes, recognizing the contributions that greater financial inclusion can make to business development, social protection, enhancing household and business resilience and lowering the costs of remittances, among other issues. These commitments have translated into progress on the ground. In the past 10 years, account ownership has increased worldwide from 51 per cent in 2011 to 76 per cent in 2021. In developing countries, account ownership grew by 30 percentage points over this period, reaching 71 per cent in 2021; 567 million adults gained access between 2017 and 2021 alone.⁴²

Despite the progress, significant gaps remain in access to and the affordability of financial services, not least for women. The global gender gap in account ownership has narrowed over the past decade, from 8 to 4 percentage points, but it remains significant: in 2021, 78 per cent of men and 74 per cent of women had access to financial services.⁴³ In developing countries, the gap is slightly broader still (figure III.B.12). Women continue to face multiple barriers, such as cost and affordability of financial services and financial literacy. Studies⁴⁴ have also highlighted the issue of women's indebtedness, suggesting that a larger proportion of women than men may use credit to pay for health and education expenses, underlining the need to consider how policy actions, including reductions in spending on public services, affect women's spending needs. There also needs to be greater efforts to advance asset ownership incentives for women to enable them to pledge collateral to access financing.

Overall, 1.4 billion adults remain unbanked globally. With account ownership nearly universal in developed countries, virtually all unbanked adults live in the developing world, with the largest gaps in LDCs, where

Figure III.B.11
Financial Development Index, 2000–2021



Source: UN DESA calculations based on IMF data.
Note: This chart uses IMF country classifications.

more than half of all adults remain unbanked. Vulnerable adults, such as the poorest, women, the unemployed and the elderly continue to be those most likely to be unbanked.

Migrant remittances and diaspora investment are important sources of income for households and SMEs. Remittances directly augment incomes of poorer households and tend to be counter-cyclical. They are expected to continue to increase due to rising migration pressures. Remittances to low- and middle-income countries are expected to have reached \$669 billion in 2023.⁴⁵ However, remittances continue to be more expensive than the commitments made in the Addis Ababa and 2030 Agendas, which set a 3 per cent target for 2030. The global average cost of sending \$200 fell slightly, from 7.7 per cent in the second quarter of 2015 to 6.2 per cent in the second quarter of 2023, but it continues to be more than twice as high as the SDG target.⁴⁶

Technological innovations have been a major driver for advancing financial inclusion.⁴⁷ Mobile money has facilitated a vast expansion of low-cost and small-scale transactions.⁴⁸ Between 2021 and 2022 alone, the number of mobile money transactions per 1,000 adults increased by 28 per cent and 24 per cent in Africa and the Asia-Pacific regions, respectively. Similarly, the value of mobile money transactions increased from 26 per cent to 35 per cent of GDP in Africa.⁴⁹ Of the 76 per cent of people worldwide who have an account at a financial institution, 36 per cent used a mobile phone or the Internet to access their account.⁵⁰ This has been driven by the adoption of digital technologies for carrying out financial transactions, such as mobile money, fast payment systems, digital identity, data-sharing arrangements and, more generally, digital public infrastructures (DPIs). Digital financial inclusion, and secure and responsible digitally enabled financial services and products could also be a key means to reach the remaining unbanked, financially excluded and underserved populations with a range of formal financial services suited to their needs. This will require greater use of national digital IDs to make it easy to open accounts. Identification is almost always a requirement for opening an account and owning a mobile phone. Digitally enabled financial services

could reduce transaction costs and foster innovative models for small business. Responsible finance lending principles should also be promoted along with greater financial consumer protection as digital lending takes off in many markets.

4.2 Redirecting investments towards the SDGs

Sustainable finance has risen to prominence over the past three decades on the back of growing investor interest. The modern approach to sustainable finance can be traced back to the 1990s, with a steady increase in investor interest since then. Over this period the field was codified at a blistering pace within a short time frame, by industry players who were grappling with new investment practices. However, the resulting high number of bottom-up standards and frameworks also led to confusion, hampering investor confidence over time. Growing political polarization has recently led to a backlash in some countries, with early signs already indicating a slowdown of investors' use of the term ESG in 2023. On the other hand, the increasing spotlight and mainstream attention on the field also underscore its rise to prominence.

While many challenges remain, the field has recently entered a maturation phase, with sustainable finance at a crossroads.

Following a rapid development phase and rise to prominence, the current moment presents an opportunity for refinement, recognizing that systemic transitions are lengthy and non-linear (see, for example, the gradual century-long development of other fields like financial accounting). There needs to be an honest reassessment of the field's real-world impact to help identify where complementary policy is necessary to achieve broader systemic change. Early maturation signals have included the clarification and consolidation of voluntary standards and regulatory and legislative action to further enhance impact (see section 4.2.4).

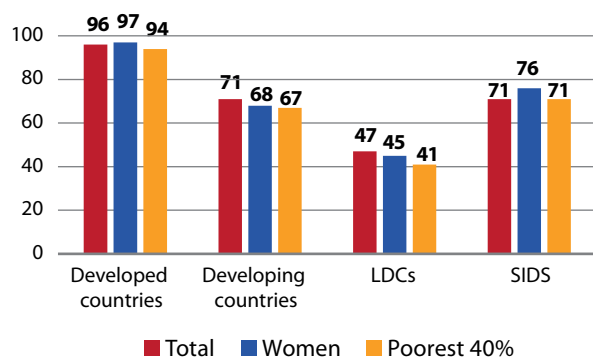
4.2.1 Rising interest and deepening focus

Sustainable investing was a niche practice until a transformative shift in the late 1990s and a notable acceleration after 2015.

Ethical funds emerged in the 1920s as an early form of socially responsible investing, restricting investments in industries that investors considered unethical, such as tobacco and firearms. Despite their early origin, these funds had limited influence. With global conferences such as the Earth Summit in 1992, sustainable development became a more prominent concern for all stakeholders, including private actors. The 2015 global agreements – the Addis Ababa Action Agenda, the 2030 Agenda for Sustainable Development, and the Paris Agreement on Climate Change – accelerated the expansion of sustainable finance (figure III.B.13). These agreements shed light on increasing systemic risks for investors and brought to the fore the interlinkages between social, environmental, economic and financial factors.

ESG factors are routinely considered by investors today. Over time, asset owners have increasingly recognized the material risks that their portfolio companies might pose, and the growing investment opportunities in sustainable sectors. This has driven a shift in portfolio reallocation and an acceleration of sustainable investment, as well as the growing integration of non-financial issues in investment decisions.⁵¹ Investors no longer consider these factors as purely philanthropic issues but view them as an integral part of risk management, and a growing number of actors also realize their value creation and impact potential. Additionally,

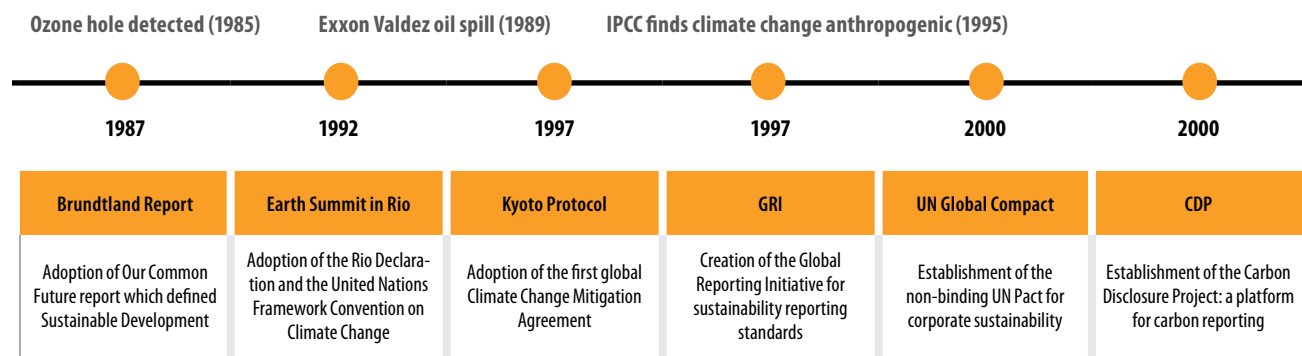
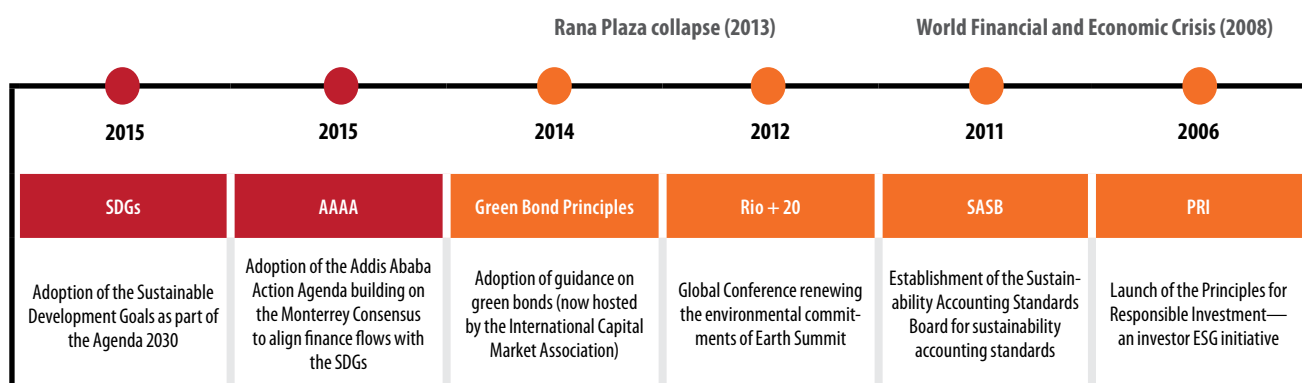
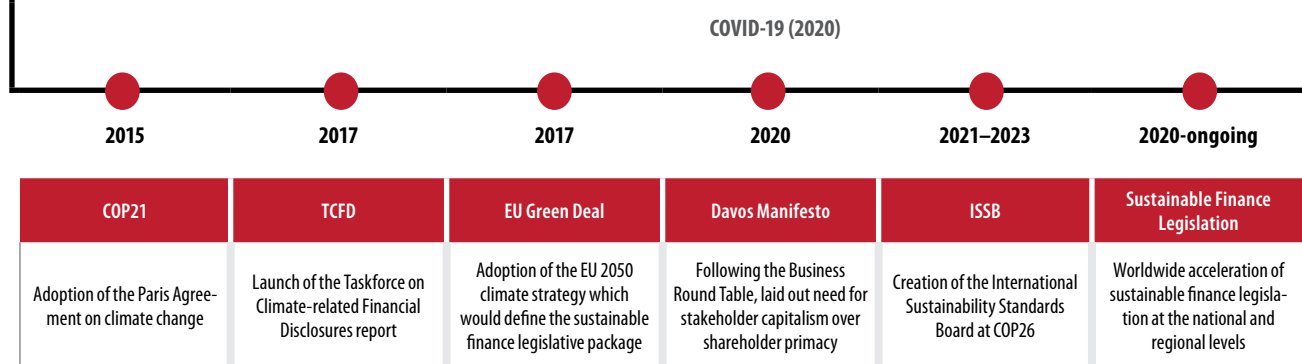
Figure III.B.12
Adults (age 15+) with a bank account by country grouping, 2021
(Percentage rates)



Source: UN DESA calculations based on the Global Findex Database 2021.

Note: LDCs comprises 38 countries from the UN DESA list of 45 Least Developed Countries. SIDS only includes data for Dominican Republic, Jamaica, Mauritius and Singapore, which are a subset of the list of SIDS produced by UN DESA.

Figure III.B.13

The evolution of sustainable finance: An historical timeline of select milestones*Igniting change: International societal sensitization (1990s–2000)**Empowering transformation: Industry-driven progress (2001–2014)**Accelerating impact: Towards regulatory frameworks (2015–Present)*

Source: UN DESA.

Note: This is a non-exhaustive list of key events.

asset owners have become more active owners or “stewards” of their investments and increasingly seek engagement with investee companies on sustainability issues.⁵² Today, around 85 per cent of chief investment officers consider ESG an important factor in their investment decisions.⁵³

The interpretation of fiduciary duty has evolved over time but remains contested. Fiduciary duties ensure that asset owners (including institutional investors, insurers and banks), also known as fiduciaries, who exercise discretionary power in managing the assets of their beneficiaries, act responsibly in the interest of these shareholders. Over time, the interpretation of these duties has widened to include the consideration of ESG issues. Under current practice, asset managers largely consider ESG risks within an overall process of commercial risk management, as studies have shown that responsible investment allows them to maximize long-term returns for their clients. A series of landmark reports, including the 2005 Freshfields Report⁵⁴ and its sequel, *Fiduciary Duty in the 21st Century*,⁵⁵ indeed concluded that investment approaches which consider ESG factors are permissible and arguably required for long-term investments. The rationale is that sustainability considerations will impact financial performance in the long-term, and neglecting ESG analysis may cause the mispricing of risks (whether legal, reputational, operational or systemic), leading to poor asset allocation and stranded assets.⁵⁶ More ambitious interpretations of fiduciary duty also encourage fiduciaries to pursue sustainability goals that may reflect beneficiaries’ preferences, regardless of whether these preferences are financially material. Financial return remains the primary goal of institutional investors today, but further analysis shows that in some jurisdictions investors are already facing a legal obligation to consider setting and pursuing real-world sustainability impact goals where doing so can be effective in achieving their financial goals.⁵⁷ However, amid the current ESG backlash, critics have recently reopened the debate on fiduciary duty, opposing the evolution of the concept and advocating for a return to its traditional interpretation (see section 4.2.3).

4.2.2 Sustainable investing trends

Sustainable investing assets have grown significantly since 2016, albeit with some year-on-year declines following the COVID-19 pandemic. Global sustainable investing assets – defined here to include all strategies of ESG integration, screening and impact investing – reached \$30.3 trillion in 2022, representing a significant increase from 2016, but below the record highs of 2020 and 2021.⁵⁸ This recent decline was fuelled by high oil prices and the turbulent economic environment during the COVID-19 pandemic. Looking at the subset of sustainable products (sustainable funds, bonds and voluntary carbon markets) rather than the entire universe of strategy-based approaches, sustainable products reached \$5.8 trillion in 2022.⁵⁹

Sustainable investment funds experienced a surge in inflows until 2021; and continued to outpace the broader market in 2022 and 2023. Sustainable funds⁶⁰ reached \$2.56 trillion in assets under management at the end of 2023,⁶¹ representing roughly 10 per cent of all sustainable assets. Their inflows of net new deposits peaked at \$558 billion in 2021 during the pandemic period, and subsequently experienced a decline to \$158 billion in 2022 and \$72 billion in 2023.⁶² Inflows still remained positive and outpaced flows into traditional funds, which suffered net outflows. But in absolute numbers, sustainable fund assets have

remained a small share of total fund assets under management, representing less than 5 per cent of total global fund assets (i.e., \$2.56 trillion of \$55.16 trillion at the end of November 2023).⁶³

Sustainable funds are mostly domiciled in developed countries, which also dominate capital allocation. Europe hosts the majority of sustainable funds, capturing 81 per cent of the market; the United States is the second-largest contributor at 13 per cent while all other countries combined account for only 6 per cent of total market share.⁶⁴ In terms of allocation, taking impact capital as an example, in 2023 the highest portion went to the United States and Canada (29 per cent of impact assets under management), followed by Western, Northern and Southern Europe (23 per cent) and sub-Saharan Africa (10 per cent).⁶⁵

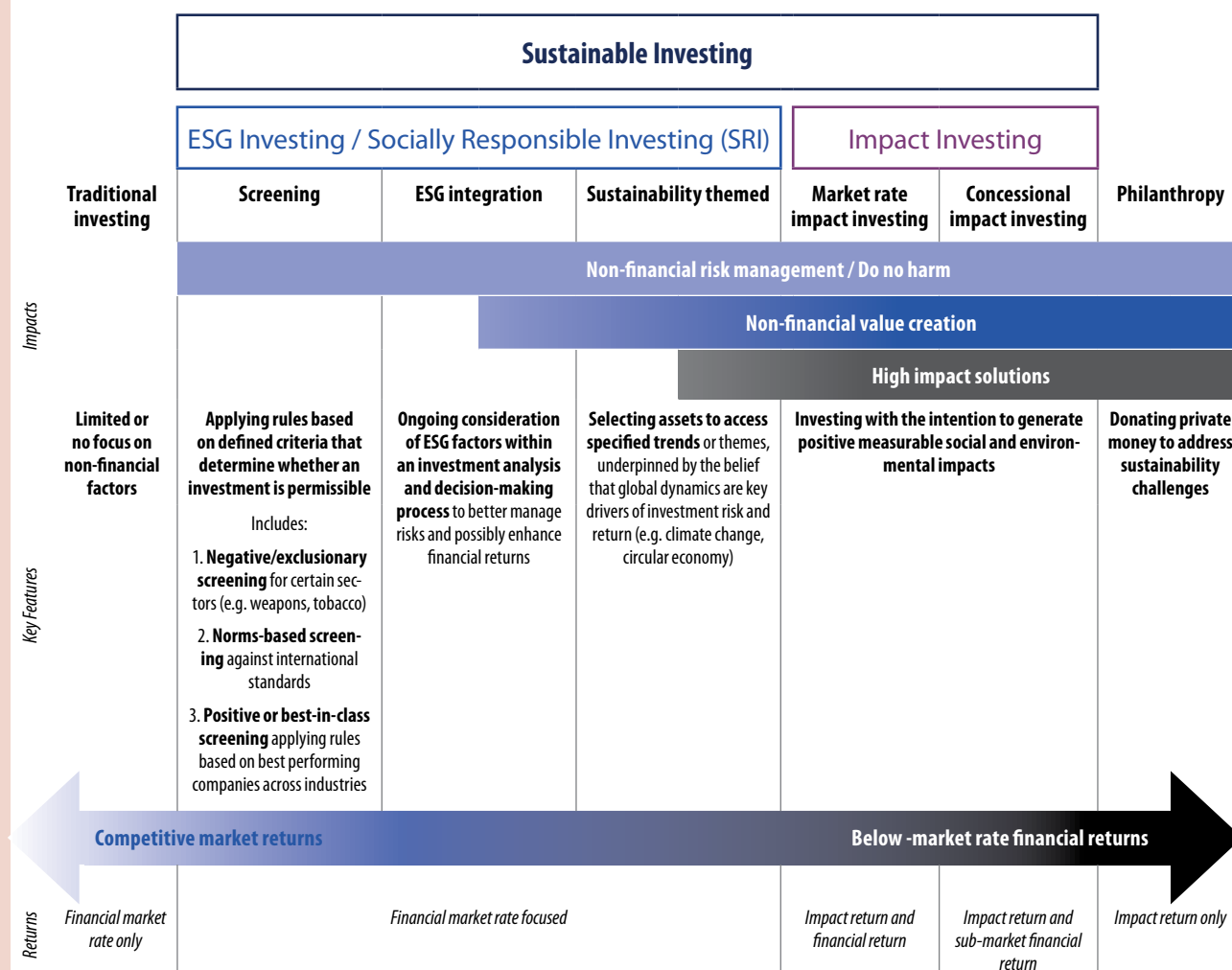
ESG integration and negative screening strategies dominate the field today, with impact investing representing only a modest fraction of total sustainable assets. Across a wide sustainable investing spectrum (box III.B.3), the majority of sustainable asset managers today prioritize “ESG integration”. This consists in integrating ESG factors into investment decisions to better manage risks and possibly enhance financial returns. The surging interest in ESG strategies is evident in the quadrupling of the number of asset managers and asset owners signing the Principles for Responsible Investment from 2015 to 2023 (although their minimum requirements do not reflect the actual level of ESG integration from signatories). Negative screening is the second most popular approach, while impact investing or thematic investing remains much smaller in scale (figure III.B.16). This may in part reflect these strategies’ short-term effects on financial performance. Impact or thematic investing, characterized by more structural biases and a focus on single industries (e.g. funds concentrated on the clean energy value chain), generally underperform other more flexible traditional or ESG strategies in the short-term. For instance, Article 9 products in the European Union (that is, for which sustainable investment is the primary objective as per the European Union Sustainable Finance Disclosure Regulation) have come under pressure in the current inflationary landscape, underperforming by -1.7 per cent in the first quarter of 2023.⁶⁶

Impact investing, although not yet dominant, holds significant growth potential and is gaining important momentum. Impact assets under management surpassed \$1.164 trillion in 2022,⁶⁷ and continued to grow across nearly every region in 2023.⁶⁸ Impact investing strategies are also evolving in terms of both depth and sophistication. This is exemplified, for example, in the rise of impact lenses, which complement impact strategies focused on sectors (e.g. renewable energy investments) by applying cross-cutting social themes to investments (e.g. applying a social lens to a renewable energy fund). These lenses have the potential to enhance investors’ positive impacts by integrating overlooked injustices that indirectly affect the outcome of all investments. Impact lenses include a gender lens,⁶⁹ a racial equity lens,⁷⁰ and a recently developed child lens.⁷¹

The impact investing market’s growth is fuelled, in part, by the rapid rise of green, social, sustainability, and sustainability-linked (GSSS) bonds. Investment figures on the labeled bonds that meet the Global Impact Investing Network’s (GIIN) definition of impact investing (e.g. certain types of green bonds and other use-of-proceed bonds) have been integrated in total impact market figures for 2022 (i.e. \$1.164 trillion).⁷² Taken separately, total labeled

Box III.B.3. Decoding sustainable finance

Figure III.B.14
Navigating a broad investment spectrum



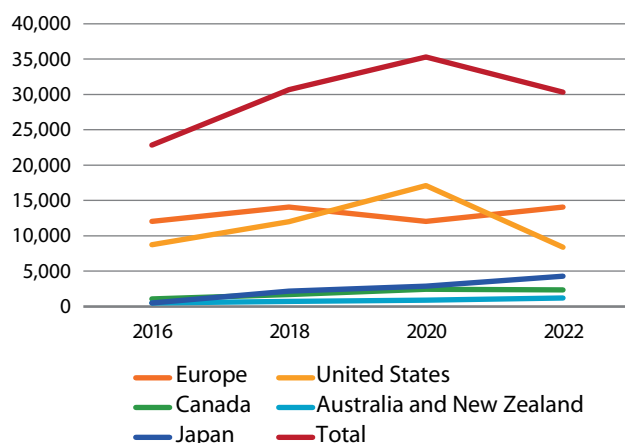
Source: UN DESA and Global Investors for Sustainable Development Alliance based on RIAA (Responsible Investment Association of Australasia), CFA Institute, Global Sustainable Investment Alliance, and Principles for Responsible Investment.

- A range of investment approaches are grouped under the term “sustainable investing”, with varying contributions to sustainable development (with ambition increasing from left to right in figure III.B.14). Definitions and denominations for sustainable investing strategies are not always used consistently; terms like “responsible investing”, “socially responsible investing”, and “sustainable investing” are frequently employed interchangeably, leading to confusion in the space. Moreover, despite being a subset of this space, the phrase ESG Investing is also commonly used as a proxy for sustainable investing as a whole. In a collaborative effort, the CFA Institute, the Global Sustainable Investment Alliance, and Principles for Responsible Investment released a detailed report to consolidate language and interpretations of the investment spectrum in November 2023^a (where applicable, these have been reflected in figure III.B.14).
- Beyond allocating capital to sustainable strategies, sustainable investors can engage in stewardship, using their rights and influence to guide businesses towards more sustainable business models and practices. Stewardship spans all asset classes, although the methods vary. Examples for equity investments include serving on or nominating directors to a company’s board and filing shareholder resolutions or statements, while for debt investments investors can attach ESG legal conditions to loans (as conditions precedent and/or subsequent). Such practices have started with multilateral investors (e.g., the International Finance Corporation) and eventually spread to the whole investment ecosystem. Asset owners and managers today regularly engage on a wide range of environmental, governance and social issues.

^a CFA Institute, Global Sustainable Investment Alliance, and Principles for Responsible Investment, “Definitions for Responsible Investment Approaches”.

Figure III.B.15

Global sustainable investing assets, 2016–2022 (Billions of United States dollars)



Source: Global Sustainable Investment Alliance (GSIA).

Note: A change in United States Sustainable Investment Forum methodology contributed to the material decrease of United States and total assets under management in 2022.

bond issuance reached \$946 billion in 2023, showing a small rebound (of 2.2 per cent) after a decline in 2022. As a whole, sustainable bond issuance grew five-fold over the past five years (see figure III.B.17). Labelled bonds span use-of-proceeds bonds (e.g. green, social, sustainability bonds), which are used to finance earmarked green or sustainable activities, and sustainability-linked bonds, which are general purpose bonds wherein issuers commit to improving overall firm performance against environmental or social key performance indicators. Representing only 6 per cent of all issuances, sustainability-linked bonds face challenges in scaling. While these instruments offer flexibility for business models unsuited to use-of-proceeds bonds, questions remain regarding the targets' rigour and ambition and their capacity to influence issuers' incentives. Despite also contending with some structural weaknesses (e.g. greenwashing concerns, lack of standardization and verification), the green bond model has given rise to a range of use-of-proceeds bonds, including but not limited to blue bonds, resilience bonds, transition bonds and orange bonds. As of today, green bonds remain the favoured instrument (60 per cent of total issuance), with a primary focus on climate mitigation. Sustainable Fitch predicts a continued rise in biodiversity and social use-of-proceeds instruments going forward.⁷³ Guidance is also gradually emerging to incentivize market uptake of these newer instruments, such as, for example, the Guidance on Sovereign SDG Bonds for Countries and Investors developed by the Global Investors for Sustainable Development (GISD) Alliance under the leadership of UN DESA and the United Nations Development Programme (UNDP), as well as the recent Climate Resilience Classification Framework for resilience bonds by the Climate Bonds Initiative.

Despite their potential, the global labelled bond market remains largely concentrated in high-income countries, much like other sustainable assets. Looking at the use-of-proceeds green, social and sustainability (GSS) bonds subset, for example, only 13 per cent of the overall GSS bond market was issued by entities in developing countries

in 2022 (further reducing to around 5 per cent when not including China). Bottlenecks to increasing GSS and sustainability-linked bond issuances in developing countries include illiquid domestic capital markets, lack of bankable and relevant projects, limited familiarity with international investors, complex public budgeting processes, and the high level and often voluntary nature of applicable global standards.^{74,75}

4.2.3 Persisting challenges

The sustainable finance field still grapples with challenges that limit both its scale and impact. These include:

- A weak information infrastructure leading to data gaps and greenwashing risks. High-quality, exhaustive and comparable data are prerequisites for informed investment decisions. Despite recent progress, a weak information infrastructure reduces market transparency and increases risks of greenwashing;
- A lack of global standardization in terminology, standards, and frameworks. A lack of consensus on terminology as well as the coexistence of various standards and investment approaches, lead to complexity and confusion in the field, although harmonization efforts are ongoing;
- Flawed ESG ratings. ESG ratings are failing to restore investor confidence, compounding existing challenges;
- Political polarization. An "ESG backlash" has introduced new reputational and regulatory risks for investors;
- Systemic barriers within the wider financial system. The persistence of traditional forms of investment alongside the increasing adoption of sustainable investing, and the limited share of more ambitious impact investing strategies, highlight broader systemic obstacles.

Weak information infrastructure

Data gaps and inconsistencies limit the ability of investors to make informed decisions. Data is one of the prerequisites to assess and price risks and opportunities. The number of companies and General Partners (GPs) reporting on sustainability data has increased over time, namely due to Limited Partners' (LPs) increasing demands. However, while 98 per cent of S&P 500 companies engaged in sustainability disclosure in 2022,⁷⁶ available data is still inconsistent and difficult to compare, pointing to remaining quality and relevance issues. Non-listed entities, as well as companies in developing markets, present even greater data availability and quality challenges due to fewer reporting requirements from investors and regulators. Standard-setters, international organizations and industry players have started making progress towards improving the global sustainability data landscape (see section 4.2.4).

A fragmented data landscape increases greenwashing risks, further jeopardizing the accurate identification of sustainable investments. Greenwashing refers to misrepresenting the sustainability profile of an entity or product through omissions, unsubstantiated claims, inconsistency, or exaggeration.^{77,78} It can be carried out by both investors and investee companies, and has become an important concern for all market participants, undermining their confidence in the sustainable investment industry.⁷⁹ Authorities are starting to adjust regulatory and supervisory mandates in response to data and greenwashing challenges (see section 4.2.4).

Figure III.B.16

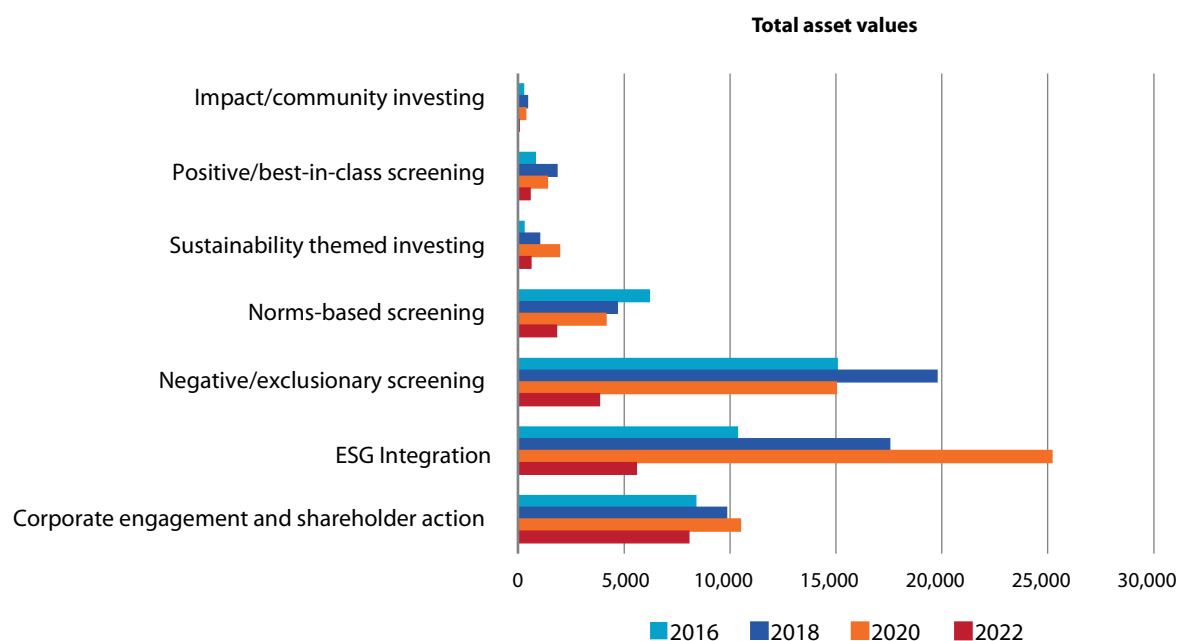
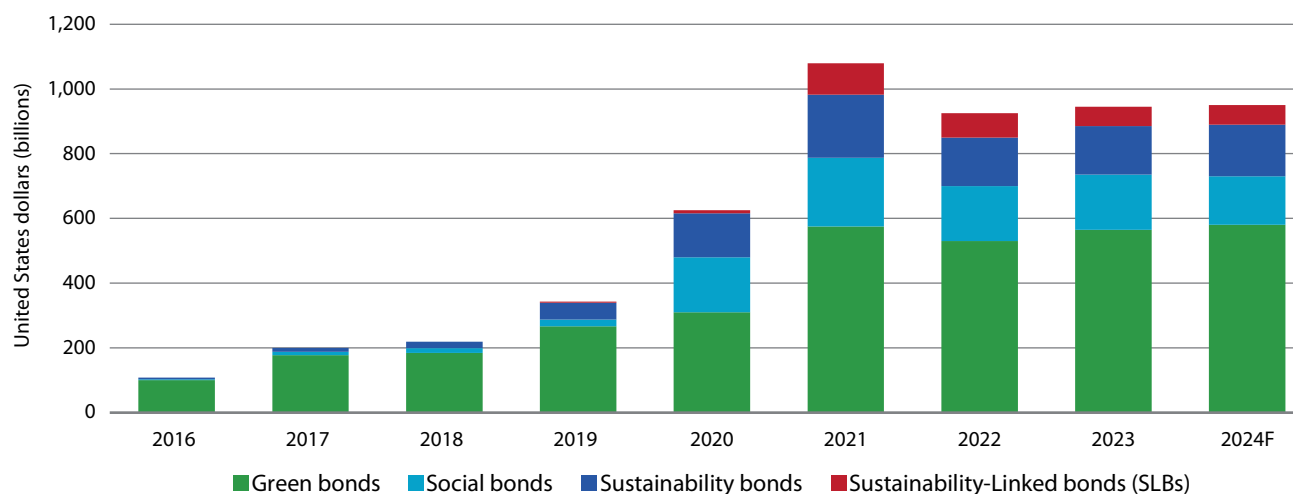
Sustainable investing assets by strategy, 2016–2022*(Billions of United States dollars)***Source:** Global Sustainable Investment Alliance (GSIA).**Note:** The sum of assets across each strategy does not equal the total assets. A change in methodology during 2022 makes comparison across report periods challenging. European data for the use of each strategy was not available in 2022.

Figure III.B.17

Annual global sustainable bond issuance (GSSS) by label, 2016–2024*(Billions of United States dollars)***Source:** Moody's Investors Service, Environmental Finance Data and Dealogic.**Note:** 2024F represents the full-year sustainable bond issuance forecast.

Lack of standardization

The rapid evolution of sustainable finance has given rise to a multifaceted system of norms and standards. The field predominantly evolved from the bottom-up, with market practitioners shaping industry rules based on international organizations' foundational principles. An array of principles, standards, frameworks and ratings emerged (see figure III.B.18). While instrumental to the field's development phase, this multifaceted normative landscape has eventually also caused confusion within the field and contributed to a fragmented information infrastructure. Harmonization efforts are ongoing (see section 4.2.4).

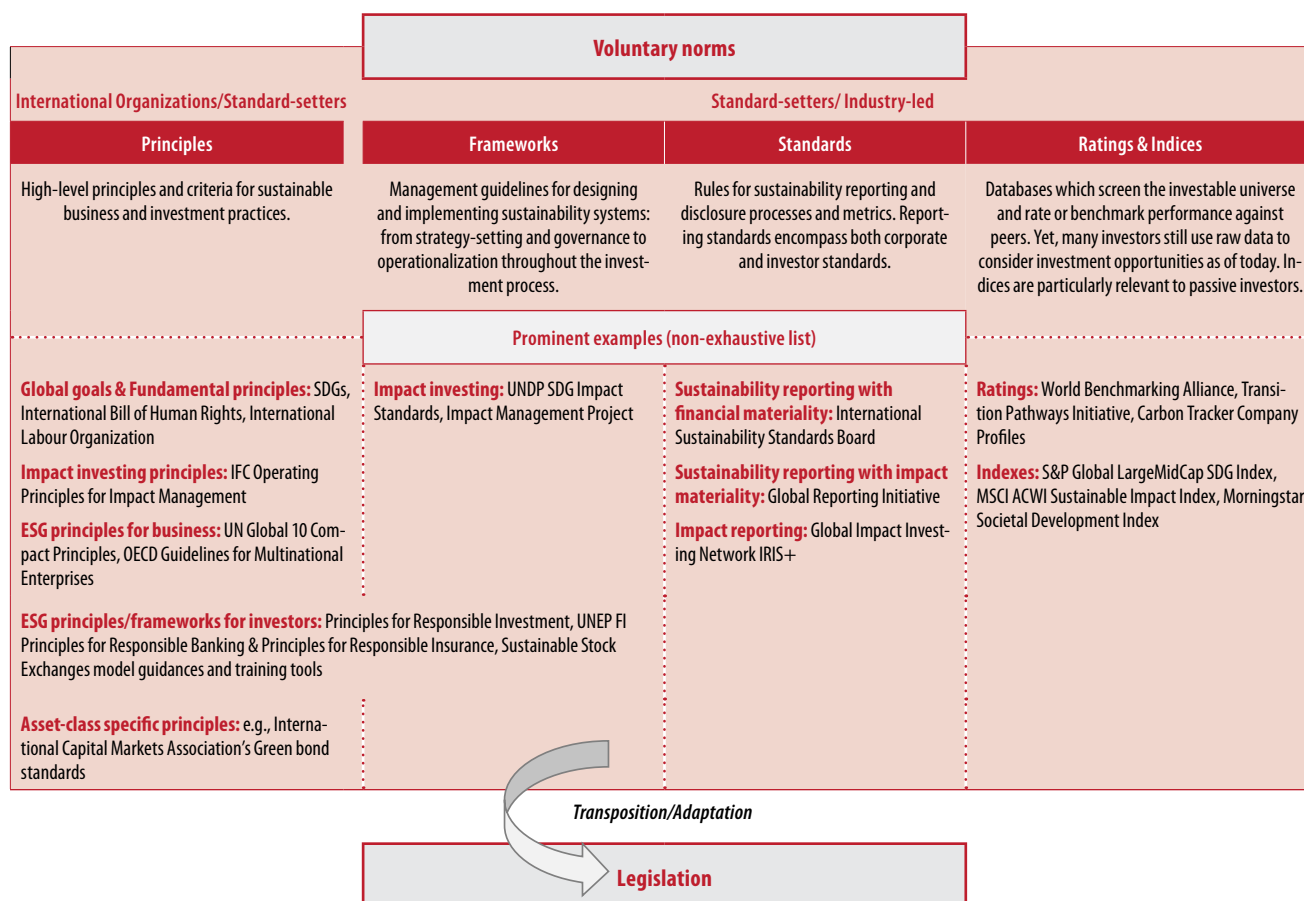
A connected challenge lies in the lack of clearly defined terminologies, including with the debated "ESG" concept. Various investing approaches fall under the umbrella term of "sustainable investing" (see box III.B.3), leading to the use, and often misuse, of different terms. Moreover, confusion arises within the sub-set of ESG investing itself. First, ESG is often equated with environmental topics only. Moreover, critics argue that the scope of issues under the ESG umbrella remains too broad, with a high and varying number of topics under each pillar (i.e., the environmental, social and governance pillars), resulting in a loss of clarity and strategic focus. The process of consolidating and refining definitions has started, including through investment taxonomies (see section 4.2.4).

Flawed ESG ratings

Thus far ESG ratings have not been able to bridge information gaps, nor to contribute to lengthening the time horizons of investment benchmarks. ESG and SDG indices, along with sustainability-inclusive credit ratings, have a role to play in supporting access to reliable sustainability conclusions, key to guiding investment decisions, particularly in the absence of audited sustainability reports. Additionally, sustainability-aligned benchmarks can contribute to lengthening investors' time horizons and performance incentives, by providing benchmarks with similar longer-term oriented strategies. However, these ratings face legitimacy issues, with ESG/SDG scores showing low correlation among providers at less than 60 per cent, compared to 99 per cent for financial ratings.⁸⁰ Moreover, there are methodological challenges and transparency gaps in the underlying information (e.g., relating to estimates) and aggregation criteria. This is particularly evident in SDG ratings, which may oversimplify companies' positive contributions by linking entire sectors to certain positive or negative impacts, neglecting the specifics of a company's activities within that sector. Concerns about potential conflicts of interest have also been brought forward, as a few major players dominate both the credit rating and sustainability ratings markets.⁸¹ There have been recent voluntary and regulatory efforts to

Figure III.B.18

A multifaceted system of sustainable finance norms



Source: UN DESA.

tackle these outstanding issues, including a Code of Conduct launched in December 2023⁸² and regulatory action in several countries, following the International Organization of Securities Commissions' (IOSCO) recommendations (see table III.B.2 in section 4.2.4).

Political polarization

The field has become increasingly politicized amid an ESG backlash. This is manifesting in scepticism, in some jurisdictions, regarding ESG integration, objections to evolving perceptions of fiduciary duty, and other more opportunistic factors and ideologies.⁸³ The increasing noise surrounding the field also underscores its rise to prominence into the mainstream discourse. According to a recent survey,⁸⁴ the financial services and insurance industries have been most targeted by the backlash, with some financial institutions facing legal action for upholding ESG criteria. This has caused a visible shift in discourse, although it is still too early to assess long-lasting effects on sustainability programmes. In 2023, 30 per cent of asset managers removed references to "ESG" or "net zero" from their marketing materials and websites in the United States.⁸⁵ Only 61 S&P 500 companies mentioned ESG in earning calls, a 60 per cent decline from 2021.⁸⁶

Systemic barriers

Systemic factors continue to favour traditional investment strategies and limit the scale of sustainable investing. Costs of capital continue to favour traditional investments, as they do not yet systematically reflect long-term sustainability risks. This is especially the case for investments with shorter holding periods. Since 2010, the borrowing costs for bonds for oil and gas firms in the United States and Europe have closely mirrored those for other debt issuers, with no premium.⁸⁷ Conversely, an analysis of euro-area credit registers indicates that banks applied higher interest rates to firms with higher carbon emissions during the period from 2018 to 2022.⁸⁸ This could be attributed at least in part to the longer loan terms for bank credits. Indeed, an analysis of the world's largest public institutional investors revealed that more than half these asset owners consider the material impacts of sustainability issues, such as climate change, a determining factor in their investment strategies and portfolio selection.⁸⁹ Extending investors' time horizons is thus imperative to align their objectives with long-term sustainable development trends. This is one of the focus areas of work of the Global Investors for Sustainable Development (GISD) Alliance, whose efforts will contribute to the preparations for the Fourth International Conference on Finance for Development.

4.2.4 Maturation

Sustainable finance is showing signs of maturation. Despite the varying pace of change across regions and industries, several consistent trends are emerging:

- a. **The streamlining and refinement of voluntary standards.** Standard-setters have started the consolidation and refinement of voluntary disclosure standards and management frameworks;
- b. **The adoption of national and regional legislation.** A burgeoning body of sustainable finance legislation is addressing issues related to the sustainable finance information infrastructure and broader investor duties.

However, persistent challenges remain in aligning finance with global sustainability goals, requiring collaborative efforts among countries and continued public-private cooperation. The upcoming Fourth International Conference on Financing for Development offers a timely platform for Member States to continue collaborating towards (i) widespread adoption and coordination of sustainable finance legislation to allow for interoperability and prevent fragmentation, while taking into account regional and local specificities; (ii) mandatory disclosure standards with a double materiality vision at national level; (iii) facilitation of impact investing at scale; and (iv) adoption of a more systemic whole-of-government approach that makes sustainable finance policy part of a broader set of economic and financial policies that align all financial flows to national and international sustainability goals.

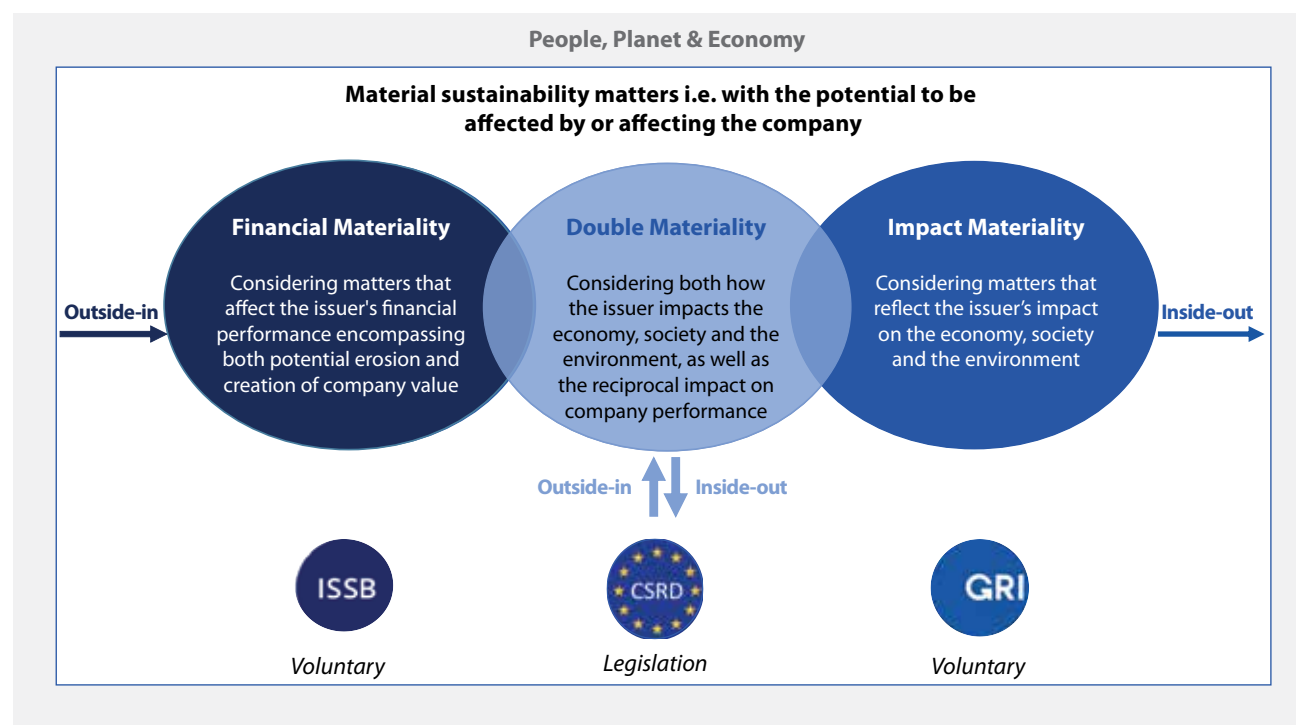
Consolidating and clarifying voluntary standards

An early signal of market maturation has been progress around the consolidation of disclosure standards for a stronger ESG data infrastructure. Leading these efforts are two primary standard-setters: the Global Reporting Initiative (GRI), established to foster more corporate accountability in 1997 (a few years after the public outcry post-Exxon Valdez oil spill), and the International Sustainability Standards Board (ISSB), founded in 2021 in response to investor-focused reporting needs identified at the United Nations Framework Convention on Climate Change Conference of the Parties (COP) 26. The ISSB has so far consolidated five major reporting standards, including: the Task Force on Climate-Related Financial Disclosures, the Climate Disclosure Standards Board, which included the Carbon Disclosure Project, as well as the Value Reporting Foundation which housed the Sustainability Accounting Standards Board and the International Integrated Reporting Framework. The ISSB's inaugural standards on sustainability-related financial disclosures (S1) and climate-related financial disclosures (S2) were published in June 2023 and endorsed by IOSCO thereafter.

Differing materiality visions should eventually converge into a double materiality approach, ensuring short-term interoperability. Operating under the umbrella of the International Financial Reporting Standards (IFRS) Foundation, which also houses the International Accounting Standards Board (IASB), ISSB supports financial (or single) materiality for investor decision-making. This approach adopts an "inward" vision, prioritizing sustainability issues that affect entities' cash flow and value. On the other hand, GRI focuses on impact materiality from an "outward" perspective, prioritizing matters that have an impact on the economy, society and the environment, thereby catering to a wider range of stakeholders (figure III.B.19). A third perspective, double materiality, integrates both perspectives, in a two-pillar structure with equal footing. This perspective was endorsed by EFRAG for its European Sustainability Reporting Standards in 2023, as well as by China's three major stock markets in early 2024.⁹⁰ Given the coexistence of single, impact, and double materiality approaches, interoperability is crucial in the short term, to facilitate international investors' reporting. ISSB and GRI have made significant progress through a Memorandum of Understanding, referencing GRI in ISSB standards and developing targeted interoperability guidance, including for greenhouse gas emissions reporting.⁹¹

Assurance standards are a key component of reporting standards, as mechanisms for auditing disclosures are essential to ensure

Figure III.B.19
Materiality visions



Source: UN DESA.

data reliability and comparability. IOSCO has begun work to coordinate and promote global consistency for sustainability assurance standards. In 2022, IOSCO started the process of assessing whether the existing sustainability assurance ecosystem is fit for purpose or whether further enhancements, including through standard setting, will be required. IOSCO has engaged key stakeholder groups, including the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants. The IAASB is currently developing a standard for assurance on sustainability reporting, with plans to publish it before the end of 2024.⁹² The assurance standard will allow to verify sustainability information prepared under different reporting standards, including those of the ISSB. As jurisdictions transpose voluntary standards to national legislation, they can also opt to tailor assurance requirements to their specific legislative provisions, such as was done by the European Union for its Corporate Sustainability Reporting Directive.

Diverse initiatives have also emerged to strengthen and deepen the field's data information architecture. Guidance from international organizations has emerged to help investors navigate the landscape of voluntary standards, including studies⁹³ and a wide range of databases (see, for example, the United Nations Global Sustainable Finance Observatory⁹⁴ and the Global Economic Monitor⁹⁵).

Beyond data, clarification is also underway for management frameworks, but persistent fragmentation highlights the need for consolidation. While reporting standards have been a focal point in sustainable finance discussions, they constitute just one element of investors' sustainability management toolkit. Management frameworks

provide wider comprehensive guidance for designing and implementing sustainability systems, encompassing aspects from strategy-setting and governance to operationalization throughout the investment process. They are necessary to ensure that disclosure is coupled with actual management of sustainability impact, as studies have shown that disclosure alone is not sufficient to influence lending.⁹⁶ In the impact space for example, management frameworks have been used to translate and operationalize the SDGs for private actors. As of today, the SDGs are used by 75 per cent of impact investors as a baseline framework.⁹⁷ However, this translation process has led to a proliferation of impact management frameworks and lack of harmonization. As a result, industry-led groups like the Impact Management Platform and the GISD Alliance have worked to enhance clarity with a System Map⁹⁸ and an SDG Navigator,⁹⁹ respectively, which summarize and categorize available resources. Despite strides in transparency, fragmentation endures, highlighting the need for consolidation akin to the approach taken with reporting standards. Early indications of consolidation have included, for example, the announcement by the GIIN that it would host the IFC Operating Principles for Impact Management from 2022.¹⁰⁰

Accelerating the adoption and harmonization of sustainable finance legislation

Sustainable finance is increasingly embedded in regulatory and legislative frameworks. Countries are strengthening the financial sector's role in advancing sustainable development. Several databases have emerged to record progress made.^{101,102} As of July 2023, the

Green Finance Measures Database registered over 780 sustainable finance policy measures in 109 countries, a 70 per cent increase since 2015.¹⁰³ Taxonomies and disclosure legislation have been at the heart of legislative efforts, with at least 30 taxonomies and 200 frameworks, standards and guidelines on sustainability and climate disclosures in place across 40 countries. By setting out clear and transparent criteria for sustainable economic activities, sustainable finance regulatory frameworks can enable the development of a reliable and credible market for allocating capital to the sustainability transition. Table III.B.2 provides examples of sustainable finance legislation along four main categories: alignment definitions (e.g. taxonomies), data availability and reliability (e.g. disclosure legislation, investment product labels, greenwashing), data comparability (e.g. regulating ESG ratings), as well as investor duties (e.g. stewardship-related legislation). Such sustainable finance policy tools are to be complemented by wider national strategies or frameworks mainstreaming sustainability considerations, as well as other sector-specific and product-specific measures.

The growing regionalization of sustainable finance legislation already reveals disparities and fragmentation across jurisdictions, highlighting the need for global interoperability. Sustainable finance legislation is being tailored to regional priorities, as seen by the different taxonomies adopted by the European Union, Latin America and

the Asia-Pacific region, each emphasizing different social or environmental aspects reflecting the regions' unique local contexts. While this regionalization is legitimate and important, without effective coordination it risks causing fragmentation and high compliance burdens for investors, which would reverse progress made on the consolidation of standards. In fact, this could potentially go as far as leading investors to underestimate the sustainability credentials of funds (IOSCO is already warning of emerging "green muting" and "green bleaching" practices).¹⁰⁴ This emphasizes the necessity for, at minimum, global collaboration towards interoperability, while simultaneously exploring a global foundational framework which would leave room for regional adaptation. For example, a global taxonomy could link all industry activities to a global framework such as the SDGs, helping regions to coordinate their own visions across regional taxonomies. There is already a growing focus on the harmonization and interoperability of regulations across jurisdictions to accelerate sustainable finance flows.

With uneven progress across regions, promoting universal coverage requires addressing several challenges. As of now, the majority of sustainable finance legislation is being adopted in developed economies (62 per cent of 109 countries).¹⁰⁵ Successful implementation of sustainable finance legislation requires bolstering institutional means, legal frameworks and capital markets through enhanced capacity building support and technical guidance. The United Nations Global Sustainable

Table III.B.2
Sustainable finance legislation—Key policy categories & prominent examples

Legislation	Description	Prominent examples
Category 1: Alignment		
Taxonomies	Classification systems for sustainable economic activities, defining alignment criteria based on shared sustainability goals	<i>Green taxonomies</i> - European Union Green Taxonomy - Colombia Green Taxonomy <i>Social taxonomies</i> - Georgia Sustainable Finance Taxonomy <i>Transition taxonomies (with traffic light system)</i> - Singapore Green & Transition Taxonomy <i>SDG taxonomies</i> - China Technical Report on SDG Finance Taxonomy
Category 2: Data availability		
Disclosure legislation	Corporate and investor sustainability disclosure requirements, including mandatory assurance provisions	- Countries accounting for nearly half of the world's GDP have either passed or proposed sustainability-related disclosure legislation, with many jurisdictions contemplating ISSB adoption - A prominent example is the European Union Corporate Sustainability Reporting Directive (CSRD) and its European Sustainability Reporting Standards (ESRS)
Category 3: Data & Product Reliability and Comparability		
Greenwashing and conduct-related	Financial and consumer product classifications (e.g. regulating fund classification systems, regulating eco-labels)	- United Kingdom Financial Conduct Authority (FCA) Sustainability Disclosure Requirements (SDR) - Switzerland's Federal Department of Finance (FDF) sustainable investment labelling rules - European Union Sustainable Finance Disclosure Regulation (SFDR) and European Union Proposed Directive on Green claims (consumer products)
ESG rating legislation	Regulating ESG service providers' methods and transparency	Regulatory action emerging in different countries including Japan, Hong Kong as well as the European Union
Category 4: Investor duties		
Stewardship-related legislation	Outlining good practice for investor engagement with companies and related issues, such as proxy voting	- United Kingdom Stewardship Code - European Union Shareholder Rights Directive II (2017/828/EU)

Source: UN DESA.

Finance Observatory informs capacity-building efforts on sustainability disclosure, taxonomies, carbon pricing, as well as sector and product specific measures. Stock exchanges can also play an important role in helping markets navigate new ESG requirements. The number of exchanges that have ESG disclosure guidance, mandatory ESG reporting, ESG training, and related bond and equity offerings has increased in the past few years. Moreover, support from development cooperation providers is needed to build capacity in developing countries to access sustainable finance, including the use of innovative instruments, such as insurance and investment based on results, which mitigate risk and attract external resources aligned with the SDGs without increasing debt distress. Strengthening the climate information architecture and aligning the practices and products of financial and information intermediaries can contribute to scaling up blended finance for climate mitigation and adaptation in developing countries (e.g., see the Network for Greening the Financial System's Technical Document on Scaling up Blended Finance for Climate Mitigation and Adaptation in Emerging Markets and Developing Economies¹⁰⁶).

Legislative efforts should incentivize impact across asset classes in line with Agenda 2030 and global climate goals, while being carefully crafted to avoid distortions. Only 14 per cent of impact investors have perceived progress in government support over the last decade.¹⁰⁷ A global taxonomy linking global industry activities to the SDGs could be the first step towards improving the identification of SDG-aligned investments, supported by policies financially incentivizing them. These include: (i) developing the supply of capital, such as through risk-sharing mechanisms, adjusted market costs and improved transaction efficiency or guarantees; and (ii) developing pipelines and the capacity of capital recipients. To address current funding gaps, a specific focus could be placed on channelling impact funds towards underfunded sectors, particularly those requiring private investment to complement public funds (e.g., climate adaptation and disaster risk reduction activities). Nevertheless, such incentives should be carefully crafted to avoid distortions and stability risks for the global financial system.

New disclosure legislation should aim to facilitate the measurement of the private sector's progress towards impact and climate goals by adopting an impact or double materiality perspective.

Countries accounting for nearly half of the global GDP are adopting disclosure legislation, with many having already pledged the transposition of ISSB standards. Jurisdictions already contemplating ISSB adoption can leverage current progress while integrating additional provisions for a double materiality vision. This should not be misconstrued as imposing additional burdens on investors, but rather as aligning with the objective of preventing fragmentation across jurisdictions and reducing investor confusion, which in turn decreases transaction costs and high compliance burdens (i.e. preventing global investors from having to prepare different sustainability reports to comply with varying financial and double materiality requirements across jurisdictions). Additionally, the double materiality approach mitigates medium to long-term transition risks for policymakers and investors. It will seamlessly align with transition-aligned legislation, which will progressively demand increased accountability from companies regarding their externalities and contributions to global climate goals.

Beyond policies focused on improving or widening the field, sustainable finance must become integrated into broader efforts to achieve sustainable transformations. Regulatory frameworks need to consider the roles of actors across the financial system, including pension funds, insurers, and banks, to align financial flows with national, regional or global sustainability objectives. Sustainable finance policy must be seen as part of a whole-of-government approach and a wider set of economic and financial policies that together create enabling conditions for sustainable transformations. Sustainable finance policy reform has already moved from a siloed approach led by environmental ministries to a key consideration for financial policymakers. This includes the consideration of the interplay between sustainability and financial stability (see also chapter III.F), for instance through climate transition plans (see, for example, the recommendations of the Network for Greening the Financial System on transition plans for banks¹⁰⁸ or the Glasgow Financial Alliance for Net Zero Financial Institution Net-Zero Transition Plans' report¹⁰⁹). It also includes broader fiscal and regulatory policies to create the "right" (sustainability-aligned) incentives for real economy actors, and financial sector and macroeconomic policies supportive of sustainable transformations which create investment opportunities for sustainable finance at scale.

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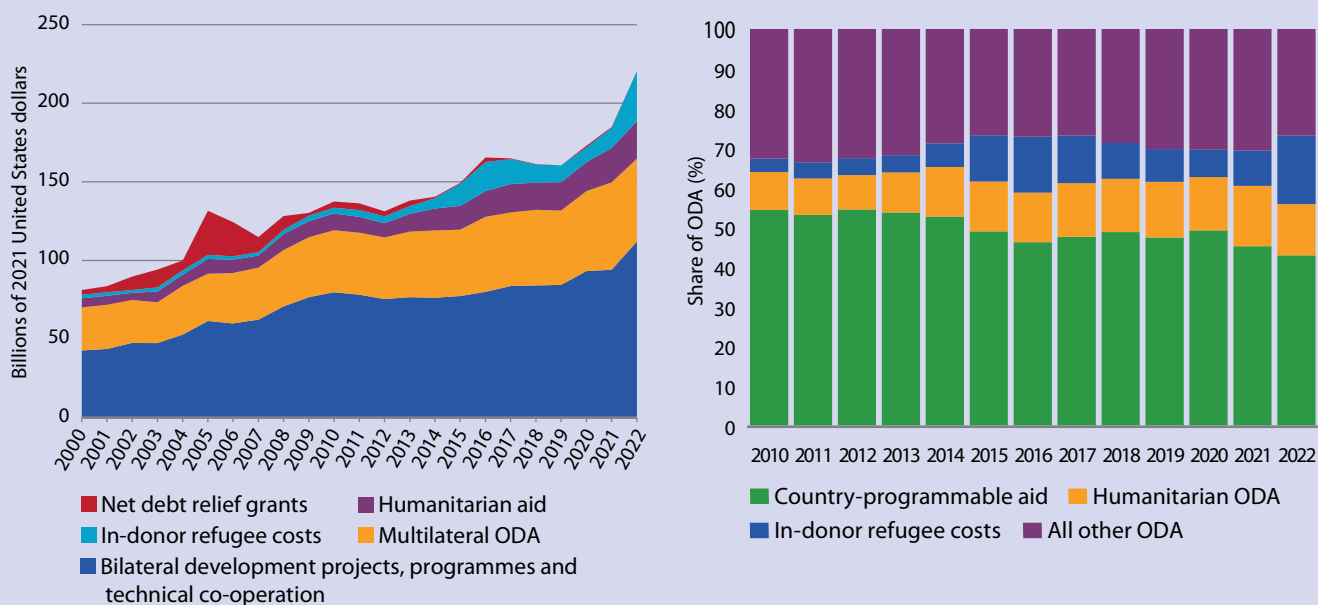
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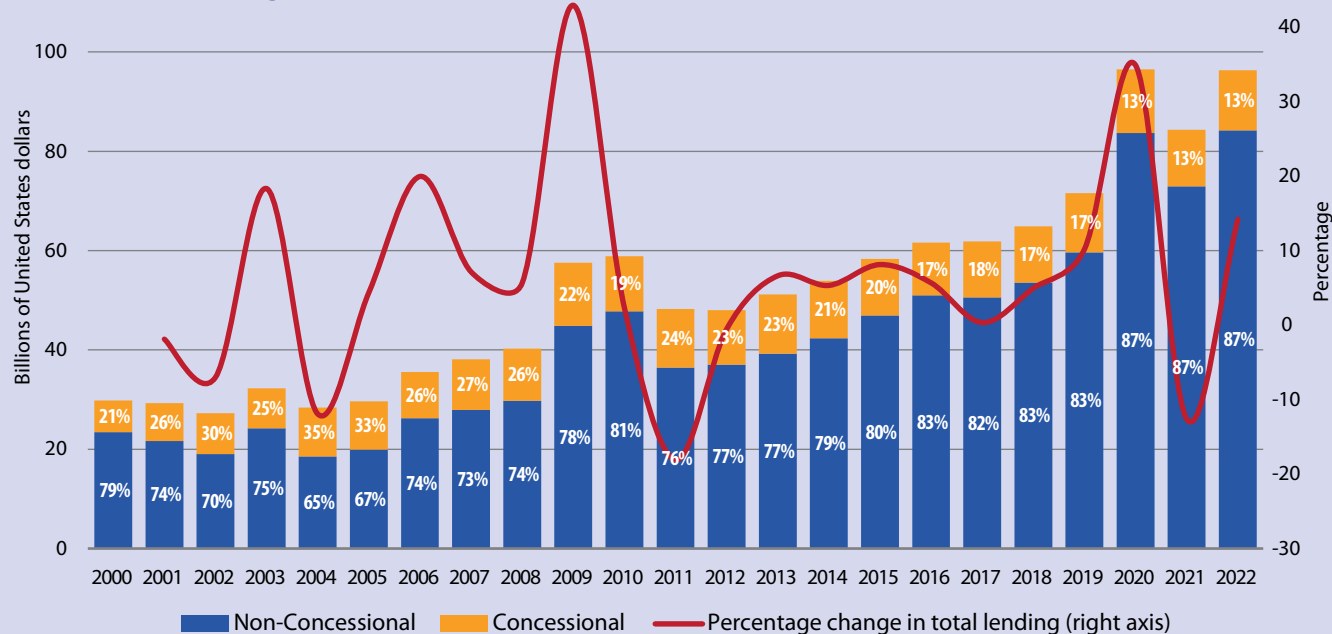


International development cooperation *in numbers*

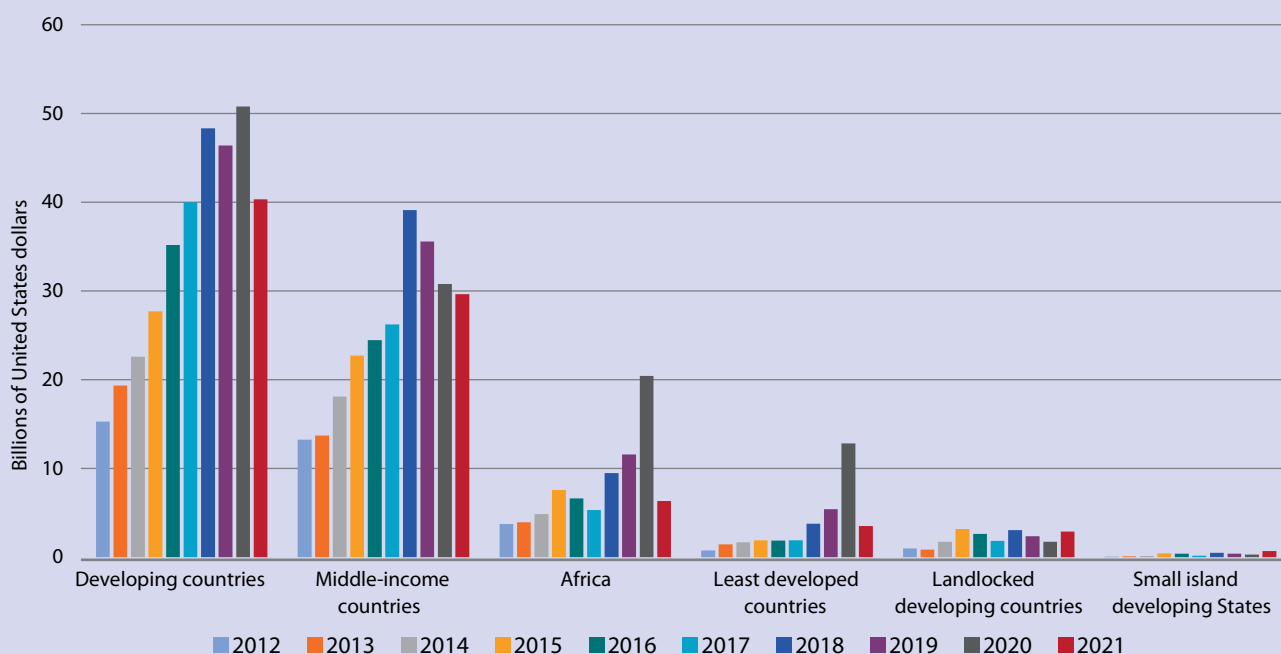
ODA has risen to record highs in recent years, but still falls short of commitments and is under pressure to respond to growing crisis response needs.



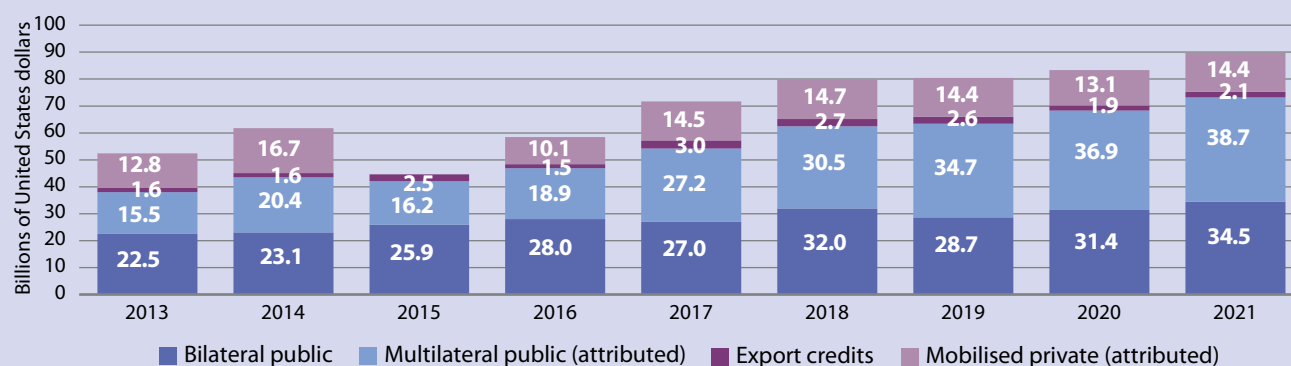
MDBs have significantly expanded their lending over the last 20 years; scaling up their resources is critical to meet heightened demands.



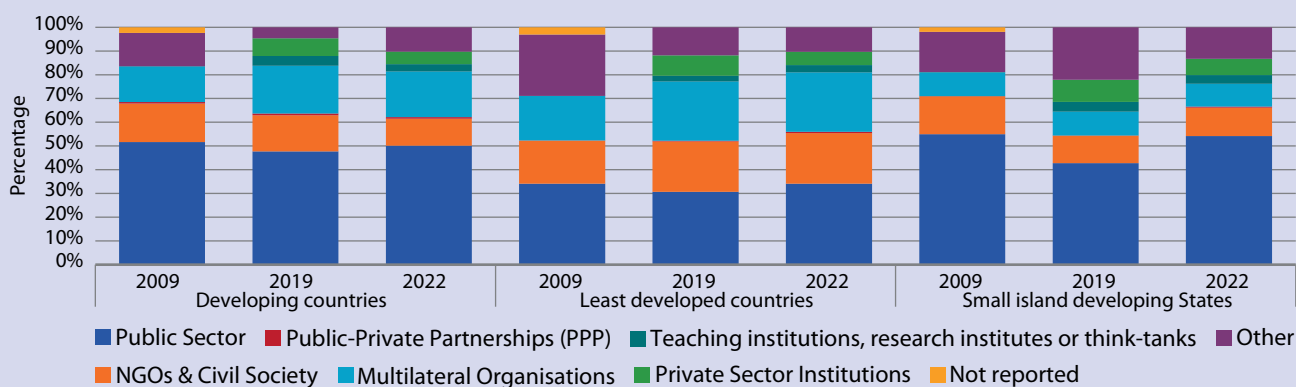
While blended finance has grown over the last decade, amounts mobilized remain far below expectations.



Mobilization of climate finance falls short of what is needed to effectively address the scale of climate challenges and remains grossly inadequate for the most vulnerable countries.



Global progress in improving quality, impact and effectiveness of development cooperation has been mixed, with less than half of ODA channelled through the public sector of recipient countries.





Chapter III.C



International development cooperation

1. Key messages and recommendations

International development cooperation has grown since the adoption of the Monterrey Consensus in 2002. At the same time, the demands on development cooperation have increased substantially, largely due to the ever-growing impacts of the climate crisis and an expanding and more ambitious global development agenda. Most recently, the COVID-19 pandemic, conflict and the cost-of-living crisis have placed unprecedented demands on international development cooperation. Urgent action is needed to boost all types of international development cooperation and to use them as effectively as possible, not least by fulfilling long-standing commitments on official development assistance (ODA) and climate finance.

ODA has reached new highs but still falls short of both needs and commitments and is under pressure to respond to growing demands. In 2022, ODA provided by members of the Organisation for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC) reached \$211 billion. ODA has more than doubled in real terms compared to the start of the new millennium. Yet, in a more crisis-prone world, there are concerns that growing expenditure on refugees and humanitarian aid as well as climate mitigation is cutting into support for long-term investments and other development priorities. This highlights the urgent need to increase the total ODA envelope to ensure that additional resources are available to address mounting challenges, and that these resources are targeted appropriately to countries most in need. Collectively, donors have also continued to fall short of ODA commitments, with a decreasing number of countries—four in 2022—meeting the United Nations target of providing 0.7 per cent of gross national income (GNI) as ODA.

Countries that are particularly vulnerable to the adverse effects of climate change and to debt vulnerabilities, such as least developed countries (LDCs)

and small Island developing States (SIDS) need more concessional resources and grants. To better take into account the vulnerabilities of such countries, measures of vulnerability could be considered to inform allocation decisions for concessional financing. At the same time, innovative financing instruments and mechanisms should be explored to raise additional resources for financing sustainable development. The Fourth International Conference on Financing for Development could build on recent and renewed interest in innovative financing to bring mechanisms to scale.

Multilateral development banks (MDBs) are in a unique position to accelerate investments in sustainable development. MDBs remain a critical source of affordable, long-term finance for developing countries as well as countercyclical support in times of crisis. At the same time, the paid-in capital bases of MDBs have not increased in line with the expansion of the global economy or growing investment needs. Recent global shocks have increased the urgency for MDBs and their shareholders to review their scale, roles and functions to adapt and respond to the challenges in achieving the SDGs. In response, the MDBs have begun to undertake a wide range of reforms to expand their financial capacity and enhance their development impact, including through addressing global public goods, aligning lending and operations with the SDGs and improving the measurement of development and climate impact. The upcoming 21st Replenishment of the World Bank's International Development Association (IDA), which is the primary source of concessional finance for LDCs and other lower-income countries, will need to be the largest ever to help meet SDG financing needs. The Fourth International Conference on Financing for Development should galvanize progress on these efforts to achieve ambitious outcomes.

Development cooperation needs to step up its political and financial engagement in mobilizing other (public and private) financial resources for sustainable development.

The Addis Ababa Action Agenda recognized the importance of international public finance as a catalytic force. While there have been many good examples of the galvanizing effect of development cooperation, these remain too limited in scale and scope. Political engagement at home as well as technical assistance is needed to ensure that development cooperation helps to mobilize other resources, for example additional tax revenue by providing capacity support in this area, sustainable finance by deepening local markets, and mobilization of private investment at scale and for impact through a new approach to blended finance focused on impact. Support for sustainable trade and responsible business conduct can ensure that trade and investment flows contribute to sustainable development.

Climate finance—and the alignment of international development cooperation with climate and biodiversity goals—are not keeping pace with the escalating impacts of climate change.

While climate finance has grown over time and an increasing share of climate-related development finance also targets biodiversity goals, commitments have yet to be fully met. Climate finance flows, mainly adaptation finance, remain grossly inadequate particularly for the most vulnerable countries, causing a further widening of the financing gap. While the creation of the Loss and Damage Fund marks a historic milestone, more financial commitments will be crucial. At the same time, the increasingly complex and fragmented global climate finance architecture has not only created monitoring and reporting challenges, but has also made coordination and access to finance more difficult for developing countries, particularly LDCs and SIDS.¹ Several proposals have been put forward to improve the climate finance governance structure.² Concerns also remain over how to ensure the additionality of support for climate change mitigation and other areas that have a global public good character. The Fourth International Conference on Financing for Development provides an opportunity to address these challenges, including additionality, and ensure that climate finance is effectively delivered at scale.

The effectiveness of development cooperation must be revitalized to pursue better development results and strengthen trust in a rapidly changing financing landscape. International development cooperation has changed in multiple ways over the last decade, with a more diverse set of providers, different modalities and more complex instruments, which have increased burdens on developing countries. Amid all these changes, delivering support effectively remains as important as ever, including to better allocate and mobilize more resources, while paying more attention to the quality, impact and effectiveness of development cooperation, which has been lagging.

This chapter will provide a brief overview of ODA trends over the past two decades within the context of a more crisis-prone world. It then elaborates on the role of MDBs, including as critical sources of affordable long-term finance to developing countries. The chapter also discusses developments in the area of blended finance and mobilized private finance and concludes with a discussion of South-South cooperation and finance for climate change and biodiversity.

2. Official development assistance

ODA trends in a more crisis-prone world

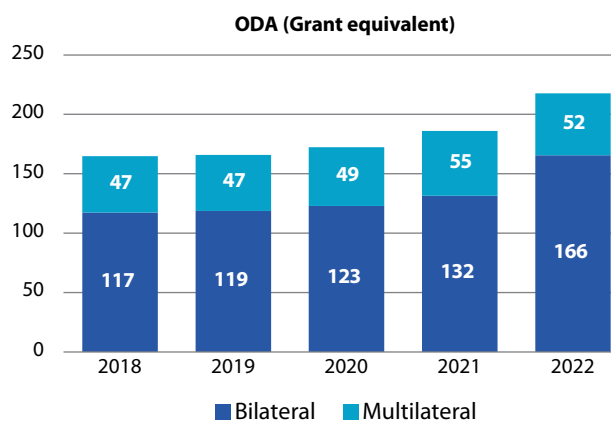
While ODA has risen to record highs in recent years, it has failed to keep pace with escalating needs and continues to fall short of commitments.

ODA levels have risen significantly over the past three years, driven by responses to multiple crises. In 2022, ODA provided by members of the OECD DAC rose by 17 per cent in real terms to reach an all-time high of \$211 billion, as calculated by the new grant-equivalent measure (figure III.C.1). However, this sharp increase was largely attributed to a surge in donor countries' spending on processing and hosting refugees, as well as aid for Ukraine. ODA to Ukraine from DAC countries surged from less than \$1 billion in 2021 to \$17.8 billion in 2022. Excluding in-donor refugee costs, ODA in 2022 increased by 7.3 per cent in real terms compared to 2021. Recent increases in ODA continue a broader upward trend since the adoption of the Millennium Declaration in 2000. Based on the previous cash-flow methodology, total net ODA to developing countries has more than doubled in real terms compared to two decades ago (figure III.C.2). However, most OECD DAC members are not meeting their international commitments. Since 2000, DAC donors, on average, have consistently failed to provide 0.7 per cent of their GNI as ODA and 0.15–0.20 per cent of GNI to LDCs (table III.C.1). In 2022, four donor countries met or exceeded the 0.7 per cent target and only two—Luxembourg and Sweden—met or exceeded both targets.

There are growing concerns that in a more crisis-prone world, persistently higher spending on refugees and humanitarian aid will come at the expense of support for long-term SDG investments.

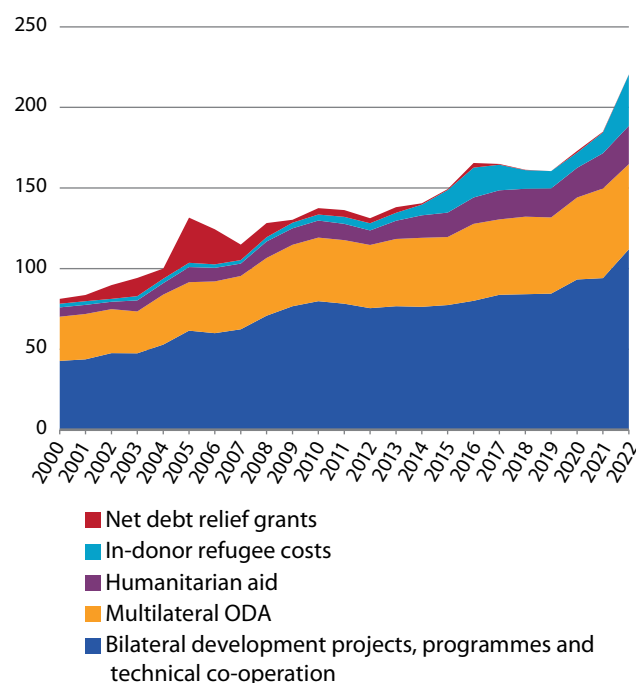
Amid a series of humanitarian crises and more prolonged conflicts, in-donor refugee costs and humanitarian aid as a share of total net ODA have increased from just over 9 per cent in 2000 to 25 per cent in 2022 (figures III.C.2 and III.C.3). This trajectory poses a risk of diverting ODA support away from the poorest and other vulnerable countries and from investments in the SDGs and climate action. In 2022, DAC countries' bilateral aid to LDCs and sub-Saharan Africa fell by 5.2 per cent and 8.6 per

Figure III.C.1
Official development assistance, 2018–2022
(Billions of United States dollars, 2021 constant prices)



Source: OECD Creditor Reporting System database.

Figure III.C.2

ODA on a cash basis by component, 2000–2022*(Billions of United States dollars, 2021 constant prices)*

Source: OECD Creditor Reporting System database.

cent, respectively. This highlights the urgent need to increase the total ODA envelope to ensure that additional resources are available to address the mounting challenges to sustainable development. Given the difficulty of budgeting for volatile humanitarian funding and in-donor costs, setting targets for country programmable aid (CPA) in addition to total ODA could reduce the risk of diversion of resources from important multi-year projects for sustainable development.³

As more countries pass per capita income “graduation” thresholds, more efforts are needed across all contexts to ensure a smooth and sustainable transition from requiring international support.

In the context of international development cooperation, “graduation” encompasses three separate events, namely, graduation from: i) ODA eligibility; ii) multilateral concessional assistance, including concessional windows at MDBs (see *MDB section*); and (iii) LDC status.⁴ A country’s GNI per capita is a key metric in determining graduation in the first two cases, and also plays a role in LDC graduation (which also includes measurement of a country’s human resources and vulnerability).⁵ There is a need to strengthen the support provided to countries as they undergo graduation in all contexts, including by enhancing emphasis on pre-graduation planning, capacity development and extending exceptional and temporary support measures.⁶ As income per capita increases, some countries lose access to concessional finance, which increases the risk of financing gaps in critical areas of sustainable development such as health and education. Graduates that are highly vulnerable to climate-related disasters and shocks and other natural disasters face additional challenges. In response, in the 2020 and 2023 OECD triennial reviews of the DAC list of ODA-eligible countries, several SIDS were granted a delay in their graduation from ODA

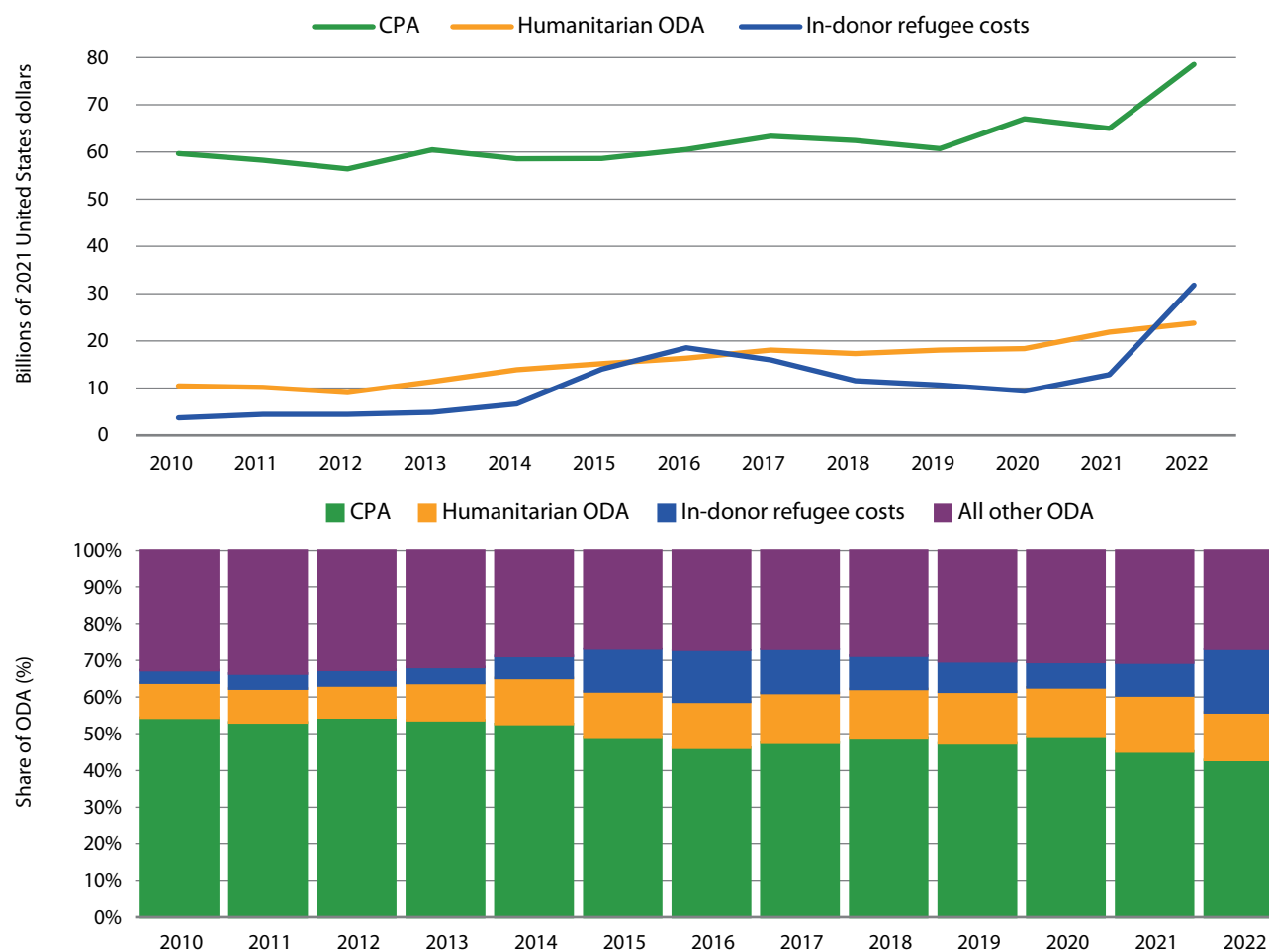
eligibility. ODA providers are also increasingly including greater flexibilities for different risks and vulnerabilities that graduated countries may encounter. In 2018, the DAC agreed on a set of rules and criteria for reinstating a country that had graduated on the DAC list of ODA recipients, particularly if the country had suffered a large negative per capita income shock. As discussed below, there are exceptions for multilateral concessional assistance that, for example, allow SIDS to access concessional funding even if they exceed income thresholds. However, there is a need to strengthen and institutionalize support provided to countries as they undergo graduation in all contexts.⁷ This could include increasing emphasis on mobilization of broader public and private resources, pre-graduation planning, capacity development in areas where financing constraints may be greatest and extending exceptional and temporary support measures for countries in transition.

Vulnerability criteria could be used to complement income measures in allocation decisions for concessional financing.

Growing systemic risks and more frequent and severe natural hazards have increased the urgency of incorporating vulnerabilities into access to concessional finance. For SIDS in particular, their small size, remoteness and high vulnerability to climate-related shocks have constrained their capacity to mobilize public resources domestically. Hence, many low- and middle-income SIDS rely on ODA to a significant extent, while other high-income SIDS have seen significant accumulation of external debt. The new Multidimensional Vulnerability Index (MVI), which offers a comprehensive approach to characterize and measure vulnerabilities, could complement income-based criteria to determine more accurately the needs for accessing additional sources of financing and highlights the steps that countries must take to build structural resilience. In its report published in September 2023, the High-level Panel of Experts on a Multidimensional Vulnerability Index for Small Island Developing States found that 70 per cent of SIDS, 63 per cent of LDCs and 50 per cent of landlocked developing countries (LLDCs) scored above the median, highlighting their structural vulnerability and lack of resilience across multiple sustainable development dimensions.⁸ However, any decision to incorporate vulnerability criteria in allocation decisions must be carefully analysed for impacts on all eligible countries, and to ensure alignment with the eligibility criteria of allocation frameworks.

The focus areas of ODA allocation have shifted in response to changing global priorities and emerging challenges. CPA, which excludes donor refugee costs, humanitarian aid, debt relief and administrative costs, is the portion of aid that donors can programme for individual countries or regions, and over which partner countries could have a greater say. CPA has declined compared to its peak in 2009, coinciding with the growing focus of aid providers on humanitarian aid and refugee expenditure. In volume terms, CPA to developing countries has increased significantly over the past 20 years, mirroring the overall increase in ODA, and reaching a total of \$97 billion in 2022 (figure III.C.4). CPA to most developing regions, including LDCs, LLDCs and Africa, grew at a rapid pace in the 2000s, but declined for many recipient countries in the post-world financial and economic crisis period: Between 2011 and 2019, total CPA to LLDCs and the SIDS contracted at an annual average rate of 1.2 per cent and 3.0 per cent, respectively. Amid the impact of recent crises and competing demands, a more constrained ODA budget environment could further decrease CPA to vulnerable countries.

Figure III.C.3

CPA, humanitarian ODA and in-donor refugee costs, as shares of official development assistance, 2010–2022*(Billions of United States dollars, 2021 constant prices, and per cent)***Source:** OECD Creditor Reporting System database.**Table III.C.1**
OECD DAC performance against international commitments

	Target	2000	2007	2012	2016	2020	2021	2022
ODA as a share of GNI	0.7	0.22	0.27	0.28	0.32	0.33	0.33	0.37
No. of countries that met target		4	5	5	5	6	5	4
ODA to LDCs as a share of GNI	0.15 - 0.20	0.05	0.08	0.09	0.09	0.09	0.09	0.08
No. of countries that met target		7	9	8	6	6	5	3

Source: OECD Creditor Reporting System database.**On a sectoral basis, aid to social sectors remains the largest category of ODA to developing countries.**

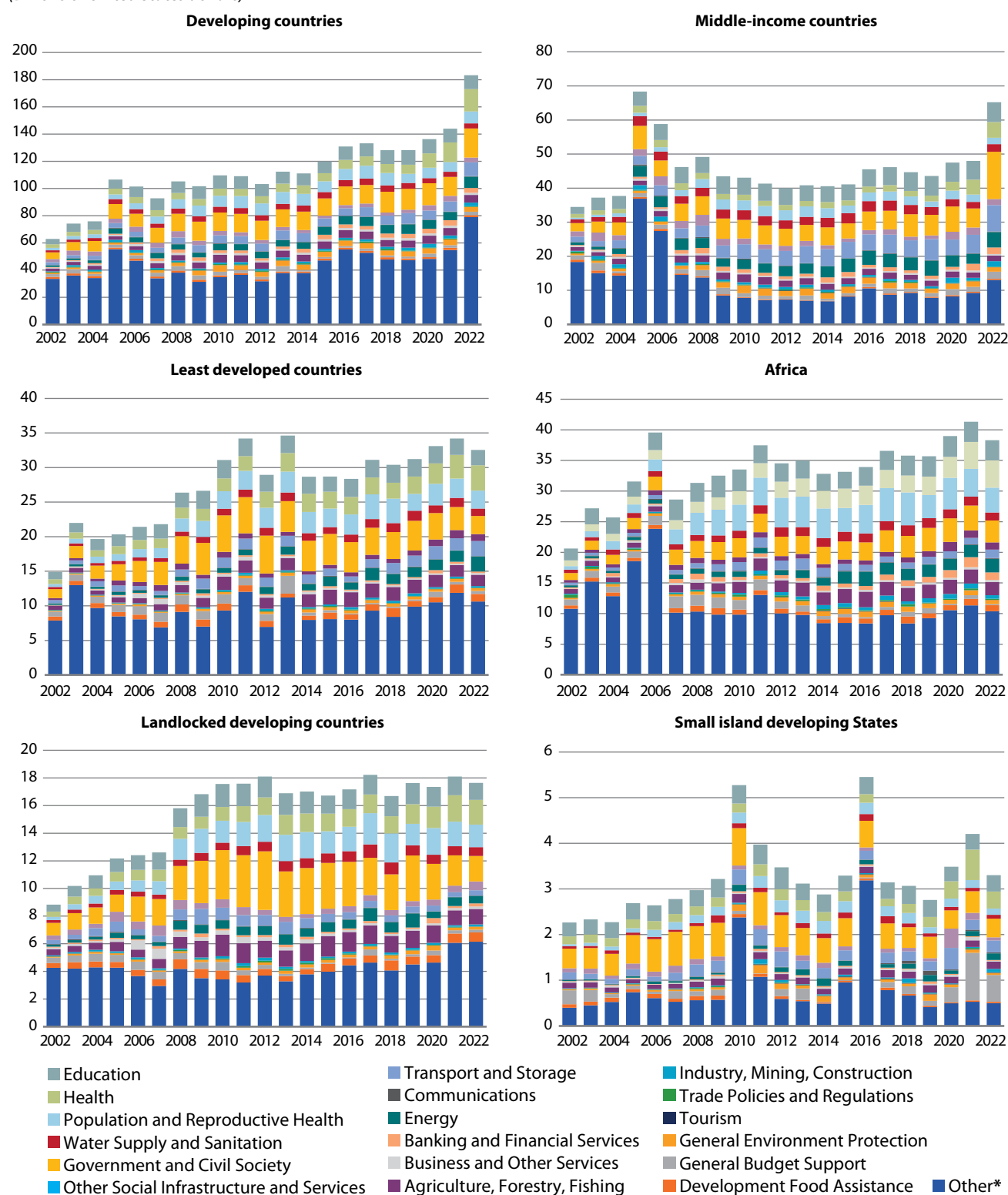
Support to social sectors is crucial to help vulnerable countries strengthen their systems and build resilience to future shocks. Prior to the pandemic, ODA for the social sectors, including health and social protection systems, was on a declining trend, particularly for LDCs, LLDCs and SIDS. This trend has partially reversed over the last three years, driven by responses to COVID-19. Overall, aid flows do not, at the aggregate level, seem to be well matched with recipient country priorities, even though alignment with country priorities is acknowledged

to be a key factor in the quality and effectiveness of development cooperation. For example, since 2009, LLDCs have experienced a steady decline in assistance channelled to the transport and storage sector, despite the acute logistical and infrastructure challenges faced by these countries. The adoption of integrated national financing frameworks informed by national development cooperation policies can guide allocation of ODA and other forms of international development cooperation to better support country priorities and national sustainable development strategies.

Figure III.C.4

ODA by sector, on a cash basis, 2002–2022

(Billions of United States dollars)



Source: OECD Creditor Reporting System database.

Note: The "Other" sector includes various categories, such as Other Commodity Assistance, Other Multisector, Action Relating to Debt, Humanitarian Aid, Administrative Costs of Donors, Refugees in Donor Countries, and Unallocated/Unspecified.

The share of ODA commitments with gender equality objectives has declined since the pandemic. Since 2011, the volume and share of DAC countries' ODA commitments with gender equality as a policy objective had steadily increased, reaching \$60 billion on average per year or 45 per cent of total bilateral allocable aid in 2019/20 (figure III.C.5). However, while volumes have continued to increase, the share fell to 43 per cent in 2021/22, down from 45 per cent in 2019/20. By sector, the integration of gender equality is particularly weak in the humanitarian and energy sectors despite evidence that integrating gender equality objectives in programming across every sector can strengthen the effectiveness and sustainability of interventions.^{9 10} Amid an increase in competing needs, there are also growing risks of distortion, dilution and diversion of finance, which would affect both the quality and quantity of financing for gender equality.¹¹ To address this, donor countries should intensify efforts to prioritize gender-focused ODA commitments and enhance gender policy safeguards. Leadership commitment by donors and well-designed adaptive programming are crucial in helping to advance ODA for gender equality.¹²

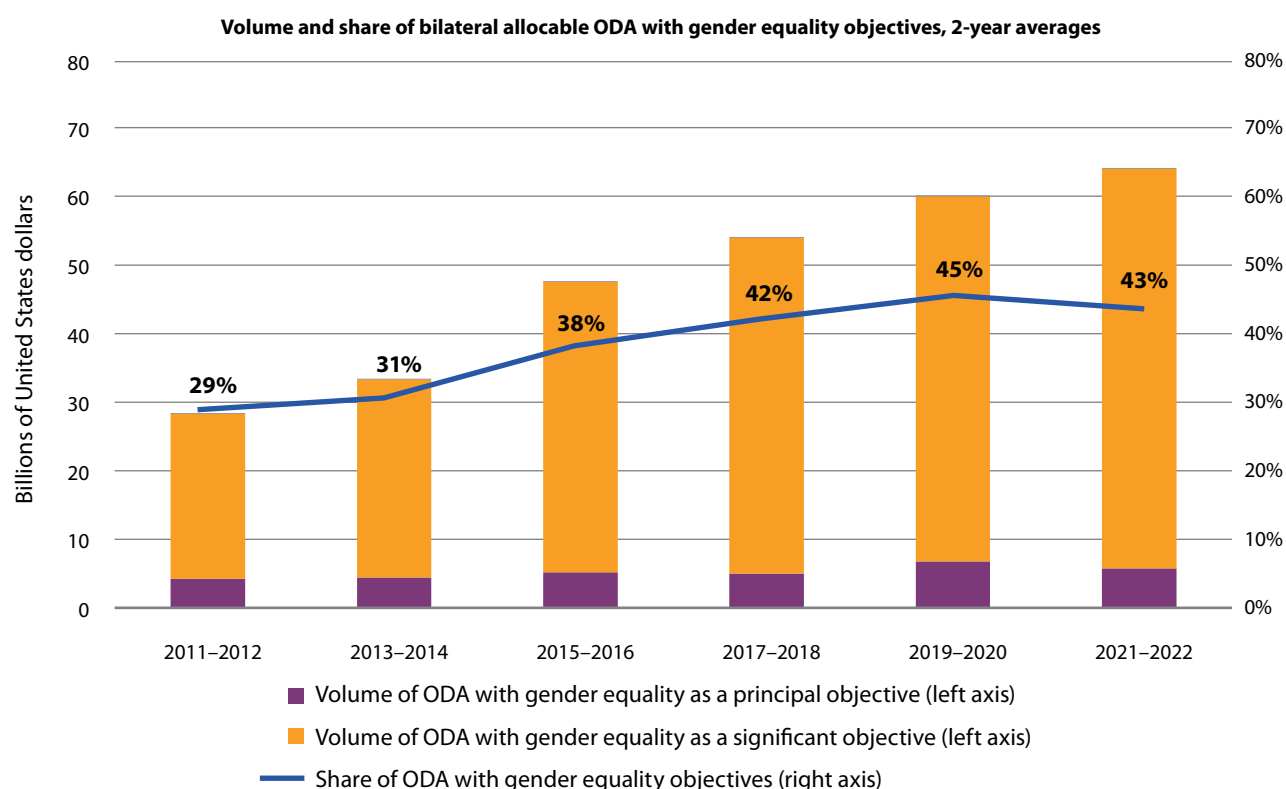
Amid a rapidly changing development finance landscape, there are multiple ongoing efforts to update and improve measurements of official support. In 2012, the OECD DAC began a process to

modernize the way that ODA is measured and reported.¹³ The main objectives of this process are to ensure the integrity and comparability of DAC members' data on development finance, create the right incentive mechanisms for effective resource mobilization and better reflect the changing development cooperation landscape. This includes the increasing significance of non-DAC providers, more diversified financial instruments, the importance of debt sustainability and the growing overlap between development policy objectives and other policy areas.¹⁴ The DAC clarified the eligibility rules for peace and security (2016) as well as in-donor refugee costs (2017) and migration-related activities (2022), introduced the grant equivalent system for measuring ODA for a fairer reflection of actual efforts by donor countries and a more realistic comparison of grants and loans (2014),ⁱ reached a consensus on the treatment of debt relief which introduced a hard ceiling equal to the nominal value of the original loan for debt relief of ODA claims (2020), and agreed on revised methods for treating private sector instruments in ODA, which will become effective in 2024. In parallel, there have also been efforts to develop a broader measure of cross-border resource flows beyond ODA and to support to the provision of global public goods as part of total official support for sustainable development (TOSSD) (box III.C.1).

Figure III.C.5

Volume and share of ODA commitments with gender equality and women's empowerment as principal and significant policy objective, 2011–2022

(Billions of United States dollars, 2021 constant prices)



Source: OECD Creditor Reporting System database.

ⁱ The introduction of the grant equivalent system and of a quantitative definition of concessionality aimed at correcting major inconsistencies in DAC members' interpretation of the term "concessional in character" within the ODA rules.

An important improvement to the SDG indicator framework was adopted in 2022 with new indicator 17.3.1 on additional financial resources mobilized for developing countries from multiple sources, which includes a clear set of cascading sustainable development criteria to only count flows aligned with the SDGs. It contains six separate sub-indicators for data on: a) Official sustainable development grants; b) Official concessional sustainable development loans; c) Official non-concessional sustainable development loans; d) Foreign direct investment; e) Mobilized private finance on an experimental basis; and f) Private grants. The United Nations Conference on Trade and Development (UNCTAD) and the OECD as co-custodians have undertaken to ensure that there are no overlaps in global reporting for this indicator in cases where countries or multilaterals provide their information to both organizations.

Humanitarian finance

Large-scale crises and emergencies have driven unprecedented humanitarian needs globally, but funding has not kept pace.

Over the past two decades, financing requirements for the United Nations-coordinated humanitarian response plans have risen about 30-fold, from \$2 billion in 2000 to a record high of \$57 billion in 2023.¹⁵ The growth in humanitarian finance needs has accelerated in recent years due to the war in Ukraine, protracted armed conflicts, the global food crisis, the climate crisis and increasingly frequent disasters, as well as

health epidemics (including COVID-19, Ebola, cholera and monkeypox). It is estimated that 300 million people worldwide are in need of humanitarian assistance in 2024, close to double the 168 million in 2019.¹⁶ With the rise in humanitarian needs far outpacing funding, the humanitarian financing gap has widened to its highest level ever (figure III.C.6). In 2023, only one third of requested funding was received, with the first decline in funding in 13 years. With competing pressures on aid budgets, there is a high risk that new emergencies will both remain underfunded and further divert resources away from longer-term development funding and support for existing crises, including in the African continent.¹⁷ This requires comprehensive action to reduce risk, address root causes and build resilience in humanitarian contexts.

Progress in strengthening the humanitarian financing model has been mixed. Given escalating needs and the evolving nature of crises, the international community has continued to explore new ways to improve the efficiency and effectiveness of humanitarian aid. Established in 2006, the United Nations Central Emergency Response Fund (CERF) remains a key instrument in funding very early responses to humanitarian emergencies. In 2016, Member States committed to doubling the annual funding target of CERF from \$450 million to \$1 billion, but contributions have fallen far short of the target, totalling \$612 million in 2022. CERF funds now account for just over 1 per cent of global requirements, down from 9 per cent in 2007.¹⁸ The Contingency Fund for Emergencies of the World Health Organization (WHO), which was set up in 2015, has provided rapid responses to disease outbreaks and health emergencies, including the COVID-19 pandemic. Substantial progress has been made in delivering on the commitments of the 2016 Grand Bargain and the reformulated 2021 Grand Bargain 2.0, including improvements in cash assistance coordination, more flexible and multi-year funding, improved joint needs analysis and more harmonized reporting. However, challenges remain in other areas, including a lack of progress in ensuring the participation of affected people and limited direct funding to local and national actors.¹⁹ Another key issue is the phenomenon of debanking, sometimes as a result of unintended

Box III.C.1

Broader measures of development support

Total official support for sustainable development

Initiated by the OECD and developed by an international task force of experts created in July 2017, TOSSD aims to capture both cross-border resource flows to developing countries and support to international public goods and global challenges. It includes concessional and non-concessional support from traditional and emerging bilateral and multilateral finance providers, including South-South and triangular cooperation providers. It also captures private finance mobilized by official interventions. TOSSD data on 2022 flows was published in February 2024, covering activities from 119 respondents, including 58 countries and 61 multilateral organizations. Several pilot studies have also been conducted, including to ensure appropriate review of TOSSD data by developing countries.^a TOSSD 2022 data includes activity-level information for \$438 billion of official support and an additional \$62 billion of private finance mobilized by official interventions.^b TOSSD is one of the data sources for indicator 17.3.1.

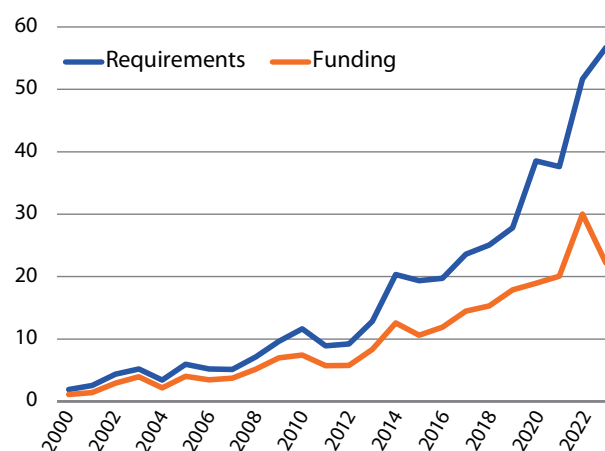
From 2024 onwards, the TOSSD standard will be governed by the International Forum on TOSSD with a balanced representation of provider and recipient countries (including dual provider/recipients) and international organizations. Civil society organizations will have a permanent observer seat in all bodies of the International Forum on TOSSD.^c

^a See the TOSSD website at <https://tossd.org/pilot-studies-data-stories/>.

^b TOSSD data available at <https://tossd.online>.

^c Terms of Reference of the International Forum on TOSSD available at https://tossd.org/docs/TORS_IPT_Oct_2023_final.pdf.

Figure III.C.6
Humanitarian response plans, funding gap, 2000–2023
(Billions of United States dollars)



Source: United Nations Office for the Coordination of Humanitarian Affairs (OCHA). 2023. "Appeals and Response Plans 2023". Financial Tracking Service, accessed 15 January 2024.

consequences of anti-money laundering or countering the financing of terrorism standards, or international sanctions, which highly complicates the delivery of humanitarian services. Political will and collective action over the next phase of the Grand Bargain (2023–2026) are needed to accelerate improvements to the humanitarian finance landscape. Innovative measures to expand the humanitarian finance toolbox should also continue to be explored, as called for in the 2016 Agenda for Humanity. These could include scaling up investments in pooled-funding mechanisms like CERF, which can help to simplify and expedite emergency responses.²⁰

The most cost-effective actions to tackle growing humanitarian needs are preventative, such as investments in disaster risk reduction, peace and security. Yet, insufficient attention is being paid towards prioritizing such investments. Despite the world experiencing the highest number of violent conflicts since 1945, DAC members' spending on peacebuilding and conflict prevention in fragile contexts has declined to a 15-year low, accounting for 10.8 per cent (\$5.27 billion) of its total ODA in 2021.²¹ Countries are recognizing the urgent need to shift away from reactive responses to crises towards scaling up pre-arranged funding, such as through improved joint planning and systematically mainstreaming disaster risk reduction into the humanitarian system.²² At the same time, anticipatory financing remains limited even when studies have shown that a large number of humanitarian crises are foreseeable.²³

Enhancing the coherence and complementarity between humanitarian assistance, development co-operation and peace efforts in contexts affected by crises remains critical. The growing prevalence of protracted crises threatens to reverse gains in sustainable development, while blurring the line between humanitarian and development needs. In 2022, four out of five people in need of humanitarian assistance lived in countries experiencing protracted crisis.²⁴ The New Deal for Engagement in Fragile States by the Group of Seven (G7) Plus, which was endorsed in 2011, laid out a first set of principles to guide development interventions in fragile or conflict-affected situations. In 2017, the United Nations Joint Steering Committee to Advance Humanitarian and Development Collaboration was established to ensure that humanitarian assistance efforts and longer-term sustainable development programmes are more coherent, with the objective to achieve collective outcomes to reduce need, risk and vulnerability. Addressing humanitarian needs and human rights necessitates investments in promoting sustainable development recognizing the pivotal role of resilience.

3. The role of MDBs

MDBs are a critical source of affordable, long-term finance to developing countries and provide essential countercyclical support in times of crisis. The time horizons of MDBs and public development banks (PDBs) are longer than those of private investors, enabling them to provide long-term and concessional financing terms for investments that would otherwise not be competitive on a risk-return adjusted basis. MDBs provide grants, concessional finance and non-concessional finance at below-market rates, including for middle-income countries. MDBs have also provided vital countercyclical support to developing countries in times of crisis, as evidenced by the sharp increase in disbursements following the 2008 world financial and economic crisis and the recent COVID-19 pandemic shock in 2020.

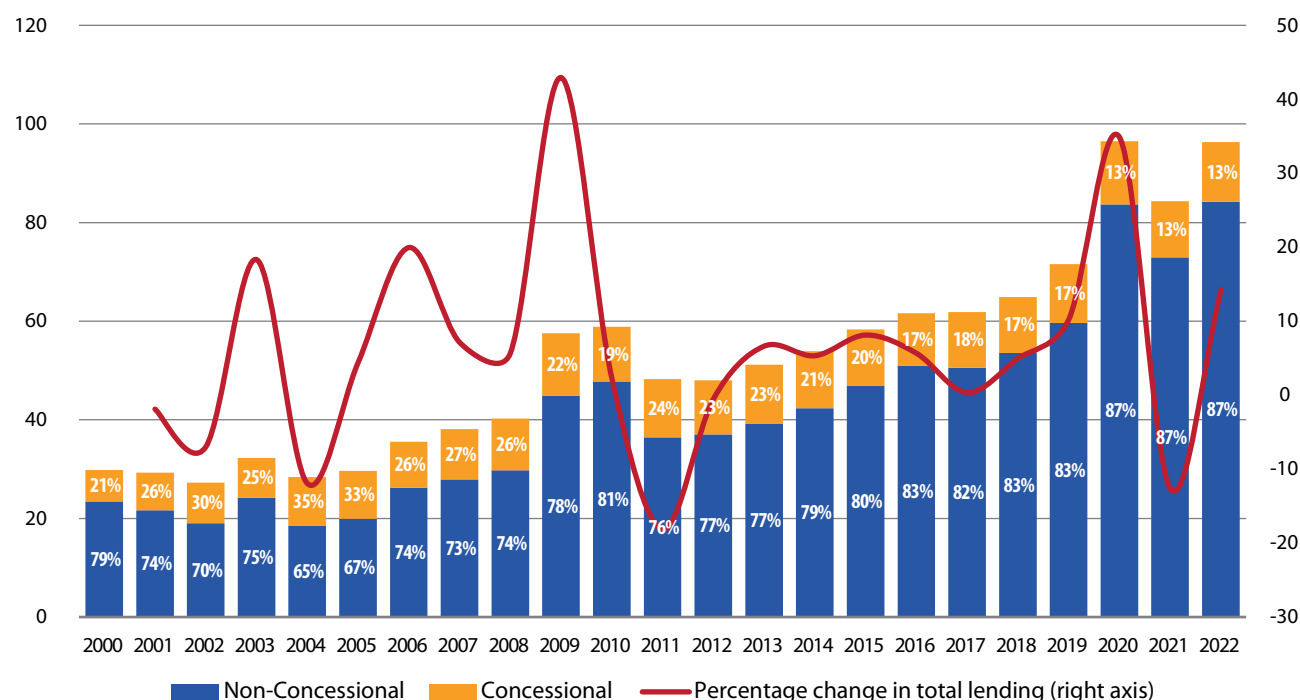
The focus areas of MDB lending have evolved over the past few decades amid a changing global landscape and a more diverse set of development priorities. Historically and in line with their original mandates, the primary focus of many major MDBs, such as the World Bank's International Bank for Reconstruction and Development (IBRD) and the Asian Development Bank, was to provide financing for large-scale infrastructure projects. This was broadened to include support for policies and programmes to reduce poverty and strengthen health, education and other human development programmes.²⁵ In recent years, growing attention has also been paid to alignment with sustainable development and the SDGs, and to considerations of how best to support global public goods such as addressing climate challenges and pandemics.

Over the past two decades, MDB lending has grown significantly, although concessional funding has declined. Annual disbursements increased from \$30 billion in 2000 to \$96 billion in 2022 (figure III.C.7). The establishment of two South-led multilateral financial institutions over the past decade have provided additional sources of infrastructure finance, while contributing to the strengthening of South-South cooperation (see section 6). While concessional finance as a share of total MDB lending to developing countries rose in the early 2000s, it has since declined from a peak of 35 per cent in 2004 to 13 per cent of total MDB lending in 2022. Similarly, the share of grants to LDCs and SIDS has declined from peaks seen in the 2000s. This trend may reflect the challenge of providing higher volumes of financing with no associated increase in the volume of donor contributions, leading to fewer concessional resources.

The World Bank's IDA remains the largest source of concessional financing. IDA remains the primary source of concessional financing for lower-income countries. The most recent replenishment of IDA (IDA20) was finalized in December 2021, with a record-high \$93 billion financing package for fiscal years 2022 to 2025. In 2023, the World Bank established a new Crisis Facility for IDA aimed at scaling up support for the world's poorest and most vulnerable countries, including to address food insecurity and extreme climate events.²⁶ In the face of multiple global shocks, however, the World Bank board has emphasized the need for donor countries to further boost the availability of IDA resources going forward. Further measures to strengthen IDA's medium- to long-term financing capacity were assessed at the December 2023 mid-term review of IDA20. At that time the next replenishment was launched, and IDA21 negotiations will continue through 2024.

Development banks are in a unique position to accelerate investments in sustainable development. Scaling up MDB resources and better aligning MDB operations with the SDGs is critical to meeting heightened demands. Relative to the size of the global economy and to needs, the financial capacity of MDBs remains limited: With the exception of the African Development Bank, the paid-in capital bases of MDBs have not increased in line with the expansion of the global economy or with growing investment needs (figure III.C.8). The Addis Ababa Action Agenda already stressed that development banks should make optimal use of their resources and balance sheets consistent with maintaining their financial integrity. It also encouraged MDBs to update and develop their policies in support of the sustainable development agenda and establish a process to examine their own scale, roles and functions in order to adapt and better respond to the challenges in achieving the SDGs. Recent multiple global shocks, including the COVID-19 pandemic and the growing

Figure III.C.7

Lending by MDBs, 2000–2022*(Billions of United States dollars, current)***Source:** World Bank, International Debt Statistics.

climate crisis, have increased the urgency of such a review. The Group of Twenty (G20) Independent Review of MDBs' Capital Adequacy Frameworks laid out proposals for the MDBs to optimize the use of their resources and balance sheets. In addition, the SDG Stimulus, the Bridgetown Initiative, the Summit for a New Global Financial Pact, and other initiatives have recognized the potential for PDBs, in particular MDBs, to expand lending to meet the investment needs for sustainable development.

In response, MDBs are undertaking reforms to expand their financial capacity. Efforts to enhance financial capacity include capital management reforms, guarantee programmes and the issuance of hybrid capital (see table III.C.2 for an overview of measures taken by MDBs). World Bank shareholders agreed to a reform package boosting its lending capacity at its Annual Meetings in October in Marrakech, including through the creation of a portfolio guarantee mechanism, increasing the limits on bi-lateral guarantees, the launch of a hybrid capital instrument (including via channelling Special Drawing Rights (SDRs)), and a lowering of the minimum loan-to-equity ratio of IBRD. Going forward the institution will look at ways to better utilize callable capital. In total, measures being implemented or under consideration across the MDBs could yield \$300 billion to \$400 billion of additional lending capacity over the next decade.

The rechanneling of SDRs through MDBs has the potential to further expand lending capabilities and is under active consideration. The AfDB jointly with the Inter-American Development Bank (IADB) has put forward an innovative proposal that allows countries to provide their SDRs as hybrid capital, which they can leverage to provide long-term

financing for development and climate projects. The instrument would have a multiplier effect, leveraging SDRs by between three to four times, while maintaining the reserve asset status of SDRs. MDBs are already prescribed holders of SDRs. In 2023, the IMF approved five new institutions to be prescribed holders, bringing the total number to 20. While several major countries have expressed interest in channelling SDRs through MDBs, technical challenges remain.

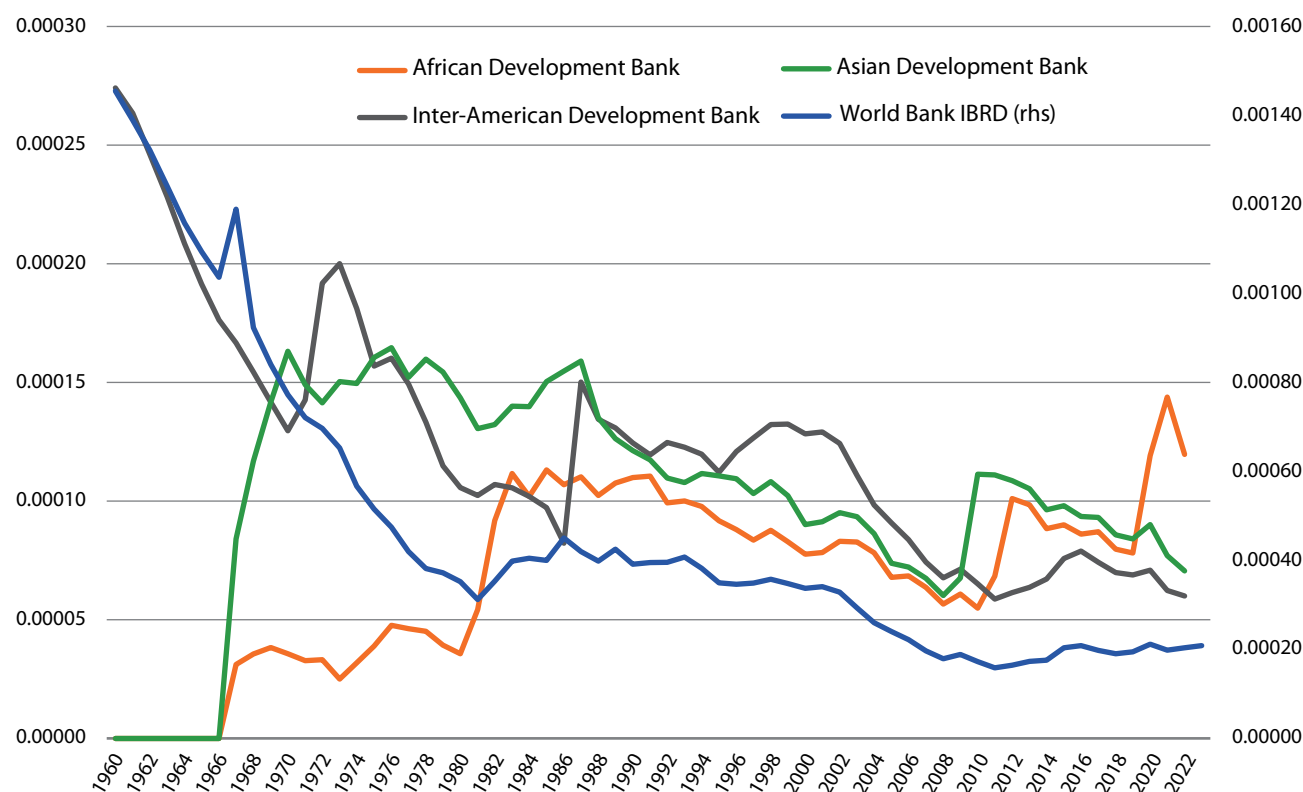
Amid mounting challenges to sustainable development, MDBs are also taking steps to better align their lending and business practices with the SDGs and climate action. For example, the World Bank has a new vision to *create a world free of poverty on a livable planet*. To this end, it will create a Livable Planet Fund by opening the Global Public Goods Fund to governments and philanthropies. Resources from the Livable Planet Fund will be used as part of the framework for providing financial incentives for investments in global public goods, including helping countries to better navigate long-term social and human capital investments and to incentivize the exit from coal as part of energy transitions. A new Corporate Scorecard aligned with the new vision and mission of the World Bank was endorsed by shareholders in December 2023. The World Bank has also expanded its Crisis Preparedness and Response Toolkit with fast access to cash for emergency response, scaled up access to pre-arranged financing for emergency response and expanded catastrophe insurance.

Improving the terms of lending of MDBs, including through the provision of longer-term and local currency loans, can provide more breathing space for developing countries. MDBs are also

Figure III.C.8

Paid-in capital as a share of world gross product, select MDBs, 1960–2022

(Ratio)



Source: UN DESA calculations, updated from the United Nations Secretary General's SDG Stimulus.

considering a range of reforms to adjust the terms of their lending. These include the provision of ultra-long-term loans to allow time for investments to have an impact on economic growth and development, with the World Bank exploring loan maturities of 35 to 40 years to help countries better navigate long-term social and human capital investment. Increasing local currency financing, as is the case with the New Development Bank, can reduce the risk of debt distress arising from currency volatility, while contributing to the lowering the debt risk profile of borrowers. At the same time, the inclusion of climate resilient debt clauses in MDB loan contracts, which is now being pioneered by several development banks, would provide breathing space for countries hit by natural disasters or other exogenous shocks.

Eligibility to MDB concessional windows is primarily based on income per capita, but MDBs have increasingly incorporated elements of vulnerability into access criteria. As of December 2022, 36 countries had graduated from IDA. Since the founding of IDA, 46 countries have graduated, and 10 of these graduates have since re-entered, or “reverse graduated” from IDA.²⁷ While a country’s graduation process from IDA begins when its income per capita exceeds an operational cut-off (\$1,314 in fiscal year 2024), several exceptions exist, reflecting an acknowledgement of the impact of vulnerability on development. The small Island economies exception, which has been in place since 1985, allows IDA-eligible small island economies continued access to IDA even

with higher incomes.²⁸ In 2017, small economy terms were extended to IDA-eligible non-island small States, which benefited Bhutan, Djibouti, Guyana and Timor-Leste. In 2019, the small island economies exception was further extended to IBRD small island economies based on vulnerability along with income and creditworthiness criteria, which benefited Fiji. An exceptional allowance was also made to Jordan and Lebanon in response to the Syrian refugee crisis. In 2024, the small island economies exception was further extended to qualifying IDA and IBRD non-island small States, in effect establishing a broader small States exception, effective starting July 2024. Several regional development banks’ concessional facilities, including the Asian Development Bank and the Caribbean Development Bank, also include exceptions that allow SIDS to access concessional funding even if they exceed income thresholds. Use of vulnerability measures to inform allocations of concessional finance could provide much-needed support to vulnerable countries such as SIDS.

Closer cooperation across MDBs and PDBs can strengthen the entire development bank system and deliver greater impact. At the Marrakech meetings, 10 MDBs²⁹ signed an agreement aimed at better coordination and cooperation, covering five areas: i) scaling up financing capacity, including use of hybrid capital and portfolio guarantees while stepping up their joint approach to credit rating agencies; ii) boosting efforts on climate and better tracking of outcomes beyond the current joint climate finance reporting; iii) enhancing country-level cooperation; iv)

Table III.C.2
Announced reform measures by major MDBs

Bank	Increase lending capacity	Improve terms of lending	Align operations with SDGs
World Bank	▪ \$157 billion increase over a decade^a through its evolution process ▪ Eliminated the statutory lending limit ▪ IBRD lowered minimum equity-to-loan ratio from 20 per cent to 19 per cent	▪ Exploring longer-term loans with maturities of 35 to 40 years ▪ Implemented Climate Resilient Debt Clauses (CRDCs) for vulnerable countries ▪ IDA offers 50-year loans with 10-year grace periods	▪ Referenced SDG Stimulus in discussing reform ambitions^b ▪ Established a Co-Financing Platform for MDBs to facilitate coordination across global and regional priorities
African Development Bank (AfDB)	▪ Aiming to increase funding by \$1.5 billion to \$4 billion over the next decade^c ▪ Launched the Alliance for Green Infrastructure in Africa in 2022^d	▪ Offering 50-year maturities with 10-year grace periods for African Development Fund countries in moderate risk of debt distress	
Asian Development Bank (ADB)	▪ Set to provide \$100 billion over the next decade^e		▪ Launched the Accelerating Climate Transitions through Green Finance initiative in Southeast Asia
Asian Infrastructure Investment Bank (AIIB)	▪ Introduced a new Guarantee Facility, along with IBRD, providing \$1 billion in guarantees^f ▪ Developed a new blended finance structure for green initiatives		▪ Discussed rechannelling SDRs through MDBs and scaling up blended finance with SDG impact
European Bank for Reconstruction and Development (EBRD)	▪ Removed its statutory lending limit	▪ Expanded operations to sub-Saharan Africa and Iraq	▪ Launched the Climate Adaptation Plan in 2022
European Investment Bank (EIB)		▪ Established EIB Global for development beyond Europe	▪ Committed to channelling 50 per cent of its lending towards climate-related projects by 2025
Inter-American Development Bank (IADB)		▪ Since 2021, introduced Climate Resilient Debt Clauses to three countries ▪ Established new financing mechanisms rewarding countries for nature and climate objectives	▪ Published the IADB Group Climate Change Action Plan in 2021
New Development Bank (NDB)		▪ Planning to issue 30 per cent of its loans in national currencies between 2022 and 2026, including South African rand and Indian rupee-denominated bonds.	

Source: MDB websites; CGD MDB reform tracker.

^a Adjustment of loan-to-equity ratio, bilateral guarantee limit, portfolio guarantee platform, hybrid capital instrument, AIIB guarantee against IBRD's sovereign-backed loans.

^b World Bank's Report to Governors on the World Bank Evolution.

^c Plans to Issue a hybrid capital note.

^d A blended finance instrument that will build a robust pipeline of bankable projects and generate up to \$10 billion worth of investments in green infrastructure.

^e Capital management reforms through an update of its Capital Adequacy Framework.

^f The Asian Infrastructure Investment Bank (AIIB) and the World Bank's International Bank for Reconstruction and Development (IBRD) are creating a new Guarantee Facility, which, using AIIB's capital to back IBRD's sovereign loans will issue \$1 billion in guarantees, increasing IBRD's lending capacity and diversifying AIIB's portfolio.

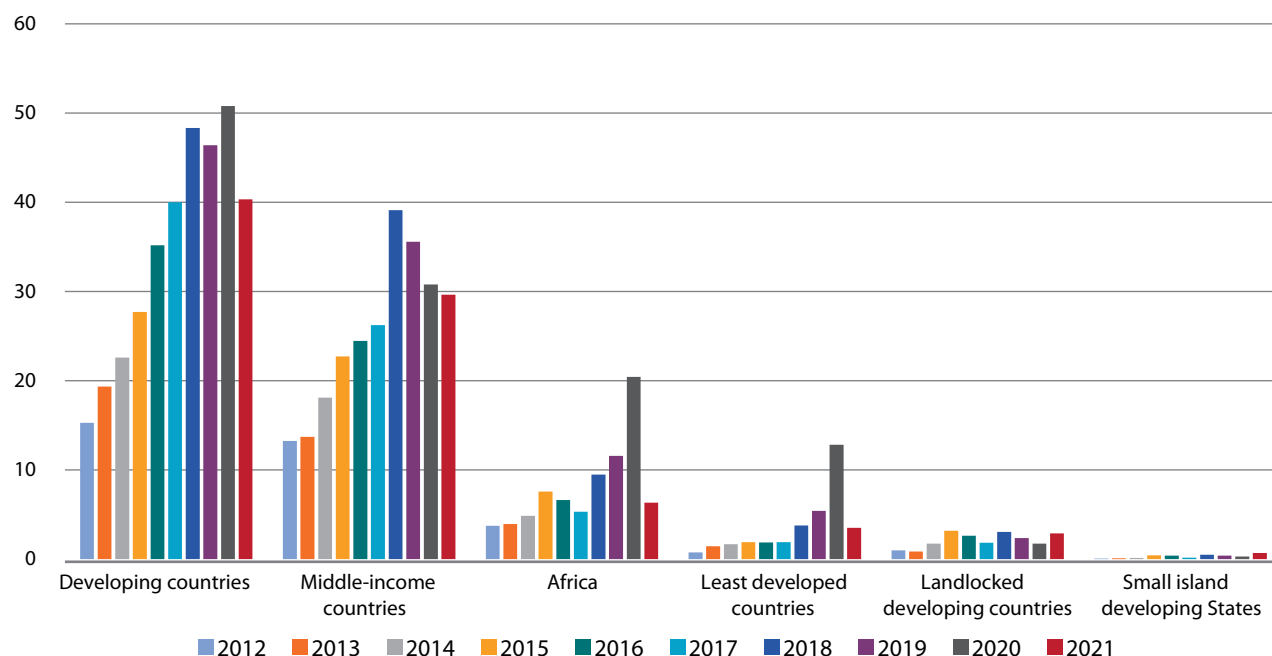
strengthening co-financing, including by standardizing processes; and v) joint mechanisms to mobilize private capital. In parallel to the MDB system, PDBs, including national development banks, have a large footprint.³⁰ The importance of cooperation among the broader ecosystem of PDBs is increasingly recognized, with PDBs at the inaugural Finance in Common Summit signing a joint declaration committing to implement a roadmap to improve the sustainability of their financing and to achieve collective results at scale.

4. Blended finance and mobilized private finance

The amounts mobilized from the private sector by blended finance activities from the official sector have grown steadily

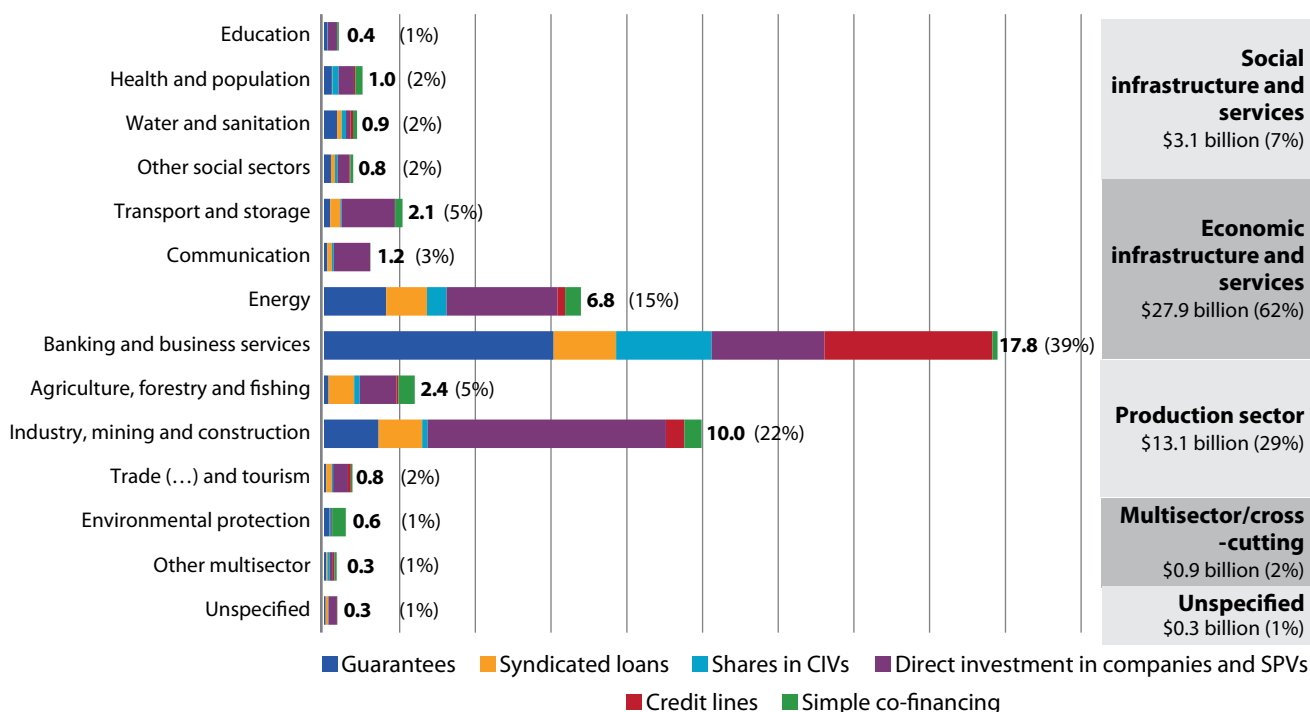
over the last decade. However, these amounts remain far below expectations. The potential for blended finance as an innovative solution to finance sustainable development, as well as principles for its use, was a main focus of the Addis Agenda in 2015. Blended finance involves the use of public development finance to crowd in additional finance, notably private finance. The main objective of blended finance is to incentivize private sector investment in areas or projects that would otherwise not be competitive with other investment opportunities, in support of national development priorities and the SDGs. Between 2012 and 2022, total private finance mobilized by bilateral and multilateral development finance providers grew by an average of 12.55 per cent annually, to reach \$61.5 billion in 2022 (figure III.C.9). Of the total mobilized, 55.5 per cent targeted the energy and banking sectors, while 5.6 per cent went to projects in social sectors (figure III.C.10). The lower share of blended finance in social sectors largely reflects the lack of a commercially viable financial return in many social sector transactions.

Figure III.C.9

Amounts mobilized from the private sector by official development finance interventions, 2012–2021*(Billions of United States dollars, current)*

Source: OECD.

Figure III.C.10

Mobilized private finance by sector, 2019–2021 average*(Billions of United States dollars, current)*

Source: OECD.

Note: CIVs = Collective Investments Vehicles, SPV = Special Purpose Vehicles.

The expansion of blended finance has slowed in recent years, constrained by the challenging global macroeconomic context, with some estimates suggesting that deal volume halved in 2022.

Convergence, a global network for blended finance, highlighted that the increase in global interest rates has constrained the balance sheets of many global banks, which are a critical source of debt capital in blended finance.³¹ Mounting debt burdens, high inflation and rising geopolitical uncertainty have also contributed to the deterioration in investor risk appetite, leading to a decline in the availability of affordable capital in emerging market economies. Amid these challenging macro-circumstances, the total volume of blended finance deals is estimated to have fallen by nearly half in 2022 compared to the previous year.³²

Only a small proportion of private finance has been channelled to LDCs. Middle-income countries attract the majority of blended finance deals. Only about 15 per cent of private finance mobilized between 2018 and 2020 went to LDCs—and to only a small number of large-scale projects—reflecting the fact that blended finance, like private finance, is drawn to areas with lower barriers to private capital mobilization. It can also indicate a tendency of blended finance to focus on less costly projects with lower-risk profiles, with projects in LDCs often characterized by less attractive risk-return profiles and potentially lower developmental impacts. In this respect, the Inter-agency Task Force has stressed that for blended finance to be applicable to LDCs, there must be a switch from a search for bankability to a search for quality and impact.

A new approach to blended finance is needed in order to realize its potential to meet the growing demand for development support.

As highlighted in earlier *Financing for Sustainable Development Reports*, the Addis Agenda sets forth several guiding principles for blended finance³³ which should be central in efforts to scale up such finance. These principles include: First, blending needs to be aligned with country priorities and be a part of broader national sustainable development strategies. Second, the primary focus of all blended deals should be development impact rather than quantity or degree of leverage. Third, analysis should always include measurement of the cost of blending versus other financing mechanisms, as well as ensuring that the public sector is not overcompensating private partners. In addition, different groups of actors have defined principles for blending for their own activities, including the 2017 OECD/DAC Blended Finance Principles for Unlocking Commercial Finance for the SDGs, and the 2017 DFI Working Group Enhanced Blended Concessional Finance Principles. The 2021 OECD-UNDP Impact Standards for Financing Sustainable Development, a guide and self-assessment tool, could help to increase the SDG impact of investments, including through improved monitoring and transparency.

5. South-South cooperation

The evolution of South-South cooperation initiatives has been marked by a growing recognition of its transformative potential.

The history of South-South cooperation dates back over 70 years, marked by the establishment of the first United Nations technical aid programme by the Economic and Social Council in 1949. Since then, South-South cooperation has evolved significantly, including through the adoption of the Buenos Aires Plan of Action (BAPA) for Promoting and Implementing Technical Cooperation among Developing Countries in 1978 and the

establishment of the United Nations Office for South-South Cooperation in 2013. Another milestone was set at the High-level United Nations Conference on South-South Cooperation in 2009, which highlighted the crucial roles that national governments, regional entities and United Nations agencies play in supporting and implementing South-South and triangular cooperation. Following the adoption of the 2030 Agenda, this commitment was reaffirmed at the second High-level United Nations Conference on South-South Cooperation (BAPA+40) in 2019, which emphasized the significance of South-South cooperation in accelerating progress towards sustainable development.

South-South cooperation has expanded in scope, volume and geographical reach. South-South cooperation has evolved substantially over the years to include a more diverse range of both governmental and non-governmental actors, while encompassing a larger number of developing countries. South-South cooperation has proven to be a valuable complement to North-South cooperation across both financial and non-financial areas of development cooperation. This was evident during the COVID-19 pandemic, when a wide range of South-South cooperation initiatives supported developing countries, including through providing finance, humanitarian relief and medical supplies.³⁴ There have also been growing efforts to measure South-South cooperation flows in a comparable manner, resulting in a voluntary conceptual measurement framework (further details below) developed and agreed upon by countries of the global South. Reflecting the rich modalities of South-South cooperation, the framework was welcomed by all Member States.

South-led development banks have enhanced the availability of financial resources for long-term investments in developing countries. In 2015, two new South-led multilateral financial institutions were established with the primary objective of mobilizing resources for infrastructure and sustainable development, namely the New Development Bank and the Asian Infrastructure Investment Bank. In tandem with growing operations and member countries, the balance sheets of both banks have expanded consistently over the past few years. For the New Development Bank, total assets have increased from \$10 billion in 2017 to \$26 billion in 2022, with total loans of \$33 billion to more than 96 projects.³⁵ To enhance its development impact, the New Development Bank is not only expanding its membership, but has also committed to more financing in local currency loans. Meanwhile, the total assets of the Asian Infrastructure Investment Bank have increased from \$18 billion in 2017 to \$47 billion in 2022.³⁶ As of end-2023, the Asian Infrastructure Investment Bank had approved a total of 251 projects with financing of over \$50 billion, benefiting many middle-income countries, LDCs, SIDS and LLDCs.³⁷ At the same time, lending by regional and subregional development banks, such as those in Latin America and Africa, continue to play an important complementary role to multilateral institutions as their regional knowledge enables them to likely be more effective in responding to regional needs and demands.³⁸

The development of a United Nations Conceptual Framework to Measure South-South Cooperation marks a breakthrough in the measurement of South-South cooperation, allowing for the quantification of both financial and non-financial dimensions. Variations in approaches, modalities and instruments of South-South cooperation across countries have made it challenging to develop a common definition and to quantify global trends of South-South cooperation flows. Progress

in South-South cooperation measurement reached a milestone in 2021, when a voluntary Conceptual Framework was developed by a subgroup on South-South cooperation as part of the Inter-agency Expert Group on SDG Indicators Working Group on Measurement of Development Support. This Framework would inform SDG indicator 17.3.1 on “additional financial resources mobilized for developing countries from multiple sources”, which was adopted by the United Nations Statistical Commission in 2022. The Commission also welcomed this Framework and requested that it be enabled by the co-custodianship of UNCTAD and led by countries from the global South.³⁹ In 2023, UNCTAD, in collaboration with the United Nations Regional Commissions and other United Nations entities, launched a capacity development project to test the Framework in eight pilot countries in Africa, Asia and Latin America. The project is intended to strengthen national coordination on data collection, while generating feedback on the feasibility and challenges of measuring financial and non-financial forms of South-South cooperation by applying the Framework in these countries.⁴⁰ In 2023, the Islamic Development Bank launched its South-South Cooperation Index, a composite measure to assess the existence, effectiveness and growth of the elements of national South-South cooperation ecosystems of a country.⁴¹ Other innovative tools to measure South-South cooperation, including measurement of its effectiveness, are also being developed (box III.C.2).

There is also a subset of Southern providers that report to the OECD: over the past two decades, development assistance flows from the 19 non-DAC countries that report to the OECD have risen from \$1.1 billion in 2000 to \$17.7 billion in 2022.⁴² In recent years, a few developing countries, including Türkiye and the United Arab Emirates, have provided ODA of more than 0.7 per cent of their GNI. Arab providers account for almost half of non-DAC reported development assistance, with flows directed mainly through grants to the Middle East and North African region.⁴³ As another major effort, China’s Belt and Road Initiative has

expanded to include over 150 countries across Asia, Latin America, Africa and parts of Europe since its launch in 2013. With the primary objective of boosting global connectivity and trade through infrastructure development, the Belt and Road Initiative has established over 3,000 cooperation projects and generated nearly a trillion dollars in investments.⁴⁴ In 2021, China launched the Global Development Initiative with the aim of revitalizing global development partnerships for the SDGs as well as to foster synergies through South-South cooperation.

Triangular cooperation is an important link between South-South and North-South cooperation. According to data compiled by the OECD, although triangular cooperation still constitutes a small share of development finance flows, its volume and usage has grown significantly over the past two decades. The largest share of triangular cooperation is with partners in Latin America and the Caribbean, and there has been a visible rise in its usage in sub-Saharan Africa and the Asia-Pacific region since 2018. While triangular cooperation is used across a range of sectors, most partners use it as an experience and knowledge-sharing instrument, particularly in regard to how to support the government and civil society. The involvement of multiple partners may sometimes create coordination challenges, leading to higher implementation costs. To better assess the evolution of triangular cooperation and its effectiveness, there is a need for all partners to improve the monitoring and reporting of its use at the national level, and to encourage better monitoring at the regional and global levels.⁴⁵

The United Nations system continues to support South-South and triangular cooperation. Most United Nations entities are mainstreaming South-South and triangular cooperation as implementation modalities towards realizing the SDGs. In 2022, 73 per cent of United Nations entities reported integrating South-South and triangular cooperation into their global strategic plans.⁴⁶ Many United Nations entities are also enhancing

Box III.C.2

Innovative tool to measure the effectiveness of South-South Cooperation

Between 2020 and 2022, Colombia, a member of the Steering Committee of the Global Partnership for Effective Development Co-operation (GPEDC), led the development of a Self-Assessment Framework on the Effectiveness of its South-South Cooperation. With support from Switzerland and the United Nations Development Programme (UNDP), the tool has been piloted in seven countries, namely Bangladesh, Cabo Verde, Colombia, El Salvador, Indonesia, Kenya and Mexico.

The tool utilizes responses to 61 questions to construct a multidimensional index of South-South cooperation effectiveness. Efforts to develop this tool involved the comparison of internationally agreed principles of effective development cooperation and those of South-South cooperation, as summarized in the 2016 UN Framework of Operational Guidelines on United Nations Support to South-South and Triangular Cooperation,^a as well as identifying common ideas between both spaces. It aims to contribute to the design and characterization of a more robust methodology to measure the effectiveness of South-South cooperation, as well as to provide insights into how a country manages the effectiveness of its South-South cooperation and to identify areas for potential improvement.^b

In the results, country ownership was found to be the most well-applied principle among respondents, potentially explained by the highly demand-driven nature of South-South cooperation.^c The results, however, also revealed that ownership is interpreted as national government-centric, with opportunities for improvement through consultations with local governments in areas where South-South cooperation activities are carried out, and with non-public stakeholders. The use of Data Governance Frameworks to standardize the use of data for informing South-South cooperation-related policy was identified as a key challenge, as only one of the seven pilot countries has a Data Governance Framework finalized and in use.

Colombia and Indonesia are currently leading efforts to further refine the tool and expand its application and uptake in other countries, including in Africa, Asia and Latin America and the Caribbean, in conjunction with the roll-out of the fourth monitoring round of the GPEDC.

^a <https://digitallibrary.un.org/record/826679?ln=en>

^b <https://www.effectivecooperation.org/system/files/2023-05/Thematic%20Initiatives%20-%20SSC%20Self%20Assessment%20%28EN%29.pdf>

^c <https://www.effectivecooperation.org/SSC-Pilot-Self-Assessment-Summary-Report>

efforts to strengthen knowledge-sharing, codify good practices and broker South-South partnerships.⁴⁷ For example, the “South-South Galaxy” platform coordinated by the United Nations Office for South-South Cooperation, promotes knowledge-sharing and partnership development, including through connecting Southern partners with financing mechanisms. The new United Nations Framework to Measure South-South Cooperation for SDG indicator 17.3.1 has started bringing United Nations entities together to support Member States in their efforts to quantify South-South cooperation. The Development Cooperation Forum knowledge platform provides an interactive platform for South-South cooperation among Member States on more than 12 topics regarding development cooperation, supporting discussion forums, initiatives, experiences and national policies.⁴⁸ Through regional agreements, the International Atomic Energy Agency supports countries in the Global South in building capacities to apply nuclear technologies and techniques in several areas, including agrifood systems and energy.

6. Finance for climate change and biodiversity

Mobilization of climate finance falls short of what is needed to effectively address the scale of climate challenges and remains

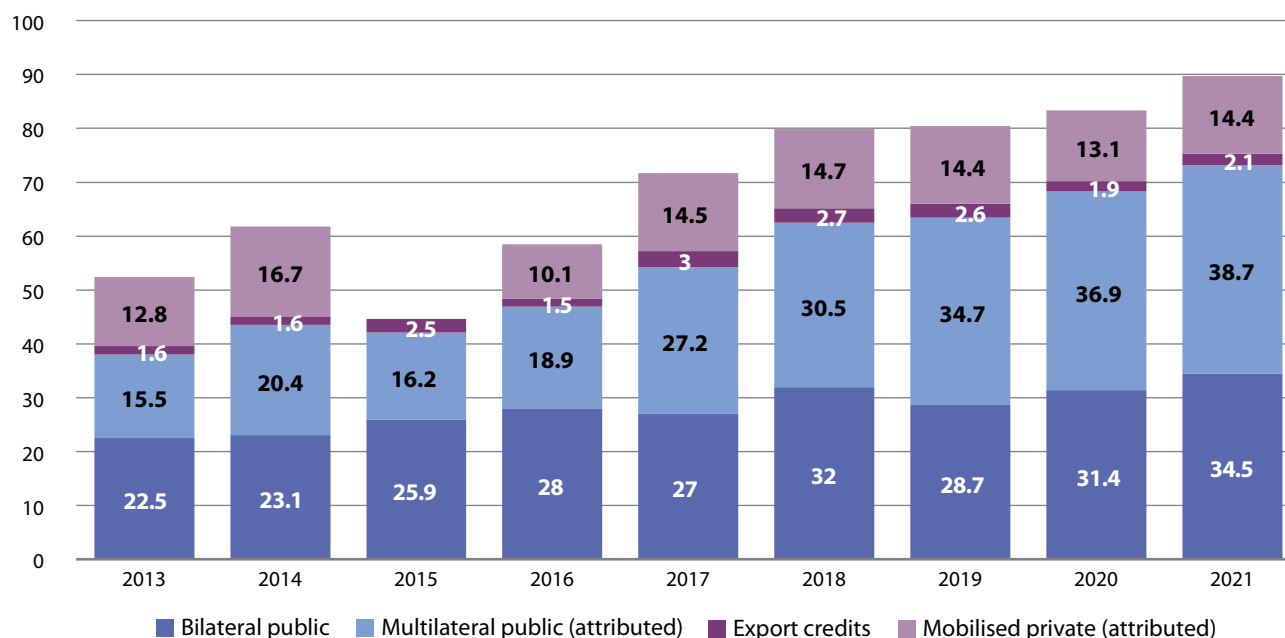
grossly inadequate for the most vulnerable countries. There are large investment gaps in climate change mitigation and adaptation as well as in disaster risk reduction; lack of investment in climate action is threatening to become a vicious circle in many countries, as limited resources prevent countries from investing in resilience, in turn making them more vulnerable to climate shocks. Both public and private financing will be needed to close these investment gaps, not least significant concessional public finance for vulnerable developing countries. At the 2009 United Nations Climate Change Conference in Denmark (COP15), developed countries agreed to jointly provide and mobilize \$100 billion a year by 2020 to support climate action in developing countries. While climate finance has grown significantly over time, the target is yet to be met. The latest OECD assessment of progress showed that climate finance provided and mobilized amounted to \$89.6 billion in 2021, an increase of over 70 per cent compared to 2013 (figure III.C.11).⁴⁹

While public climate finance has increased strongly over the past decade, private finance mobilized continues to be significantly lower in recent years, particularly on climate adaptation investments. This is despite growing interest in sustainable investing by the private sector. At the same time, climate finance channelled to countries that are most vulnerable to climate change remains grossly insufficient. Of the total climate finance mobilized between 2016 and 2021, only 17 per cent was channelled to LDCs and 3 per cent to SIDS.⁵⁰

Figure III.C.11

Climate finance provided and mobilized by developed countries for developing countries, 2013–2021

(Billions of United States dollars)



Source: Based on biennial reports to the United Nations Framework Convention on Climate Change, OECD Development Assistance Committee and Export Credit Group statistics, as well as complementary reporting to the OECD.

Note: Figures may not add up to totals due to rounding. The gap in time series in 2015 for mobilised private finance results from the implementation of improved measurement methodologies in OECD data collections from 2016 onwards. These improved methodologies measure the mobilisation effect of public interventions, taking into account the specific mechanisms employed to attract investments from the private sector, such as guarantees, collective investment vehicles, syndicated loans or project finance. Such an instrument-specific and granular approach is not fully compatible with the estimates developed for 2013–14. As a result, volumes of private finance mobilised and grand totals in 2016–18 and in 2013–14 respectively are not directly comparable.

The growing impacts of climate change underscore the importance of more ambitious climate finance goals and national commitments. At the 2023 United Nations Climate Change Conference in Dubai (COP28), countries concluded the first “global stocktake” of progress made on climate action since the Paris Agreement. The stocktake noted that the amount of climate finance remains insufficient despite growing financial pledges for climate action, including a record \$12.8 billion for the second replenishment of the Green Climate Fund. Amid intensifying climate challenges, the stocktake stressed the urgent need to raise ambitions and accelerate implementation of climate action across all areas.⁵¹ Furthermore, in 2015, countries agreed that prior to 2025, they would set a New Collective Quantified Goal (NCQG) raising the climate finance target from a floor of \$100 billion per year to account for the needs and priorities of developing countries. The discussions on the NCQG will conclude at COP29 at the end of 2024.

The global climate finance architecture has become increasingly complex and fragmented. There has been a proliferation of climate funds over the past two decades. As of end-2022, there were an estimated 81 active climate funds, consisting of 62 multilateral funds as well as bilateral, regional and national funds.⁵² While each individual fund was established with a separate purpose, as a whole they are contributing to a fragmented aid landscape, with different implementing agencies and bureaucratic processes. This has not only created monitoring and reporting challenges but has also made coordination and access to finance more difficult for developing countries, especially LDCs and SIDS. As the urgency to ramp up climate investments grows, so have calls for reforms to enhance the coherence and effectiveness of the global climate finance architecture. Proposals include shorter-term measures such as improving the coordination and specialization of funds, and longer-term strategies such as the consolidation of dispersed funds to create mechanisms at scale.⁵³

The adaptation finance gap is widening. Although adaptation finance has increased over the past decade, it has not kept pace with growing climate risks. Despite pledges made at COP26 to double adaptation finance by 2025, adaptation finance has recently been falling: bilateral adaptation-related ODA reached \$27 billion in 2021, according to data provided by OECD DAC members. This marked a decrease from the \$30 billion reported in 2020 (although it was an increase over the 2019 volume of \$20 billion).⁵⁴ At the same time, estimates of adaptation costs have risen significantly and are expected to increase further amid accelerating climate impacts.⁵⁵ Against this backdrop, the adaptation finance gap has widened to its highest ever, with adaptation needs estimated at 10 to 18 times greater than finance flows.⁵⁶ Bridging this gap requires more than just an increase in public resources, but also, where possible, greater private finance. To attract more private capital to adaptation activities, new and innovative instruments and mechanisms are being explored (box III.C.3). These include the African Development Bank’s Adaptation Benefits Mechanism which aims to share risks and incentivize investments in adaptation.⁵⁷

MDBs are playing a stronger role in funding climate action, but shareholders need to ensure that funding for mitigation in particular is additional. In response to the growing urgency to scale up climate finance, MDBs are raising their climate ambitions, including to provide higher levels of adaptation finance. In recent years, the provision of climate finance by MDBs has surpassed the targets they set in 2019,⁵⁸

Box III.C.3 Innovative development finance

The potential for innovative finance to enhance development cooperation was first recognized in the Monterrey Consensus. Shortly thereafter, the Leading Group on Innovative Financing for Development was established with the aim of promoting innovative solutions for financing across various areas, including health, poverty eradication, food security and climate change. While no agreed definition exists, innovative financing for development has often been understood to include sources and mechanisms that raise additional funding for sustainable development on top of conventional ODA.^a

While there have been some successes in innovative financing, particularly early in the period, overall uptake has remained limited. Earlier discussions were focused on solidarity taxes, which were successfully used in funding UNITAID (to address HIV/AIDS, tuberculosis and malaria). Other measures to better manage aid flows have also been introduced, such as ODA securitization and advanced market commitments for funding vaccines (most recently for COVID-19 vaccines). As noted in the Addis Agenda, these earlier innovative instruments still have the potential to be replicated and scaled up.

The series of global shocks over the past few years have reignited interest in the innovative public finance agenda, in particular to scale up financing of global public goods, including for health and climate action. Following the success of COVAX, the multilateral mechanism for equitable global access to COVID-19 vaccines, there have been growing discussions on enhancing future pandemic preparedness, including through the establishment of a pandemic vaccine pool.^b At COP28 in Dubai, a group of international organizations and development finance institutions announced plans to boost innovative financial instruments for sustainable climate and nature-linked sovereign financing.^c Other recent innovative finance proposals include imposing a levy on shipping emissions, taxes on extreme wealth^d and a facility to support food imports for countries most exposed to surging food prices.^e

^a https://www.diplomatie.gouv.fr/IMG/pdf/2021_12_-_leading_groupe_innovative_financing_en__web2_cle85adb2.pdf

^b <https://reliefweb.int/report/world/world-leaders-commit-us48-billion-help-break-covid-now>

^c <https://www.iadb.org/en/news/eight-international-organizations-and-development-finance-institutions-join-forces-boost>

^d <https://www.theguardian.com/business/2023/jan/18/tax-us-now-ultra-rich-wealth-tax-davos>

^e Responding to soaring food import costs and addressing the needs of the most exposed (fao.org)

with financing for low- and middle-income countries reaching a record \$61 billion in 2022.⁵⁹ A few MDBs, including the World Bank and the Asian Development Bank, recently revised their climate finance commitments to above their post-2020 targets. In addition to increasing financial flows, MDBs also have an opportunity to improve how these funds are programmed and disbursed. Climate and debt-vulnerable countries, such as LDCs and SIDS, need more concessional resources and grants. The MDBs launched the Joint Methodological Principles for Assessment of Paris Agreement Alignment in June 2023 and have been implementing this

framework for aligning their operations with the goals of the Paris Agreement. This includes working together to strengthen the global response to the threat of climate change in the context of sustainable development and efforts to eradicate poverty, by keeping global warming well below 2° Celsius above pre-industrial levels and pursuing efforts to stay below 1.5° Celsius; fostering adaptation, resilience and low-emissions development without threatening food production; and ensuring that finance flows are consistent with a pathway towards low-emissions, climate-resilient development. MDBs also need to develop mechanisms to better account for climate finance to ensure that increasing financing for climate action does not come at the expense of development finance for other priorities.

Global climate finance discussions reached an important breakthrough at the end of 2023 with the creation of the Loss and Damage Fund. Loss and damage first appeared in negotiated outcomes as part of the Bali Action Plan in 2007, but discussions only gained momentum from 2013 onwards.⁶⁰ In 2022, the United Nations Climate Change Conference in Sharm el-Sheikh (COP27) decided to establish a Loss and Damage Fund to support vulnerable countries in addressing the escalating effects of climate change. The creation of the Fund reflects the growing recognition that developed countries, largely historically responsible for climate change, should provide support to developing countries in dealing with irreversible losses and costly damages due to climate disasters. At COP28, governments pledged around \$700 million to the Fund, which will be hosted at the World Bank on an interim basis. In light of the size of climate-related losses, which have been estimated at around \$400 billion a year by 2030 for developing countries,⁶¹ more financial commitments from developed countries will be crucial, as will be the mobilization of other sources of financing, including private finance. For the Fund to be effective, its efforts should also be coordinated with existing climate adaptation and mitigation initiatives to help close gaps in the current architecture and ensure complementarity and a more holistic approach.

Biodiversity finance

Biodiversity loss is a threat to human well-being and sustainable development. The unprecedented decline in biodiversity and environmental degradation pose systemic risks to a large number of social and economic goals.⁶² Over half of the world's GDP is moderately or highly dependent on nature and is thus exposed to the risks posed by biodiversity loss.⁶³

The international community must mobilize more financial resources to halt and reverse the decline in biodiversity. The Addis Agenda contained a range of commitments to protect ecosystems, including one that encourages the mobilization of financial resources to conserve and sustainably use biodiversity and ecosystems. This was consistent with the Strategic Plan for Biodiversity 2011–2020 and its Aichi Targets of the Convention on Biological Diversity. The latest progress report showed, however, that at the global level none of the 20 targets had been fully achieved, although six targets have been partially achieved, including target 20 on resource mobilization.⁶⁴ ODA for biodiversity-related objectives more than doubled over the period of the Strategic Plan for Biodiversity, from \$5.4 billion in 2011 to \$11.1 billion in 2021,⁶⁵ but the broader biodiversity financing gap remains large.⁶⁶

In the follow-up to the Strategic Plan, the Kunming-Montreal Global Biodiversity Framework was adopted in December 2022,

marking a historic agreement that lays out a set of ambitious goals and targets to address the rapid loss of biodiversity. These targets include the repurposing of \$500 billion per year in harmful subsidies, mobilizing at least \$200 billion per year for biodiversity-related funding, and raising international financial resources for developing countries, in particular LDCs and SIDS, to at least \$30 billion per year. To support the implementation of this framework, the Global Biodiversity Framework Fund was launched in 2023, with Canada and the United Kingdom providing initial contributions for its capitalization. The Global Biodiversity Framework Fund, which is now operational, forms part of the Global Environment Facility (GEF), which is the main financing mechanism of the Convention on Biological Diversity. Since its inception in 1991, the GEF has delivered nearly \$22 billion in grants and mobilized another \$119 billion in co-financing. In 2022, the GEF finalized a record \$5.3 billion in pledges for its eighth replenishment round, with biodiversity protection as the largest component of its new programming period.

Despite their potential to tackle the climate crisis and biodiversity loss, the implementation of nature-based solutions (NbS) is hindered by financing and capacity constraints. The International Union for the Conservation of Nature defines NbS as actions that address societal challenges through the protection, sustainable management and restoration of ecosystems, benefiting biodiversity and human well-being.⁶⁷ Financing for NbS currently stands at around \$200 billion per year, accounting for only a third of the levels needed to achieve climate, biodiversity and land degradation targets by 2030.⁶⁸ The public sector continues to provide the bulk of funding for NbS, with private capital constituting 17 per cent of investments in NbS.⁶⁹ There are several barriers to unlocking private finance for NbS. NbS projects often do not offer financial returns competitive on a risk-return basis with other investment opportunities, with much of the investment to date through the philanthropy of impact investors. In addition, there is an absence of a consistent methodology to track NbS financing to gauge impact.⁷⁰ In 2023, a new database that matches biodiversity-related projects with public and private funders was launched, which could facilitate a more effective mobilization of resources for biodiversity conservation and restoration.⁷¹

7. Quality, impact and effectiveness of development cooperation

Effective development cooperation must once again become a central focus of financing discussions to address massive global development challenges in a changing financing landscape. The importance of effective development cooperation was first recognized in the Monterrey Consensus, which called not only for a substantial increase in ODA and other resources for development, but also for enhanced effectiveness of development cooperation. In the years after Monterrey, this agenda was discussed and strengthened through the Development Cooperation Forum—created at the 2005 World Summit—and officially launched in 2007. Since then, the Forum meets biennially to review trends, progress and emerging issues in international development cooperation and promote coherence and coordination among diverse actors and activities. The Addis Agenda recognized the need for continued efforts to improve the quality, impact and effectiveness of development cooperation through the Development Cooperation Forum, taking into account efforts

in other relevant forums, such as the GPEDC, in a complementary manner. The GPEDC, a multi-stakeholder platform that supports evidence-based dialogue and action on effective development cooperation through a global monitoring exercise, emerged from the aid effectiveness process, including the 2005 Paris Declaration on Aid Effectiveness, the 2008 Accra Agenda for Action and the Busan Partnership for Effective Development Cooperation in 2011. Monitoring by and discussions in these two different platforms dealing with international development cooperation reveal that progress in implementing these commitments has been mixed, and there is a need for reform and revitalization of this agenda.

Global progress in improving the quality, impact and effectiveness of development cooperation has been mixed since the adoption of the Addis Agenda. In the Addis Agenda, Member States agreed to align development cooperation activities with national priorities, including by reducing fragmentation and accelerating the untying of aid, particularly for LDCs and countries most in need. However, a 2021 survey on the quality of ODA showed that 10 years after the initiation of the Busan Partnership for Effective Development Co-operation and six years after the Addis Agenda, progress has been mixed.

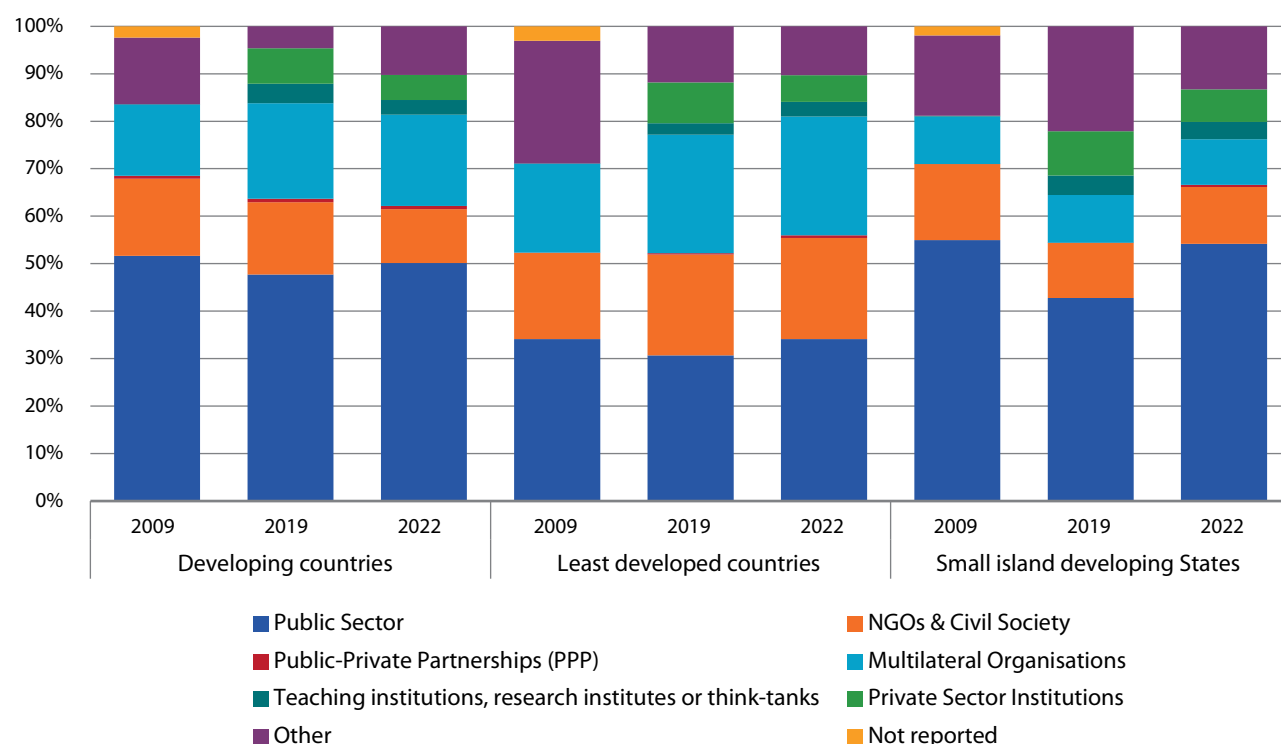
Countries are taking steps towards strengthening the enablers of development cooperation but the alignment of development partners with these enablers has been declining. A key factor in improving the quality, effectiveness and impact of international development cooperation is the strengthening of country ownership, guided

by coherent national development cooperation policies, country results frameworks, development cooperation information systems and national development cooperation forums. Since the adoption of the Addis Agenda, developing country governments have made some progress in these areas. For example, 82 per cent of 2022 Development Cooperation Forum Survey respondents reported the adoption of national development cooperation policies (up from 72 per cent in 2016) and highlighted their role in mobilizing and aligning not only ODA but also other modalities of international development cooperation. Over the same time period, countries reported engaging an increasingly diverse range of development cooperation modalities and actors.⁷² Yet, before the COVID-19 pandemic, the alignment of development partners with partner country priorities and country-owned results frameworks had been declining.⁷³ Less than half of ODA is channelled through the public sector of recipient developing countries, and only one third in LDCs (figure III.C.12).

While there has been some progress in untying aid (see below), development partners' alignment to partner country priorities and country-owned results frameworks and country public financial management systems has declined. Indeed, a broader perspective on all public and private sector financing to developing countries reveals a proliferation of official finance providers and implementing entities and the continued fragmentation of development activities, adding to the complexity of the architecture and increased transaction costs for developing countries (box III.C.4).

Figure III.C.12

Gross bilateral ODA disbursements by channel
(Percentage of total)



Source: OECD Creditor Reporting System database.

Box III.C.4**Aid architecture changes and recipient country burdens**

By complementing data reported by official donors to the OECD DAC and Creditor Reporting System with data reported by recipient governments to the World Bank Debtor Reporting System, World Bank research on aid architecture broadens the focus from ODA to all public and private sector financing to developing countries.

As official financial flows to developing countries have more than tripled over the past two decades, with the sharpest increase occurring in 2020 in the wake of the pandemic, so too has the proliferation of official finance providers and implementing entities and the continued fragmentation of development activities. All of this has added to the complexity of the global aid architecture, increased transaction costs for developing countries and impacted aid effectiveness.

Funds increasingly circumvent recipient government budgets, creating a significant coordination challenge for recipient governments. Today, three out of every four official financial flow transactions are implemented by other entities (e.g. NGOs, donor government entities and multilateral institutions) and half of these funds bypass recipient country budgets, undermining effectiveness.

An increasing number of donor-funded activities of decreasing size has resulted in fragmentation. The average ODA grant fell from \$1.5m in 2000 to \$0.8m in 2019, taxing the capacity of recipients. Pooled funding

has been a recognized solution to reduce the impact of aid fragmentation, but its uptake is low. Instead, there has been a proliferation of donors, with an increasing number of entities providing development finance: the number of donors doubled (from 47 to 70) and bilateral and multilateral donor agencies tripled (from 191 to 502). For instance, in 2020, Ethiopia, Mozambique and Nepal had to engage with 204, 172 and 154 donor agencies, respectively.

In addition, there has been a significant shift in the allocation of aid towards facilities dedicated to specific sectors or themes. These so-called vertical funds now provide developing countries with a greater volume of ODA grants than MDBs. Yet bilateral ODA channelled through horizontal platforms leverage far more resources for development than vertical platforms (the leverage ratio for horizontal platforms was 1.7 from 2011 to 2019, jumping to 3 in 2020, compared to 0.6 for vertical platforms). With limited exceptions, vertical funds use donor contributions directly as grants and only a small number of them generate new capital for development purposes or income transfers.

Source: World Bank, based on “A changing landscape: Trends in official financial flows and the aid architecture” (September 2021) and “Understanding trends in proliferation and fragmentation for aid effectiveness during crises” (July 2022).

Progress in untying aid has been uneven. Untying aid helps to strengthen country ownership and can lead to the strengthening of local economies by allowing for local procurement. Over the past two decades, the share of untied ODA has increased from an average of 47 per cent from 1999 to 2001 to 89 per cent in 2022.⁷⁴ In 2018, the DAC broadened the country coverage of the 2001 DAC Recommendation to Untie ODA to include other low-income countries and IDA-only countries, in addition to already-covered LDCs and heavily indebted poor countries.⁷⁵ However, several challenges to further progress on untying aid persist. Many countries and key ODA sectors, such as technical cooperation and food aid, remain excluded. Moreover, “informally tied aid” remains an issue amid high barriers to entry for developing country suppliers. More than half of

the value of contracts awarded in countries included in the DAC Recommendation continue to go to suppliers in DAC provider countries. While developing countries were awarded 44 per cent of the total number of contracts, these contracts represented only 13 per cent of the total value of the contracts.⁷⁶ Development partners must take urgent action to identify and remove barriers that hinder local producers, including in LDCs, so that they can reap a “double dividend” in addressing poverty and inequalities while building up local economies. In this regard, the DAC is currently reviewing the Recommendation to explore whether it could encourage greater procurement by and from local organizations and businesses in developing partner countries as policy levers to advance their sustainable development and ownership and, if so, how.

Endnotes

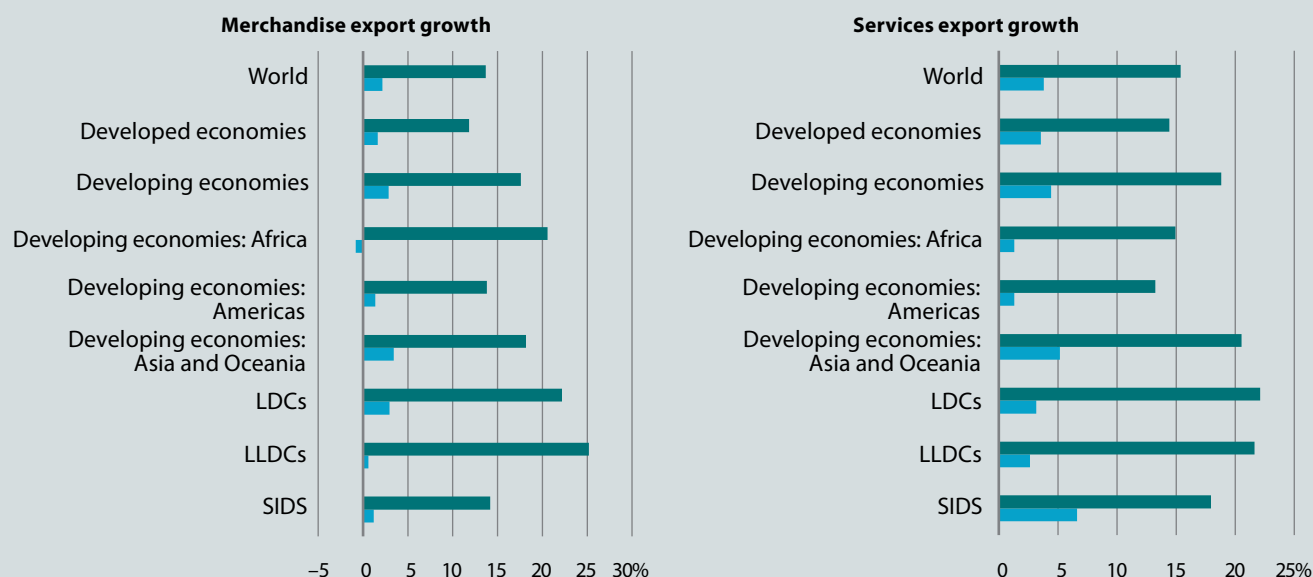
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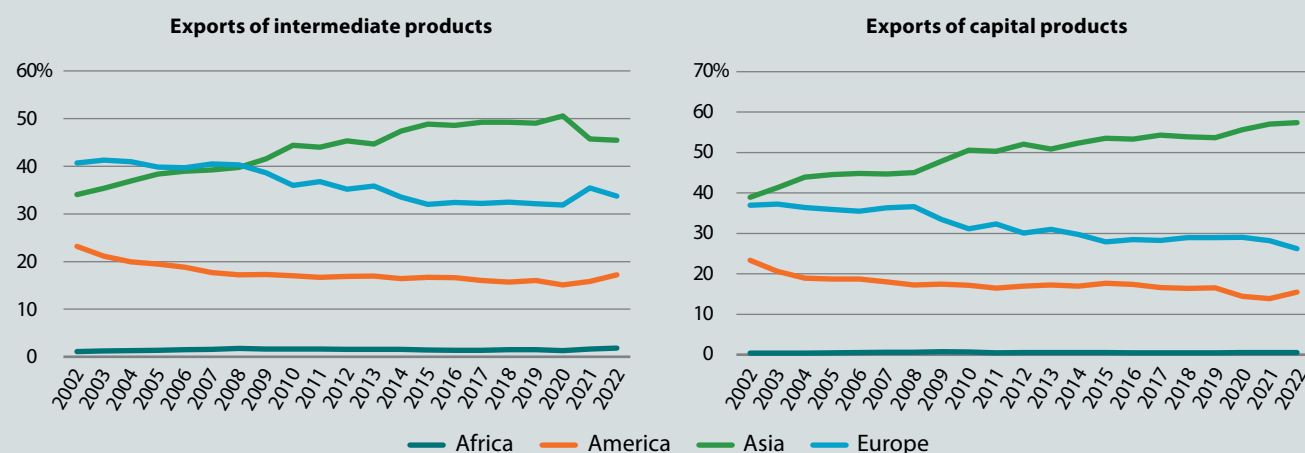


International trade as an engine for development *in numbers*

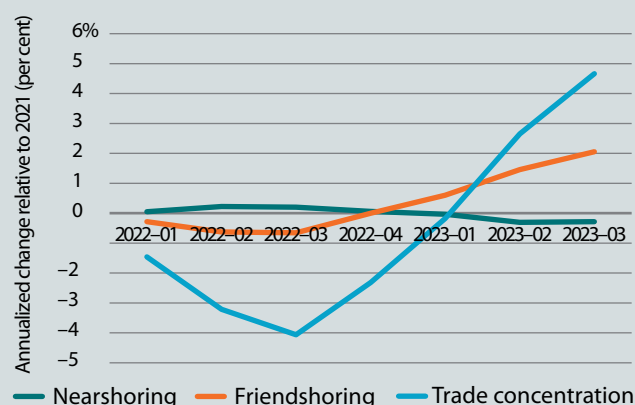
In the past two decades, international trade has acted as an engine for development for many developing countries, but trade dynamism has weakened and trade openness declined.



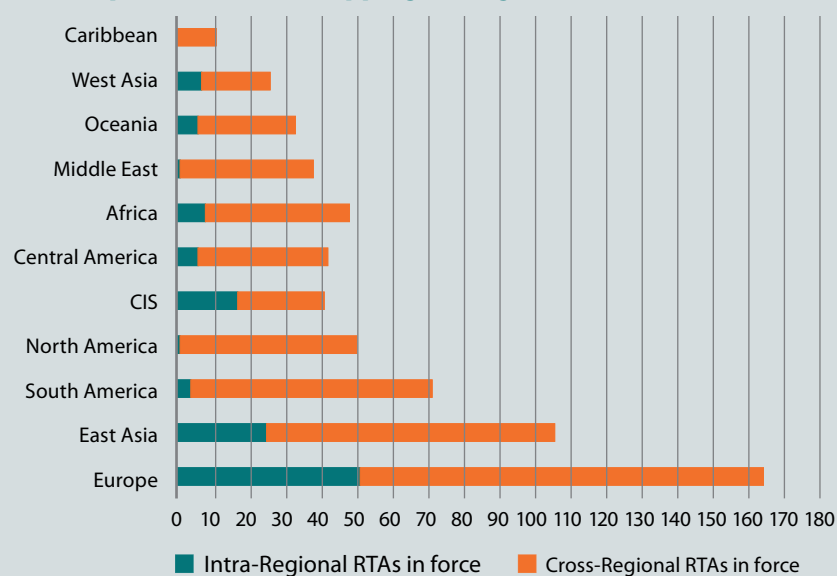
Trade growth, driven by global value chains, has been very uneven, with some developing countries, particularly in Asia, seeing rapid trade growth while many vulnerable countries remained largely marginalized.



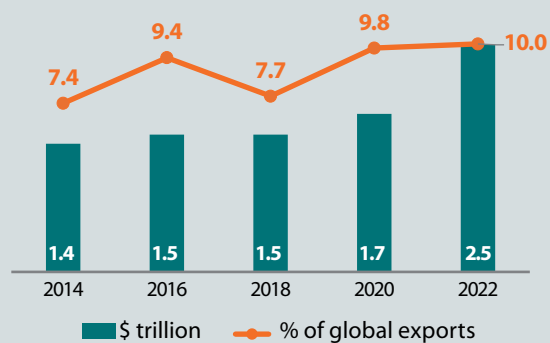
Trade growth deceleration has been in part driven by the shift towards de-risking supply chains, including through “friendshoring” and “nearshoring”.



In the absence of a comprehensive multilateral agreement on certain trade issues, countries turned to bilateral and regional trade agreements and in some cases plurilateral negotiations, resulting in a complex web of overlapping arrangements.

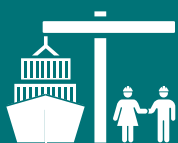


Trade finance plays a crucial role in facilitating international trade, but the global trade financing gap has increased sharply in recent years.





Chapter III.D



International trade as an engine for development

1. Key messages and recommendations

In the past two decades, international trade has acted as an engine for development for many developing countries, contributing to economic growth, poverty reduction and a narrowing of the development gap with developed countries; yet export-based development may become more difficult to pursue. While world merchandise trade nearly quadrupled in nominal terms over this period, the pace of this trade expansion has been highly uneven. A decade of rapid export growth until the 2008 world financial and economic crisis was followed by a period of weaker trade dynamism. The recent slowdown in world trade growth and declines in trade openness pose challenges for many developing countries, making the traditional export-based development model, which a number of developing countries have successfully implemented, much harder to pursue.

The vision of an open and integrated global economy with freer trade, economic interdependence and international cooperation is increasingly threatened, as increased fragmentation and an erosion of multilateralism as well as rising inequalities have prompted counter-pressures to reverse globalization and move away from existing practices. These trends have coincided with an increased focus on so-called “friendshoring” and “nearshoring” in value chains. Strong leadership and collective actions are needed to curb efforts to impose measures that are trade-restrictive and undermine global cooperation on trade.

There are also continued challenges in integrating vulnerable developing countries into the global trade of both goods and services, with digital trade threatening to further exacerbate inequalities.

Despite the increased participation of developing countries as a group, the vulnerable developing economies have largely remained marginalized in international trade. For

example, the growth in services trade has mostly benefited developed countries and a number of developing countries in Asia. The distribution of the benefits of digital trade has also been highly uneven, with countries with weak connections to networks particularly disadvantaged. This highlights the need to redouble efforts to accelerate digitalization and technology policy as well as facilitate investment in necessary infrastructures to enable such countries to benefit from digital trade.

The least developed countries (LDCs) as well as small island developing States (SIDS) and landlocked developing countries (LLDCs) remain largely marginalized in international trade. This underlines the need to continue to strengthen the participation of countries in special situations in global trade. This may include agreeing on a possible follow-up to Sustainable Development Goal (SDG) target 17.11, which calls for doubling the share of LDCs in global trade, including through accelerated efforts towards building trade and productive capacities so that the provision of preferential market access to LDCs can contribute more to export growth as well as economic diversification. This also requires redoubled efforts to put in place supportive mechanisms such as aid for trade. A fourth international conference on financing for development in 2025 should consider these and other mechanisms that can facilitate a productive integration of developing countries into the global economy.

An important impediment to accelerating integration is the global trade financing gap, which has increased sharply in recent years. The global unmet demand for trade financing is estimated to be \$2.5 trillion annually. Eighty per cent or more of global merchandise trade depends on the provision of trade financing. As private sector commercial banks will not be able to substantially narrow the trade finance gap, the role of other

trade financing providers becomes increasingly important. Multilateral development banks (MDBs) play an important role in the provision of supply chain financing in emerging markets and have provided trade financing in support of developing economies.

Moreover, the multilateral trading system as well as regional trade agreements (RTAs) and international investment agreements (IIAs) have an important role to play in providing enabling conditions for sustainable development. These agreements can be geared towards enhancing coherence between trade, investment and sustainable development, including in regard to gender equality, human rights and environmental sustainability, particularly climate actions.

There is significant scope for these agreements, once modernized, to help countries make inroads into the SDGs, as well as promote a more equitable and inclusive sharing of the gains from trade.

This chapter first discusses long-term trends in international trade, then discusses changes in the multilateral trading system, the impacts of trade on sustainable development, and finally the interrelations between trade and development financing.

2. Trade trends: Long-term trends in trade since Monterrey

2.1 Trade growth since Monterrey: rapid yet uneven

Since Member States convened in Monterrey in 2002, the pace of trade expansion has been rapid—although uneven—with the 2008 world financial and economic crisis acting as an inflection

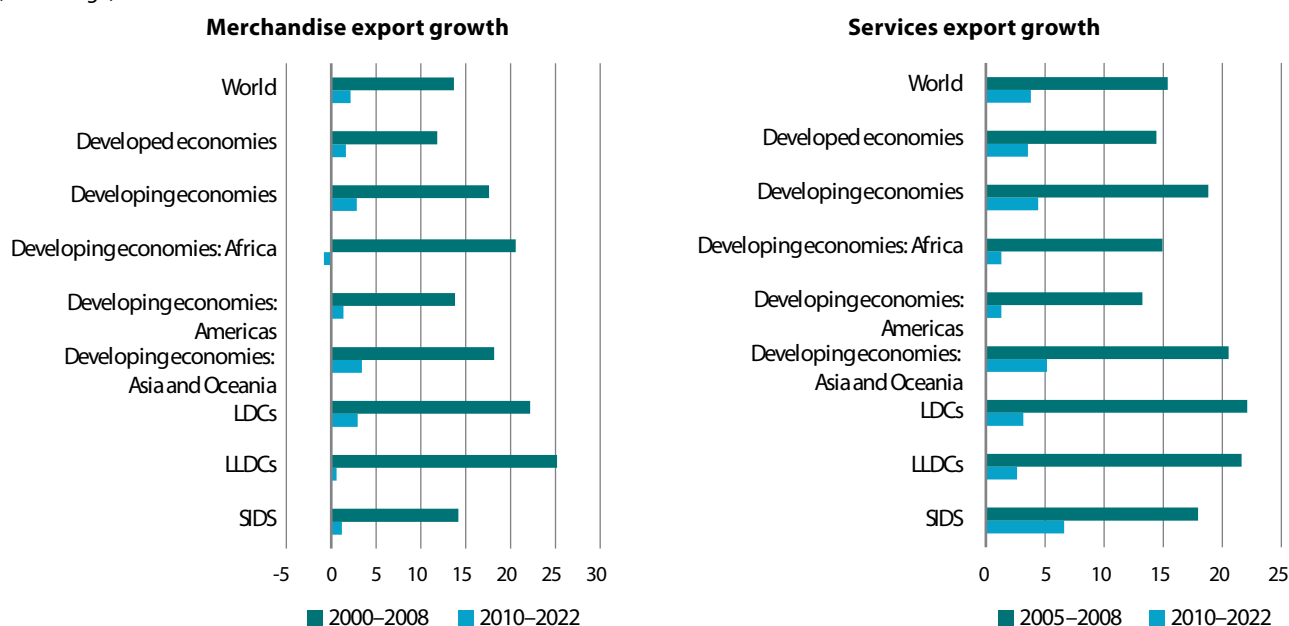
point. A decade of rapid export growth, driven particularly by developing countries in Asia, and the multilateral market opening between 1995 and 2005 was followed by weaker trade dynamism and a decline in trade openness (figure III.D.1). The main drivers of slower trade growth in the past decade include a slowdown in the expansion of global value chains (GVCs), a rise in national strategies prioritizing domestic consumption and the development of domestic supplier bases, as well as a diminishing impact of technological advances in reducing production and transport costs.¹ The special effect of the opening of economies in transition in the 1990s has also levelled off. Food and agricultural products have shown a similar pattern, stagnating since the 2008 world financial and economic crisis after an expansion in the early 2000s.²

Trade in services saw an even greater expansion than merchandise exports over the past two decades, with growth rates also slowing markedly since the 2008 world financial and economic crisis. A key driver of the expansion in services trade has been the dynamic growth of trade in digitally delivered services, which more than doubled between 2010 and 2022.

The geographical distribution of trade growth during this period was also uneven, with some developing countries, particularly in Asia, seeing rapid trade growth while many vulnerable countries remained largely marginalized. Most of the increase in the share of developing countries in world merchandise trade is accounted for by Asia. The shares of the other two developing regions, Africa and the Americas, remained muted throughout this period. LDCs and LLDCs increased their share in world trade only marginally, while it remained constant for SIDS, suggesting no meaningful progress in integrating these countries into global trade flows. Indeed, more recent trends over the past 10 years have seen LLDCs' share of world merchandise trade in goods and services

Figure III.D.1

Average export growth rate before and after the 2008 world financial and economic crisis by development status
(Percentage)



Source: UNCTAD calculations based on UNCTADstat.

decline. For commodity-dependent developing countries the diversification of exports has continued to be a pressing challenge, as these countries have exported, on average, less than a third of the number of products exported by other countries, with the gap slightly increasing over time. As commodity price indices almost quadrupled between 2000 and 2022, commodity-dependent developing countries have faced significant price variability across boom-and-bust cycles, including during the COVID-19 pandemic.

Developing country trade growth over the past two decades was driven largely by their increased participation in GVCs. The value of trade in intermediate goods, a proxy for trade in GVCs, has more than tripled since the early 2000s. Asia has been central in GVC trade, accounting now for slightly less than half of total intermediate exports (figure III.D.2). The increased participation of developing countries in international trade, leveraging upon the expansion of GVCs, is corroborated by trends in seaborne trade, where the participation of developing countries has seen a constant increase.

South-South trade has been the most dynamic trade route in the world in the past two decades, supporting the expansion of trade within GVCs. The value of South-South trade increased eightfold during the period, yet most of the rise happened during the first decade, as growth decelerated considerably after 2012. South-South trade now accounts for 54 per cent of total developing country exports, and its share in world exports almost doubled from 2000 to 2022. South-South trade is even more significant in manufactured products, particularly technology-intensive products, and has supported export diversification and upgrading. Most South-South trade involved Asia, as intraregional trade intensified throughout the value chains. South-South trade in the other two developing regions remained rather static in value terms but is growing fast in Africa in particular, underlining the potential of South-South trade for the region.

A more recent trend, contributing to the slowing of GVC expansion, has been the significant shift towards de-risking supply

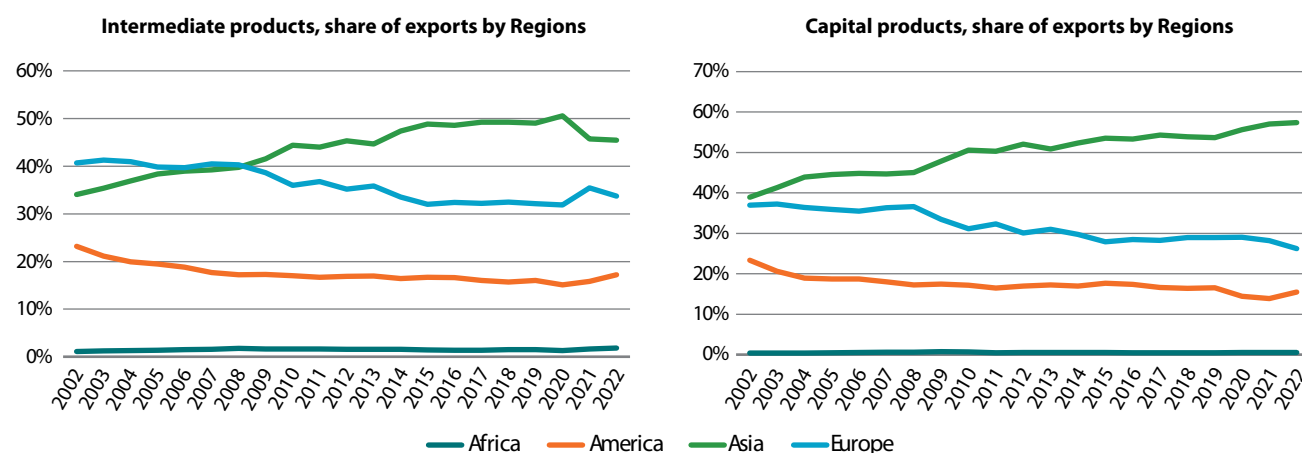
chains and diversifying suppliers and markets, including through so-called “friendshoring” and “nearshoring”. This change, depicted in figure III.D.3, is driven by heightened trade policy tensions, the disruption caused by COVID-19 and geopolitical events like the war in Ukraine. Supply chain configuration has become a primary concern for policymakers and industries, especially in the context of building resilience and self-sufficiency. Recent analysis by the United Nations Conference on Trade and Development shows that while the geographical proximity of international trade did not experience any major changes, there was a substantial rise in the political proximity of trade (friendshoring) starting in the third quarter of 2022.³

In addition, since 2010, there has been a decline in distances per tonne of containerized trade (figure III.D.4), mainly due to increased intraregional maritime trade supporting manufacturing activities in China and neighbouring countries, particularly in East Asia. The increase in the average distance travelled by containers in 2024 comes amid rising tensions in the Red Sea. However, a decrease in the distance travelled by containers is forecasted for 2025.

Overall, trade has played an important role as an engine of development and convergence for a number of developing countries, as envisaged in Monterrey. Trade has been making multifaceted contributions to development finance, generating revenue, fostering economic growth and facilitating the flow of both financial and non-financial resources. A number of developing countries, particularly in Asia, have successfully followed an export-led development model in which exports of manufactured goods play a key role in foreign exchange generation and progressive technological upgrading.

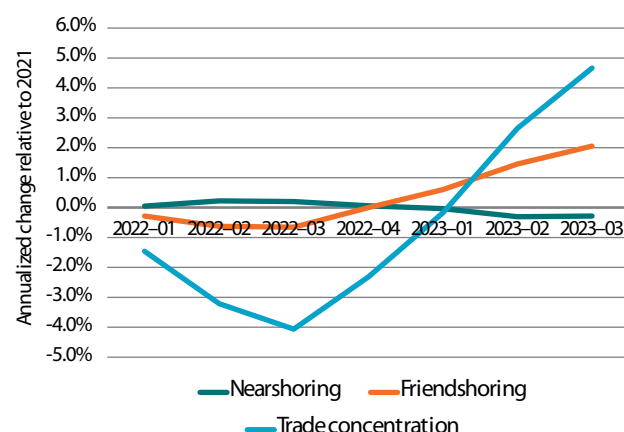
Yet, such development trajectories are increasingly difficult to pursue. The recent slowdown in world trade growth and declines in trade openness point to a persistent shift in international trade dynamism,⁴ which may reduce the appeal of export promotion development models based on manufacturing. As stressed in chapter III.B, development models that are heavily reliant on exports of manufactured goods have

Figure III.D.2
Share of world exports by region and category of products (2002–2022)
(Percentage)



Source: UNCTAD Secretariat calculations based on UN COMTRADE database.

Figure III.D.3
Recent trends in trade concentration, friendshoring and nearshoring
(Percentage annual change relative to 2021)



Source: UNCTAD estimates based on national statistics.

become increasingly difficult to pursue amid a shift towards digital business models, asset-light production and an associated slowdown in the manufacturing trade growth rate. In addition, the post-war vision of an open and integrated global economy with freer trade, economic interdependence and international rules is increasingly coming under threat. Challenges such as increased fragmentation and an erosion of multilateralism as well as rising inequalities have prompted counter-pressures to reverse globalization and return to a more divided world of regional blocs.

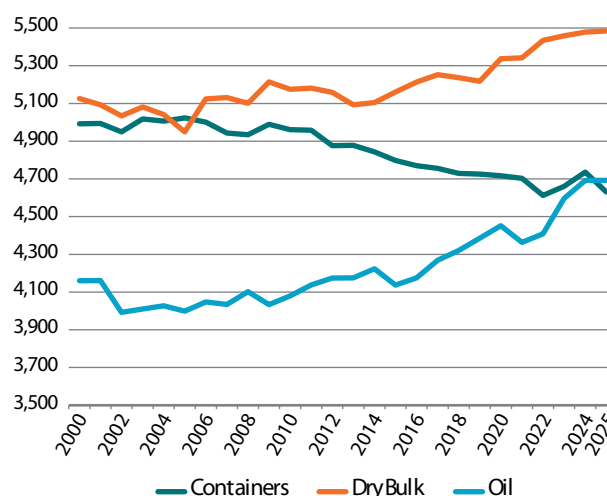
2.2 Impact of technological changes and digitalization on trade

Technological changes and digitalization have profoundly impacted trade trends since the early 2000s. Digitally delivered services have become an important component of trade, with services that can be digitally delivered over information and communications technology networks benefiting from cost efficiencies and higher reach and tradability. Digital technologies have also facilitated the direct cross-border trade of certain services, such as consulting, education and financial services. Global exports of digitally delivered services reached \$3.9 trillion in 2022, increasing almost fourfold since 2005 and accounting for 54 per cent of total global services exports and thus outpacing the growth in the export of both goods and other services.

While the participation of developing countries has increased, particularly for those in Asia, the services trade remains driven by developed countries, particularly for knowledge-intensive and digitally delivered services. Developing countries in Asia were able to increase their share of services exports (from 15 per cent in 2005 to 25 per cent in 2022), even though the participation of developing

i Nearshoring is calculated as the reverse of trade-weighted average distance in kilometers. Friendshoring is calculated as trade-weighted political proximity as measured by United Nations voting patterns. Trade concentration is calculated based on the Herfindahl concentration index.

Figure III.D.4
Average distance travelled per tonne of cargo
(Nautical miles)



Source: UNCTAD Secretariat calculations based on Clarksons Research seaborne trade data series.

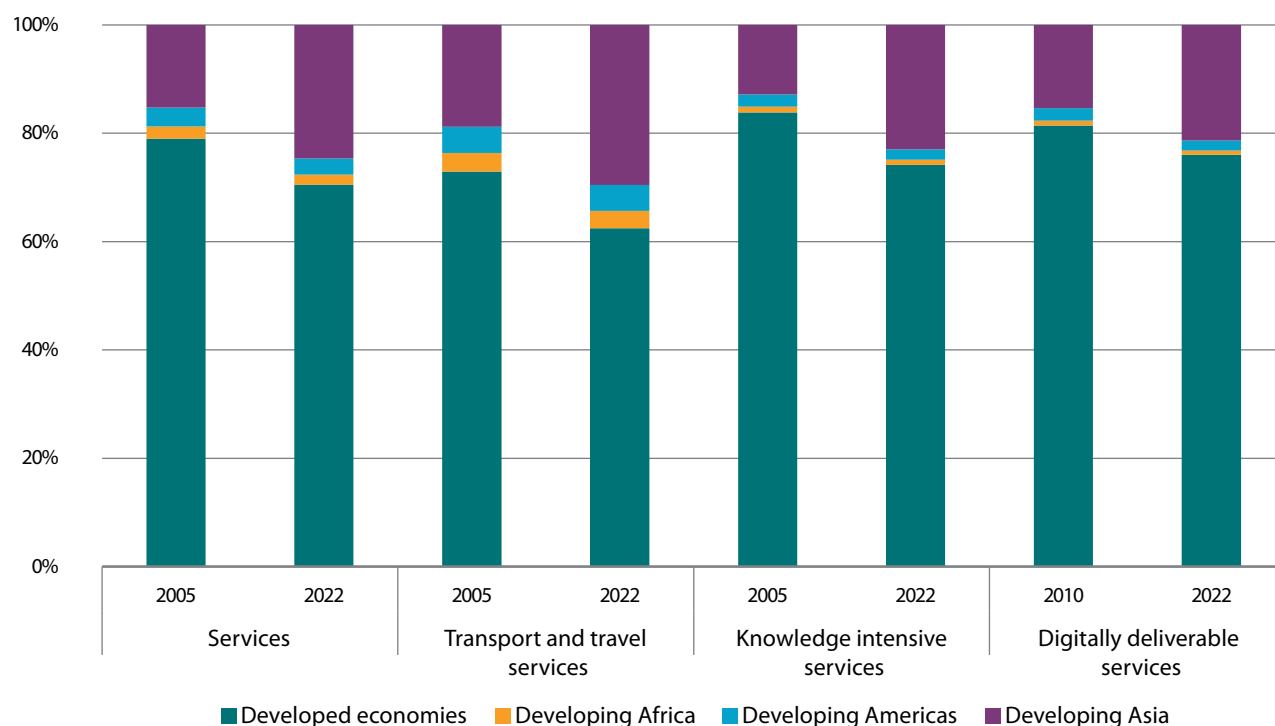
economies in Africa and Latin America and the Caribbean remained low and stable, at around 2 per cent and 3 per cent respectively (figure III.D.5).

The ongoing digital transformations render the split between what is a service and what is a good increasingly blurry. As a result, and in value added terms, services play a much bigger role in international trade than gross statistics suggest. Intermediate services are indispensable for production and exports in all sectors. Services have thus become an important component of the value added of goods and services exported by countries, giving rise to the “servicification” of economies. Indeed, the services value added that is contained in international goods and services exports now accounts for close to half of world exports, compared to about 30 per cent in 1980, with servicification being most prevalent in developed countries.

The ability to digitally deliver services also played an important role in trade resilience during the COVID-19 pandemic. While tourism and other services requiring cross-border mobility declined, digitally delivered services exports—including information technology consulting—continued to rise faster than exports of goods and other services. In the 2010 to 2022 period, digitally delivered services exports grew faster than the exports of all commercial services, both in developed and developing economies. In this trade, developing economies in Asia outpaced that of developed economies (figure III.D.6). Driven by digital technological progress and evolving business practices, the share of services trade that can be delivered remotely over computer networks is likely to continue to increase.

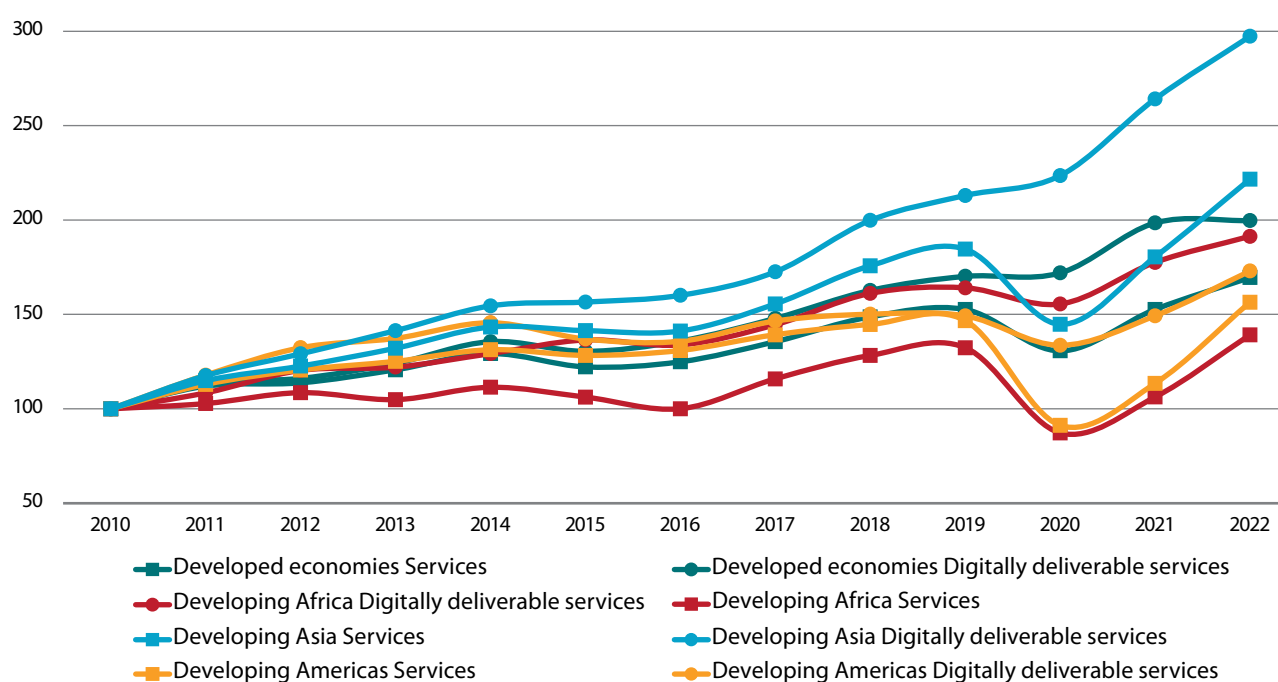
Thus far, it has largely been developed economies that have tapped the potential of digitally delivered services export markets. The proliferation of online streaming platforms, e-books and downloadable software make it significantly easier and less costly to deliver a wide range of products across borders. As a result, the international trade in goods such as books, that can be easily digitized, has stagnated

Figure III.D.5

Exports of services and selected groupings of services categories by level of development and region

Source: UNCTADstat.

Figure III.D.6

Evolution of exports of services and digitally deliverable services, by level of development and region, 2010–2022
(Index, 2010=100)

Source: UNCTADstat.

as digital distribution channels offer cost savings, immediate delivery and a broader reach. However, this is largely the case in developed countries, while digitizable goods imports continued to grow in many middle- and low-income economies.

Overall, the distribution of benefits of digital trade has thus been uneven, with countries with weak connections to networks particularly disadvantaged. Digitally delivered services play a smaller role in the commercial services exports of developing countries, with Africa and Latin America and the Caribbean furthest behind. LDCs and LLDCs still have a high untapped growth potential, including through e-commerce which has the potential to connect remote economies to global markets and create new sources of comparative advantage.⁵ However, a lack of access to 4G networks and high connectivity costs are among the factors hindering the growth of digital trade in LDCs and LLDCs, as well as a lack of digital policies due to the limited availability of data and insufficient international cooperation.

3. The multilateral trading system: Changing scope and geographies

3.1 Evolution in multilateral trade cooperation under the World Trade Organization

The World Trade Organization (WTO) has played a central role in facilitating multilateral trade cooperation since its establishment in 1995 and over a period of rapid trade expansion. The evolution of multilateral trade cooperation under the WTO reflects the changing dynamics of the global economy, shifts in geopolitical power, and the challenges associated with achieving consensus among a diverse group of member countries with varying economic interests. The future trajectory of the WTO and multilateral trade cooperation remains a subject of ongoing discussion and negotiation among its members.

The history of WTO negotiations can be delineated into distinct periods based on evolving issues, both before and after 2000. The Uruguay Round (1986–1994) marked the establishment of the WTO, replacing the GATT, and expanded the scope of trade negotiations to include services, intellectual property and agriculture. The WTO officially commenced on 1 January 1995, introducing a more comprehensive and binding framework for trade agreements and dispute resolution.

Subsequently, the Doha Development Agenda (launched in 2001) aimed to address development-related issues. However, economic shifts and divergent interests among members led to the stalling of several important elements in the negotiations—particularly in the areas of domestic support and tariff reduction in agriculture and non-agricultural market access—resulting in the round not being concluded as a single undertaking. Nevertheless, some important issues raised as part of the Doha Development Agenda have led to multilateral agreements, such as the issues of trade facilitation, export competition in agriculture including the prohibition of export subsidies, and, more recently, an agreement to reduce harmful fisheries subsidies.

In the absence of a comprehensive multilateral agreement on certain issues, countries turned to bilateral and regional trade

agreements and, in some cases, plurilateral negotiations, resulting in a complex web of overlapping arrangements. Challenges have also emerged regarding the WTO's dispute settlement mechanism, notably on the functioning and role of the WTO Appellate Body, which has led to the blockage of the appointment of new judges, hindering its ability to hear appeals. This has opened the door to situations where a party in a dispute may appeal the findings of a panel and prevent its adoption by the Dispute Settlement Body.

In addition, there has been an increase in scepticism regarding the benefits of trade. Protectionist sentiments have also risen, contributing to trade tensions and restrictions and challenging the multilateral landscape. Amid this, calls for WTO reform have surfaced with a focus on addressing issues like the dispute settlement mechanism, updating rules to reflect global economic changes and reinvigorating multilateral negotiating functions.

3.2 Regional trade agreements

The growth in the number of regional trade agreements continued into 2023, with 361 RTAs in force by the start of 2024. The number of RTAs has increased 56 per cent in the last 10 years alone. RTA activity is strongest in Europe with the European Union and the UK leading the number of RTAs in force in the region; East Asia and South America follow. However, as Figure 7 below shows, all regions in the world are actively involved in RTAs (see Figure III.D.7a). There is also an emerging trend suggesting some consolidation of existing RTA relationships (such as the CPTPP, RCEP, AfCFTA and the EAEU).⁶

Over the years RTAs have become more complex, including not just tariff liberalization but also commitments to liberalize trade in services and regulatory rules on other behind the border provisions. Around two-thirds of all RTAs notified to the WTO and currently in force include provisions on trade in goods and services. RTAs also tend to regulate other areas of trade to which WTO rules apply such as trade defence, safeguards, sanitary and phytosanitary measures and technical barriers to trade, intellectual property rights as well as services rules. They also increasingly extend their coverage to other behind the border measures not or only partially covered by WTO rules such as government procurement or competition. Most recently, the trend has been to include measures which are not covered by the WTO rules such as on the environment (59 per cent of RTAs notified have provisions on the environment), electronic commerce and labour (35 per cent and 34 per cent respectively of RTAs notified), small and medium sized enterprises (53 per cent of all RTAs notified), and gender (27 per cent of all RTAs notified), thus increasing the gap between trade regulations at the multilateral and regional levels (see Figure III.D.7).

There has been notable progress and renewed interest in deepening and reinvigorating South-South trade integration and cooperation frameworks. While some studies have pointed to highly heterogeneous trade and welfare outcomes within and across regions⁷, it is well recognized that South-South trade can have a positive effect in accelerating economic diversification and complementarities. Indeed, south-south trade can foster trade in non-traditional exports, such as higher value-added and technology-intensive manufactured goods. In Africa, the African Continental Free Trade Area, the Phase II Protocols

Figure III.D.7a

RTAs in force, by region

(Number of agreements)

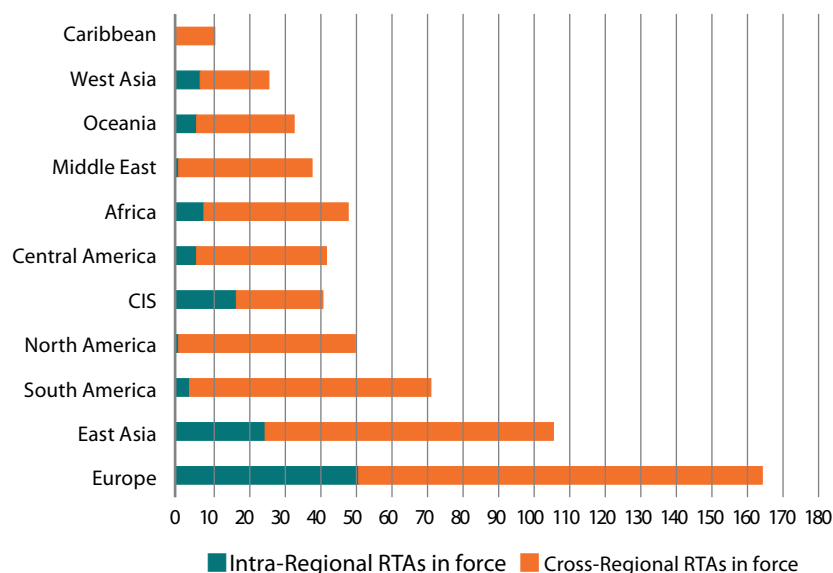
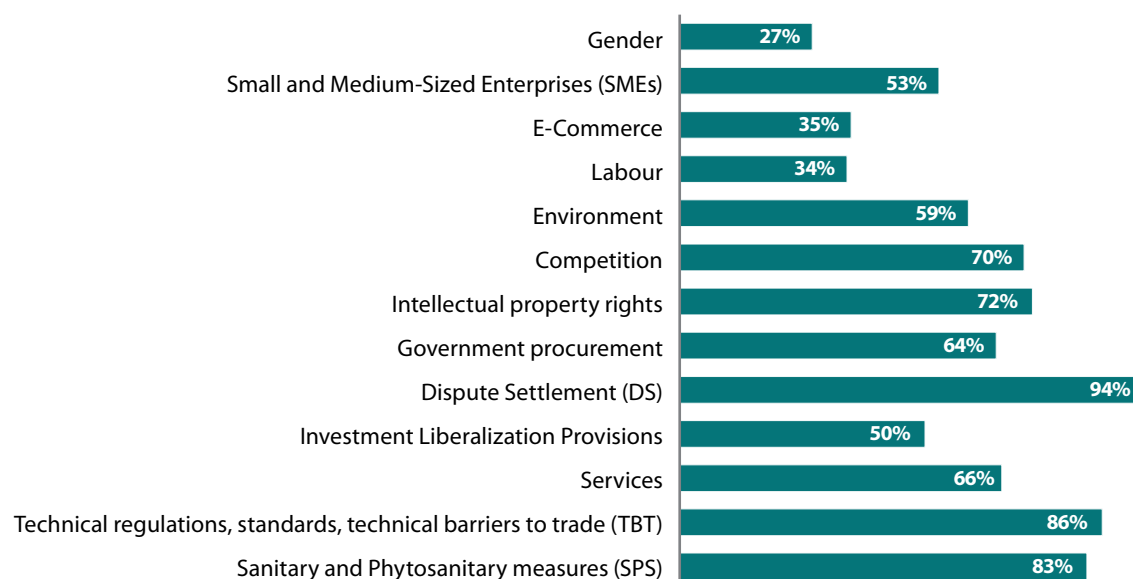
**Source:** WTO Secretariat.**Note:** RTAs involving countries/territories in two (or more) regions are counted more than once.

Figure III.D.7b

Key provisions in RTAs

(Percentage)

**Source:** WTO Secretariat.**Note:** Figures are based on 347 RTAs (out of 364) notified to the WTO and currently in force. For more details on these provisions: <http://rtais.wto.org/>.

on Investment, Competition and Intellectual Property Rights as well as Digital Trade have been concluded and approved. At the inter-regional level, members of the Global System of Trade Preferences (GSTP) seeks to further deepen South-South cooperation and trade by reducing trade barriers, with a view to addressing the most pressing challenges – such as the climate crisis or food security.

3.3 Emerging trends in regional cooperation

New trade initiatives are putting regulatory and economic cooperation to promote supply chain agility and resilience at the center of discussions. One major initiative launched in May 2022 by the United States is the Indo-Pacific Economic Framework for Prosperity (IPEF).ⁱⁱ The IPEF partners represent 40 per cent of global GDP and 28 per cent of global goods and services trade. As distinct from traditional trade liberalizing arrangements, this framework aims at enhancing resilience, sustainability, inclusiveness and competitiveness by lowering the risk of disruptions through enhanced supply chain resilience, seeking strong labour and environmental standards, as well as effective tax cooperation in accordance with UN standards.

In the context of the energy transition, there is a rising demand for critical minerals in sectors such as aerospace, automotive, renewable energy and telecommunications. They also are crucial components of low-carbon technologies such as batteries, wind turbines, electric vehicles and solar panels. With the majority of world supply concentrated in a handful of countries, there has been an increase in bilateral agreements to build supply-chain resilience and to ‘de-risk’ supply. These new partnerships on critical minerals seek to promote trade and investment opportunities, as well as research and development, including information sharing and collaboration through joint initiatives.

Another emerging trend relates to the emergence of digital economy agreements (DEAs). Unlike traditional trade agreements, DEAs focus on domestic regulatory reforms and cross-border collaboration in areas including data innovation, digital identities, cybersecurity, consumer protection and digital inclusion. New Zealand, Chile and Singapore signed the world’s first Digital Economy Partnership Agreement in June 2020. This agreement seeks to establish global standards for, and aims to benefit from the potential of, the digital economy. DEAs have inspired other trade arrangements, such as for the Association of Southeast Asian Nations (ASEAN), which is considering negotiating a regional DEA, the Digital Economy Framework Agreement.

International investment agreements

Policymaking in the space of IIAs has been a highly dynamic space, which has seen significant change over the past 20 years. As the stock of IIAs that are signed and in force has declined markedly from levels in the 1990s and 2000s (figure III.D.8), the focus of policy has shifted towards a new generation of IIAs. Modern agreements now often include a sustainable development orientation, a focus on preservation of regulatory space and improvements to or omissions of investment dispute settlements.

In 2022, investment treaty terminations again exceeded the number of new treaties. Countries concluded at least 15 new IIAs in

2022: 10 bilateral investment treaties and five treaties with investment provisions. At the same time, at least 58 IIAs were effectively terminated. By the end of 2022, there were a total of 3,265 IIAs of which 2,584 are in force (figure III.D.8). The total number of effective terminations reached at least 569, with about 70 per cent of IIAs terminated in the last decade.

New-generation IIAs exist in parallel with older IIAs. Recent IIAs signed between 2020 and 2023 feature many reformed provisions aimed at safeguarding the right of States to regulate and reform investor–State dispute settlement (ISDS). It remains to be seen whether the reformed provisions are sufficiently robust to support and not hinder countries’ sustainable development endeavours. Moreover, most new IIAs lack provisions that proactively promote and facilitate sustainable investment and only a minority of them include investor obligations. Many new-generation IIAs overlap with an earlier IIA between the same economies, highlighting the importance of expediting the modernization and consolidation of the existing stock of treaties through amendment, replacement or termination.

New types of investment-related agreements which contain proactive investment facilitation features and pay greater attention to sustainable investment are an emerging trend. In 2022, negotiations were concluded on several investment governance instruments of this type, notably the Investment Protocol to the African Continental Free Trade Area and the Angola–EU Sustainable Investment Facilitation.

Most new investment arbitration cases continue to be brought under old-generation IIAs. In 2022, claimants filed 46 new ISDS cases under IIAs. About 80 per cent of ISDS cases initiated in 2022 were based on bilateral investment treaties and treaties with investment provisions signed in the 1990s or earlier. To date, 132 countries and one economic grouping are known to have been respondents to one or more ISDS claims. As of 1 January 2023, the total number of publicly known ISDS claims had reached 1,257 (figure III.D.9). As some arbitrations can be kept confidential, the actual number of disputes is likely higher.

Old-generation treaties continue to dominate the IIA landscape. About 2,300 old-generation IIAs are still in force. The continued prevalence of old-generation IIAs entails risks for climate action, energy transition and other sustainability objectives. This challenge is compounded by the rising number of ISDS cases related to the fossil fuel and renewable energy sectors that are brought based on IIAs. Investors in these sectors have been frequent claimants, together accounting for about 25 per cent of all ISDS cases. In the fossil fuel sector, investors have initiated at least 219 cases against different types of State conduct. In the renewable energy sector, the last decade has also seen the emergence and proliferation of ISDS cases, with 119 known cases. Many of these cases challenged legislative changes involving reductions in feed-in tariffs for renewable energy production.

4. Trade and sustainable development in a complex global landscape

4.1 Economic development and trade

The links between trade and economic development are a perennial feature of debate. An extensive empirical literature on the relationship between trade and growth generally finds a positive

ⁱⁱ Includes Australia, Brunei Darussalam, Fiji, India, Indonesia, Japan, Republic of Korea, Malaysia, New Zealand, Philippines, Singapore, Thailand and Viet Nam.

Figure III.D.8

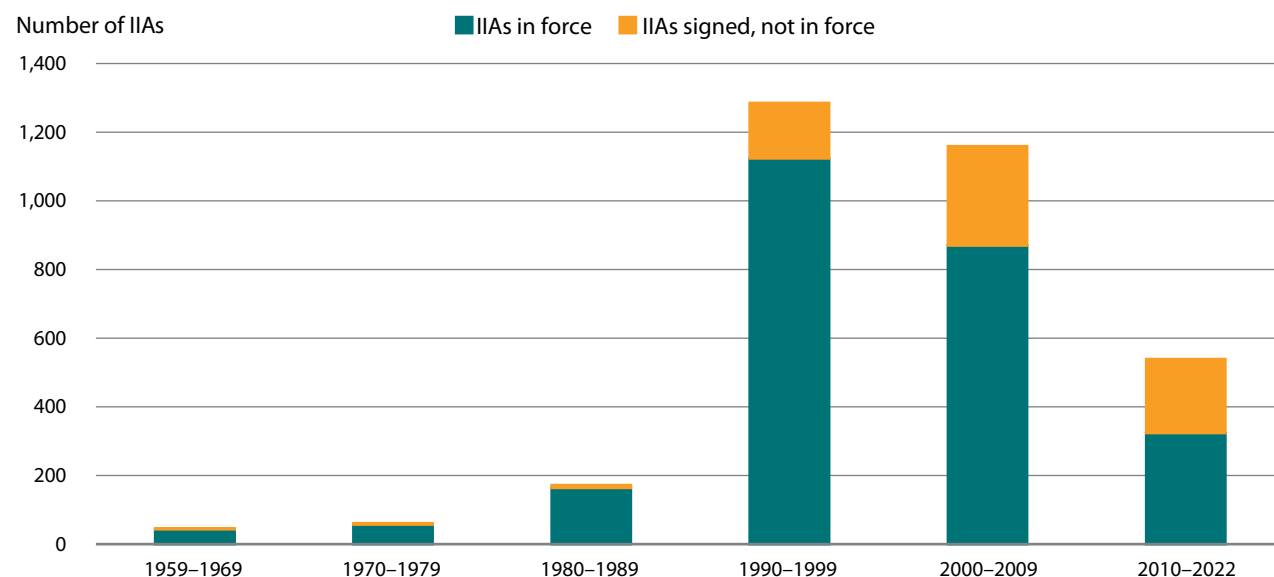
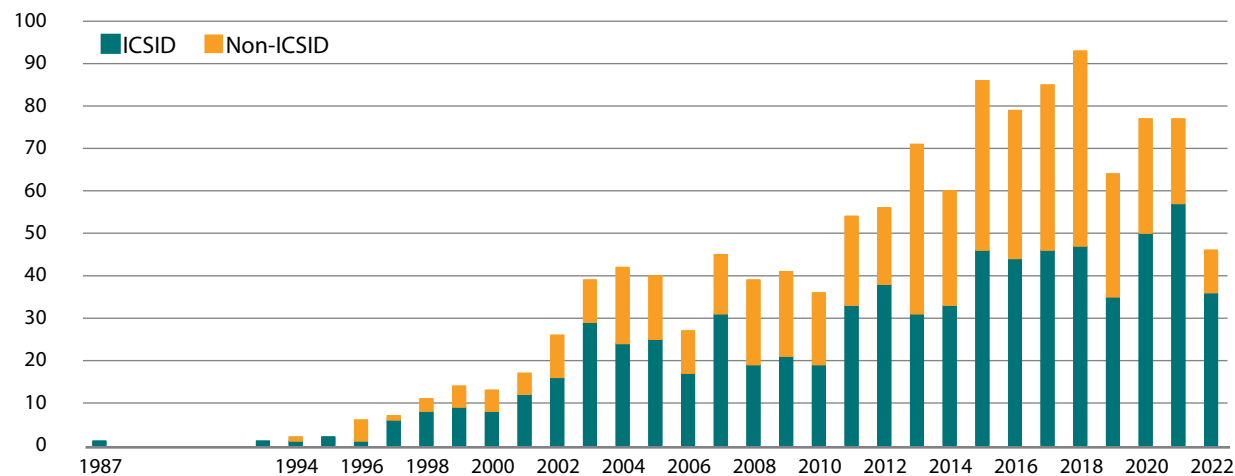
Stock of IIAs signed and in force, 1959–2022*(By date of signature)***Source:** UNCTAD, IIA Navigator.**Note:** The figure does not include IIAs that were effectively terminated.

Figure III.D.9

Trends in known treaty-based ISDS cases, 1987–2022

Annual number of cases

**Source:** UNCTAD, ISDS Navigator.

Note: Information has been compiled from public sources, including specialized reporting services. UNCTAD's statistics do not cover investor–State cases that are based exclusively on investment contracts (State contracts) or national investment laws, or cases in which a party has signalled its intention to submit a claim to ISDS but has not commenced the arbitration. Annual and cumulative case numbers are continually adjusted as a result of verification processes and may not match exactly case numbers reported in previous years.

Box III.D.1**UNCTAD IIA toolbox for the promotion of sustainable energy investment**

Various options exist to transform IIAs into tools that are conducive to sustainable energy investment and climate objectives. The new UNCTAD tool box presented in the World Investment Report 2023 focuses on four areas (table III.D.1): the promotion and facilitation of investment, technology transfer, the right to regulate, and corporate social responsibility. Renegotiation, amendment and termination of the large stock of old-generation IIAs are the main options to ensure that the international investment regime contributes to – and does not hinder – sustainable development.

Table III.D.1**IIA reform toolbox: Promoting sustainable energy for all****Promotion and facilitation of sustainable energy investment**

Incorporate IIA provisions aimed at actively promoting and facilitating sustainable energy investment.

Provide for preferential treatment of sustainable energy investment.

Establish institutional mechanisms for cooperation on R&D of sustainable technologies.

Commit to technical assistance on the adoption of investment facilitation measures for sustainable energy.

Technology transfer and diffusion

Encourage the technology transfer of low-carbon and sustainable technologies, including related know-how.

Make efforts to create an enabling environment for receiving technology.

Allow certain kinds of performance requirements relevant to the energy transition.

Ensure that the protection of intellectual property rights does not unduly impede the diffusion of technology.

Right to regulate for climate action and the energy transition

Refine the content of investment protection standards and reform ISDS with regard to energy investments.

Acknowledge the need for regulatory flexibility.

Include general exceptions related to climate change and the energy transition.

Clarify provisions on compensation and damages.

Corporate social responsibility

Include binding obligations relating to corporate social responsibility.

Specifically oblige energy investors to comply with requirements for sustainable investment (e.g., by requiring environmental impact assessments and maintenance of an environmental management system).

Source: UNCTAD. *World Investment Report 2023* (Overview).

statistical association between the two; in the first decade of this millennium rapid trade growth indeed went hand in hand with a dynamic world economy. However, the strength, nature and even direction of this relationship as well as the broader economic consequences of increased trade flows and accompanying trade policies, continue to be contested.⁸

An additional element of complexity is provided by the restructuring of the global economy around GVCs in recent decades.

Participation in GVCs is often seen as an attainable first step on the industrialization ladder and to offer a more productive integration into the global trading system. Rather than having to develop an entire product or break into an extremely competitive market on their own, countries can specialize in specific tasks or components of a multitude of value chains, starting at the relatively accessible bottom, leveraging the advantage of lower labour costs and steadily building up capacity in more skill-intensive and higher value added activities.

However, the association between participation in GVCs and development is not straightforward but rather context-specific.

Studies⁹ have shown that when increases in the foreign value added of exports occur in a larger context of greater production and exports of manufactures (figure III.D.10), GVC participation can complement industrialization and structural change. However, when increasing participation in GVCs reflects a reduction of domestic sourcing in a context of weak manufacturing export performance, participation in GVCs may even delay structural transformation, as in the case of many developing economies in Africa and Latin America. As shown in figure III.D.10, developing economies

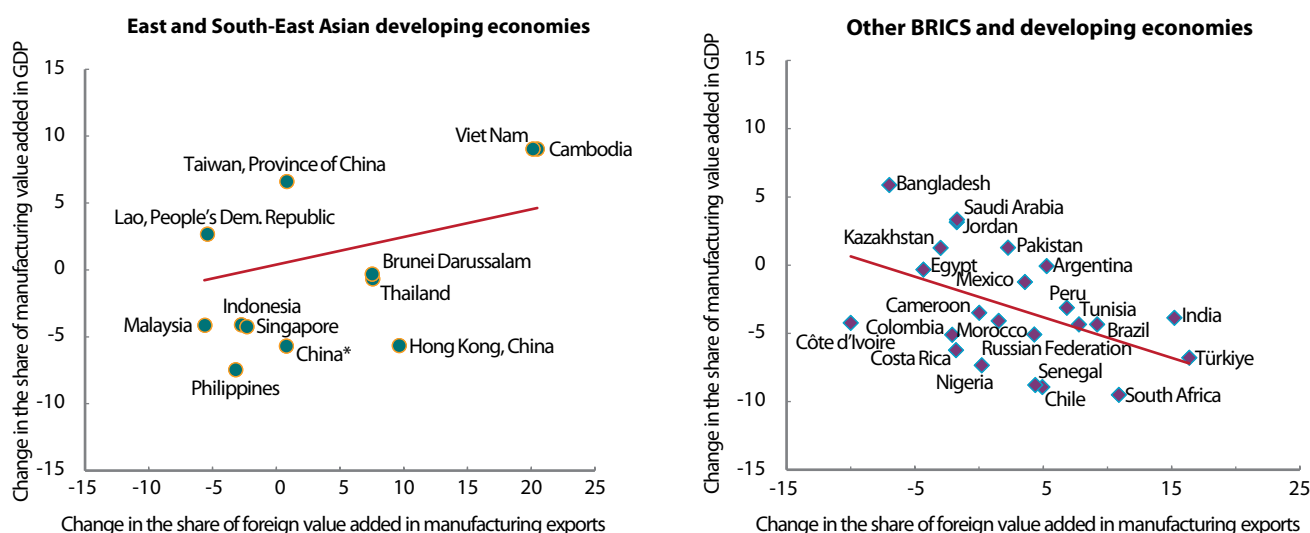
in East and Southeast Asia show a clear and strong positive association between GVC participation and industrialization, while other BRICS (Brazil, Russia, India, China and South Africa) and developing countries in other regions show the opposite relationship.

Indeed, GVCs lower barriers to entry at the bottom of the value chain, making it easier than in the past for developing countries to break into global exports of manufactures, but the conditions that enable access can also act as barriers to upgrading, since more accessible parts of the value chain are associated with few forward and backward linkages, limited institutional development and little possibility for knowledge externalities in the wider economy. Technological upgrading can be more difficult for economies that are used by transnational corporations primarily as bases for exports to third markets than for economies where foreign direct investment (FDI) is characterised by market-seeking and tariff-jumping behaviour. Developing economies with limited productive capacities can therefore remain trapped in and competing for the lowest value-adding activities at the bottom of value chains, which can ultimately result in “thin industrialization” and slow economic growth. These activities are also detrimental from a dynamic perspective since they do not generate those local productive capacities which are essential to meaningful development.¹⁰

Participation in GVCs also carries the additional risk of specialization in just a very narrow range of production activities with a concomitantly narrow technological base and overdependence on transnational corporations for access to GVCs. Such shallow

Figure III.D.10

Changes in the shares of foreign valued added in manufacturing exports and of manufacturing value added in GDP, selected economies, 1995–2020
(Percentage points)



Source: UNCTAD based on OECD-WTO TIVA database and UNSD Main Statistical Aggregates database.

Note: Shares taken in current values.

* Share of manufacturing value added in GDP for China is 1999–2020 percentage point changes.

integration manifests itself in asymmetric power relations between lead firms and suppliers and in weak bargaining positions for developing countries. For example, the experiences of Mexico and Central American countries as assembly manufacturers have been linked to the creation of an enclave economy, with few domestic linkages. Nonetheless, studies have also shown the potential benefits of supplier-buyer links between local firms and multinational enterprises in developing countries.¹¹ Meanwhile, countries able to develop productive capacities in sync with those needed by international production networks and position themselves at a relatively high level in the world distribution of tasks, are well placed to sustain a more inclusive growth process. The selection of the relevant sectors and industries for industrial policy support is critical in this respect and varies from country to country according to their pre-existing areas of strengths, potential for upgrading and dynamic comparative advantage.

What is increasingly clear is that a reversal of trade integration and deceleration of growth in trade is a threat to prosperity and economic growth for developing and developed countries alike.

Recent shocks, including the 2008 world financial and economic crisis, the COVID-19 pandemic and the war in Ukraine, have underscored countries' reliance on each other for critical supplies and revealed common vulnerabilities to external disruptions and geopolitical conflicts.

A process of de-globalization and a focus on self-sufficiency would significantly weaken the global economy and make it less efficient and less innovative, limiting the ability of countries—particularly developing countries—to achieve economic growth. Fragmenting the world trading system into separate blocs, as estimated by the WTO, could cost about 5 per cent of global real income, with developing economies facing double-digit losses.¹²

Instead, trade integration has to go hand in hand with international cooperation. Recognizing that global problems require global solutions, international cooperation would support the reinvestment in the multilateral trading system to ensure that the principles of secure, inclusive and sustainable trade are respected. This involves the active participation of economies that have yet to fully integrate into the world trading system, ensuring that more firms and workers, including women and those from low-income households, can actively engage in and benefit from trade. Measures beyond international trade cooperation, such as international collaboration in taxation and competition, support programmes and domestic policies, are also considered to enhance inclusivity. The overall aim is thus to reduce inequalities through a predictable trading environment, support global economic convergence, foster services-led development, establish e-commerce rules for inclusive globalization, provide investment facilitation for inclusive GVCs, strengthen the role of international organizations as well as complement multilateralism with deeper regional integration.

4.2 Environmental impact of trade

Although trade can aggravate environmental problems by increasing the scale of transportation and production, trade can also lead to positive environmental outcomes by affecting the composition of goods and services traded, and by helping to develop, deploy and diffuse environmental technologies.¹³ Trade-induced innovation and investment in green technologies result from expanded market access, encouraging cleaner production processes and pollution abatement.¹⁴ In addition, trade plays a role in reducing pollution intensity, as less pollution-intensive exporters gain market share and invest more in pollution abatement.¹⁵ Studies have also shown that the inclusion of

Environmental Related Provisions linked to the agriculture, fisheries and forestry sectors in RTAs, which have increased significantly over the past 20 years, can help to mitigate the environmental impacts of trade-induced production growth. There is evidence of reductions in agriculture-related greenhouse gas emissions in countries that have RTAs with more agriculture, fisheries and forestry sectors.¹⁶

In order to study the link between trade and climate change, trade economists have developed a three-effect conceptual framework, which highlights a scale effect, a composition effect and a technique effect. The scale effect assesses how increased economic activity resulting from the opening of trade may contribute to higher greenhouse gas emissions. The composition effect focuses on changes in the relative sizes of various production sectors within a country due to trade opening and shifts in relative prices. The environmental impact depends on the growth or reduction of emissions-intensive sectors. The technique effect focuses on improving production methods to reduce greenhouse gas emissions, facilitated by open trade. Access to and the lower costs of climate-friendly goods and services can contribute to emissions reduction and is particularly beneficial for countries lacking such resources.

Trade policies, particularly those pursued through increased global integration and cooperation of the multilateral trading system, can help to protect the environment in several ways.

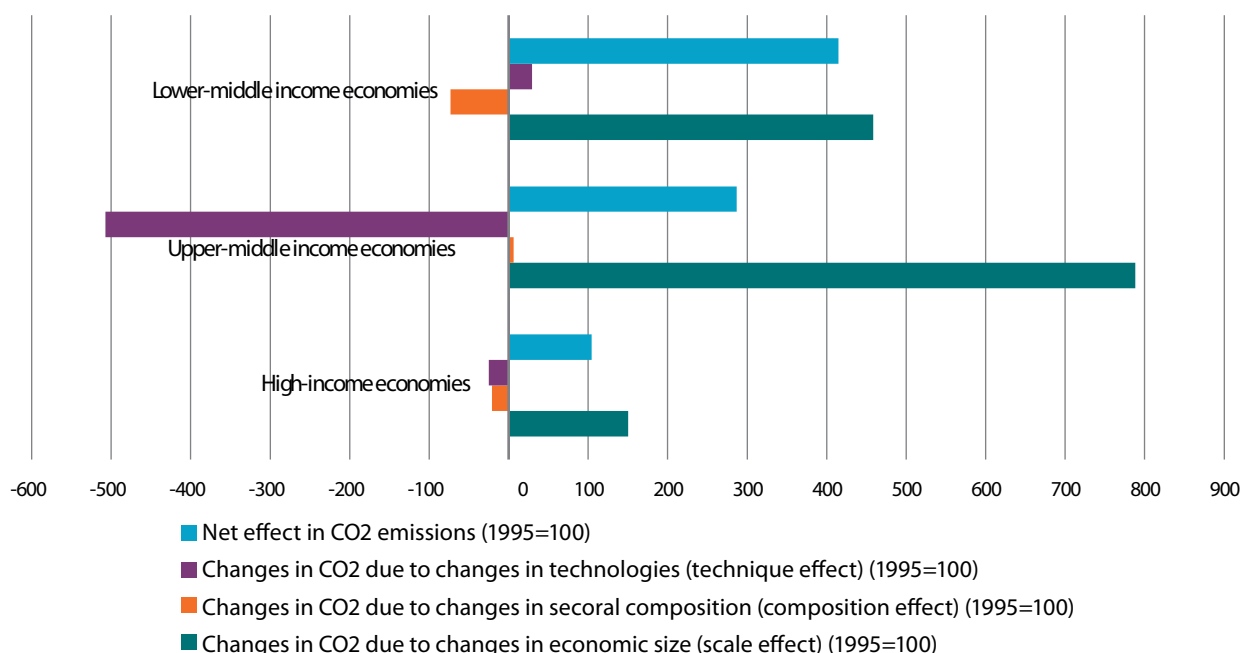
Firstly, the increasing share of digital and services trade holds promise for reducing the environmental impact of trade. Digitally deliverable services, including information technology, finance, business services and entertainment, exhibit lower carbon emissions intensity compared to other sectors (figure III.D.12). WTO projections for a future scenario with increased international cooperation on global trade policy suggest that trade in services,

particularly digitally delivered services, could exceed 30 per cent by 2040, resulting in a less carbon-intensive trade composition. Additionally, digital technologies, enabling remote trade and reducing the need for physical transportation, have the potential to decrease carbon emissions linked to international transport. Overall, digital solutions could contribute to a 15 per cent reduction in global carbon emissions.¹⁷

Overall, an integrated approach to trade and environmental policies is integral to addressing global environmental challenges like climate change, pollution and biodiversity loss due to the trans-boundary nature of environmental issues. Studies suggest that the potential benefits of such coordination, including a global carbon dioxide market, could result in gains of up to \$106 billion by 2030.¹⁸ Coordinated climate policies, such as carbon pricing mechanisms, could help to reduce greenhouse gas emissions by reflecting the social costs of carbon emissions, thereby shifting consumption and production away from carbon-intensive activities. Complementary policies should be envisaged to promote behavioural changes and counter the negative effects of carbon pricing on the poorest households and on developing countries, for example through mobilization of climate finance funds for less advanced economies. Policy coordination is essential for fostering green innovation, expediting the transition to cleaner technologies, and addressing negative externalities, particularly the implicit subsidy for carbon dioxide emissions associated with traded goods. Multilateral efforts, including eliminating tariff escalation and addressing trade policy biases, are pivotal for advancing global environmental sustainability.

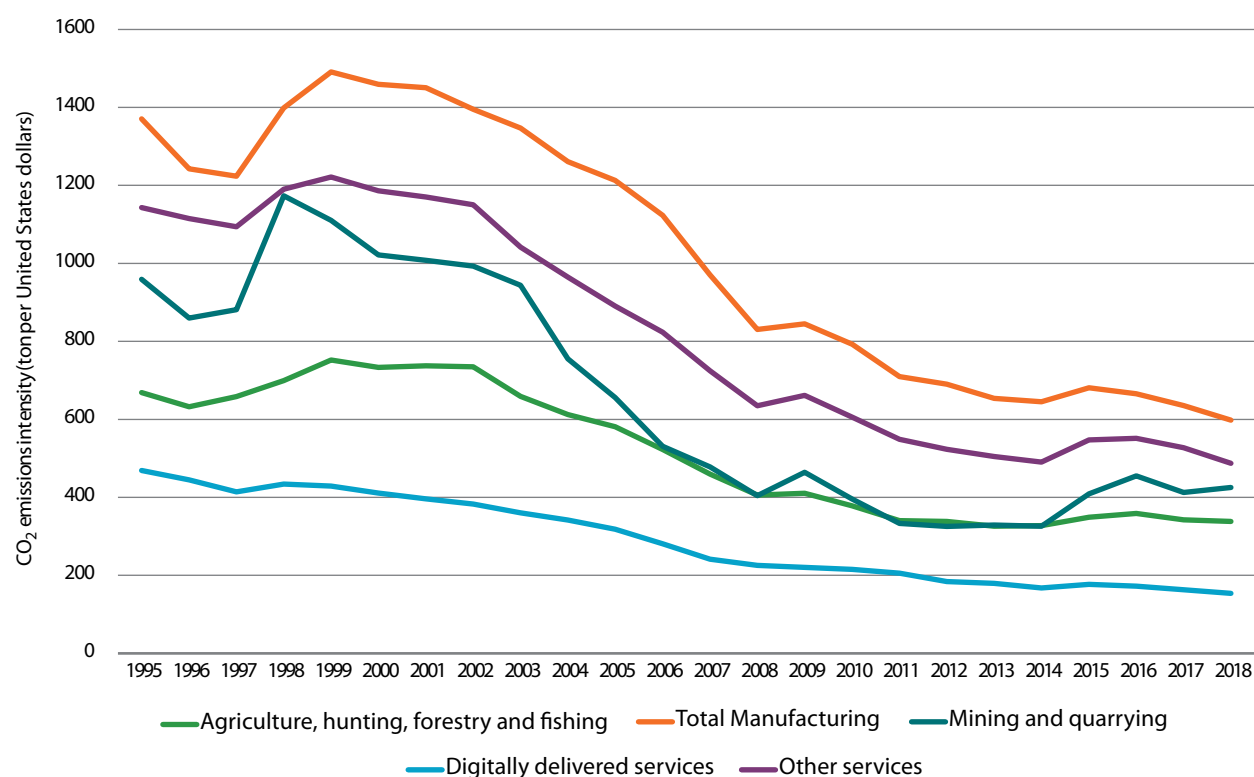
Further equitable integration into the multilateral trading system can also help developing economies to transition to a more sustainable growth path, while respecting their need for

Figure III.D.11
Technology and CO₂ emissions, 1995–2018



Source: 2023 WTO Trade Report.

Figure III.D.12

Carbon emissions intensity for digitally delivered services is relatively low*(CO₂ emissions intensity, ton per United States dollars)*

Source: 2023 WTO World Trade Report.

economic development. New trading avenues are opening in renewable energy, particularly benefiting developing economies in Africa and the Middle East with abundant solar resources. To fully exploit the potential of renewable energy, access to technology through trade and technology transfer is essential. WTO simulations indicate that decarbonization could reshape energy exports, with developing economies potentially specializing in renewable energy. Additionally, there are opportunities for developing economies in the green transition through specializing in the raw materials that are crucial for this transformation, requiring sustainable practices and adherence to environmental regulations. Sustainable agriculture trade offers export opportunities, catering to global demands for environmentally and socially responsible products.

There is also an important role for trade-adjacent government policies in promoting climate action. Environmental tax and pricing systems such as carbon taxes and “cap-and-trade” mechanisms are effective policy tools to internalize the social cost of pollution emissions. These approaches aim to reduce the demand for carbon-intensive products, redirecting investments towards cleaner technologies and generating fiscal revenues for governments. A well-designed carbon pricing policy requires complementary measures to address differences in development status, distributional concerns and other market failures associated with the transition to a low-carbon economy. The global implementation of carbon pricing initiatives has seen over 70 policies

covering 23 per cent of global emissions, with varying pricing levels ranging from over \$140 per tonne of carbon dioxide emissions to less than \$1 per tonne.¹⁹

The lack of coordination in environmental policies such as carbon pricing and subsidies can lead to costlier and less effective measures, including spillovers on trading partners. Uncoordinated environmental pricing schemes result in a patchwork of diverse regimes with varying levels of ambition, potentially hindering a cohesive response to global environmental challenges. Uncoordinated environmental policies can also have spillover impacts on trading partners, leading to rising trade concerns associated with environmental measures, particularly technical regulations and border carbon adjustment mechanisms. **Efforts to harmonize standards and mutual recognition within RTAs are crucial to preventing policy fragmentation and enhancing the effectiveness of environmental policies.** Unilateral environmental policies that negatively impact trading partners could lead to retaliatory measures and trade conflicts and undermine the effectiveness of environmental policies. This lack of coordination poses systemic risks, setting a precedent for disregarding global trade rules and hindering international cooperation in addressing environmental challenges. Improved and transparent multilateral trading rules are essential to maximize positive spillovers and prevent negative consequences from environmental policies.

4.3 Social impacts of trade

4.3.1 Inequality and trade

Rising inequality in a number of countries is frequently ascribed to trade liberalization. Inequality is a product of an intricate interplay among economic, social and political factors, with trade representing only one determinant. Trade has played a dual role: while it has contributed to reducing inequality among nations, it has fueled inequality within countries.²⁰ The reduction of inequality among countries is due to the rise in per capita incomes, spurred by the opportunities presented by global markets, yet the benefits have not been universally shared. The exports of LDCs and LLDCs, for instance, remain concentrated on commodities and low value added goods, with no positive effect on employment and wages.

Research suggests that the middle classes in developed countries have benefited the least from economic growth that took place between 1980 and 2020. As shown in figure III.D.13, the two groups that have benefited the most from the cumulative income growth in the period between 1980 and 2020 are the emerging middle classes in developing countries, notably China, and the top 1 per cent. The global 1 per cent at the top of income distribution experienced substantial income growth over this time frame, absorbing 23 per cent of global growth.²¹ Since the 2008 world financial and economic crisis this trend has levelled off, as there has been higher growth among the bottom 50 per cent and lower growth at the very top.²²

The relationship depicted in figure III.D.13, sometimes referred to as the Elephant curve, has been closely associated with an era of unprecedented trade acceleration and openness, particularly in the 1990s and early 2000s. Trade openness has influenced inequality through diverse channels, including wages, market concentration and geographic concentration. The fragmentation of production across countries tends to exacerbate wage disparities in both developed and developing economies. Market concentration, influenced by international trade as well as regulation,²³ has fostered the dominance of large multinational

enterprises, which leads to higher inequality because it disadvantages smaller firms and diminishes consumer leverage. Further increases in the market power of already-powerful firms could contribute to additional reductions in labour income shares.²⁴ Furthermore, international trade has amplified spatial disparities by concentrating in some areas and diminishing prospects elsewhere, for example in rural areas or regions producing import competing goods. Yet, trade is not the only driver of these trends, with research pointing to skill-biased technological change acting as a major driver of inequality.

Equalizing opportunities for people requires policies that promote the inclusion of disadvantaged groups, addressing the distributional effects of trade transmitted through channels such as employment and wages, consumption and the public provision of goods and services. For instance, the inclusion of labour rights in trade agreements could help to extend the benefits of trade to workers in developing countries. Policy recommendations are also available for making trade beneficial for specific groups. For example, in regard to persons with disabilities, studies show the benefits of aligning trade rules with the rights of persons with disabilities, involving them actively in trade policy design and implementation, promoting targeted jobs and facilitating the movement of assistive technologies across borders.

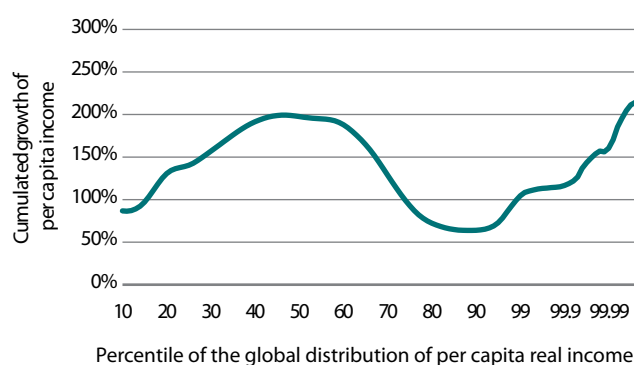
Ensuring equal opportunities for firms, particularly small- and medium-sized enterprises (SMEs), involves interventions that reduce trade costs and ease market access, for example by eliminating non-tariff barriers, promoting online trade and removing barriers to services trade. In the agrifood sector, integrating smallholder farmers, who are largely marginalized within GVCs, into markets requires policies that will promote improved rural infrastructure and services.²⁵ Effective competition laws especially for e-commerce are also imperative to mitigate the excessive power of large corporations, providing SMEs with a more level playing field.

Reducing inequality must be complemented by domestic policies aimed at improving productivity, mitigating adjustment frictions and compensating for losses. Governments should ensure that education and training opportunities are universally available, including to disadvantaged households, and that efficient safety nets cover those adversely affected by globalization, thus fostering equality of opportunity and social mobility. With regard to the private sector, policies promoting affordable financing and access to market information and export promotion activities tailored to SMEs can facilitate their participation in the global market, either through exports or engagement in GVCs.

4.3.2 Gender-responsive trade policies

Making trade policies more responsive to gender issues improves gender equality in trade, supports poverty reduction and fosters sustainable growth. Recent World Bank analysis reveals that closing gender employment gaps could raise per capita GDP by almost 20 per cent, reaching 40 to 80 per cent in the Middle East, North Africa and South Asia. Despite trade being a crucial source of economic opportunity for women, disparities persist, with male entrepreneurs nearly twice as likely to internationalize their businesses as female entrepreneurs. Recognizing these gaps, WTO members have increasingly incorporated gender issues into trade policies, with the creation of the Gender Research Hub in 2021, fostering a global network contributing significantly to research on women's economic empowerment in just two years.²⁶

Figure III.D.13
Cumulated growth in per capita income across the global population: Elephant curve, 1980–2020
(Percentage)



Source: Chancel, L., Piketty, T., Saez, E., Zucman, G. et al. World Inequality Report 2022, World Inequality Lab wir2022.wid.world

Female labour-intensive sectors face higher tariffs and greater trade costs while there is higher services trade restrictiveness in these sectors. Furthermore, there are elevated trade costs related to face-to-face interaction in female labour-intensive industries. Studies suggest that the most effective policy solution to address this is through digitalization policies, which can substantially reduce the male wage premium by almost 1 per cent, as well as services trade liberalization, which could have a modest impact.

Box III.D.2

The gender dimension of e-commerce

E-commerce promotes women's economic empowerment through several benefits that support business growth and diversification. E-commerce helps small businesses, in which women tend to be concentrated, increase customer numbers by making it possible to reach distant markets. E-commerce platforms lower barriers to market entry by providing an ecosystem of services, including marketing tools, payment services and logistics, that companies would otherwise need to outsource. Online platforms also provide information on market access, customs procedures, shipping costs, market intelligence and data that is especially important for women entrepreneurs. A lack of such information is a persistent obstacle that women face in offline trade. Online trade provides both more time flexibility compared to offline trade and the ability to work from home. This is particularly valuable for women who shoulder the burden of unpaid domestic and care work. This also helps women to overcome mobility constraints and reduce gender-based discrimination and violence.

There are also challenges for women-owned enterprises to reap the full benefits of e-commerce. Digital gender divides (figure III.D.14) in developing countries and LDCs put women entrepreneurs at a disadvantage while seeking to benefit from e-commerce.

Women entrepreneurs face obstacles such as limited business networks, lower levels of entrepreneurial skills, negative gender stereotypes and time poverty. They also face gender-based violence and harassment, common to both online and offline trade, in accessing the opportunities provided by e-commerce. These are a combination of pre-existing gender gaps compounded by gender digital divides in relation to access to technology and the Internet, education and digital skills, and insufficient capital and finance, resulting in the low profitability of operating in low value added sectors.

There are also policy-related constraints that undermine the potential benefits of e-commerce for women entrepreneurs. Several countries, particularly developing ones, still lack data on how women businesses contribute to economic growth through e-commerce. Lack of data also undermines efforts to understand and address the specific obstacles that women entrepreneurs face in this area and negatively affects the design of sound policies. Most developing countries have not yet put in place comprehensive national digitalization strategies; in those countries that have developed them, gender considerations have rarely been mainstreamed.

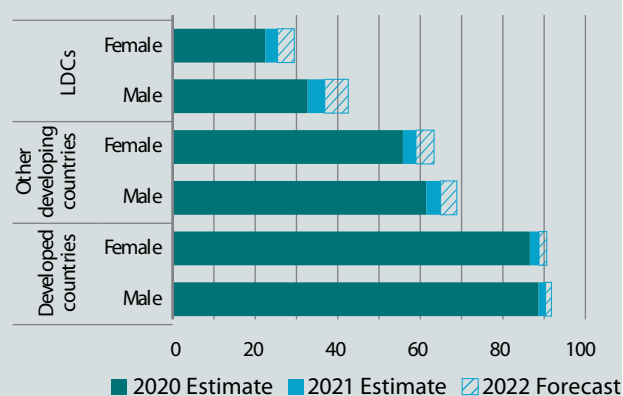
5. Trade and development financing

5.1 Trade finance: Trade finance gaps and instruments

Trade finance plays a crucial role in facilitating international trade, offering a low-risk mechanism where the shipped goods serve as collateral. The WTO estimates that 80 per cent or more of global merchandise trade depends on the provision of trade financing.²⁷ Despite

Several positive initiatives have been taken to lower the constraints faced by women entrepreneurs, as reviewed by UNCTAD. For example, Jumia—a major online marketplace in Africa—developed its Women and Youth Empowerment Program to help women and youth build a local e-commerce market. WEConnect International brings large corporate, multilateral and government buyers together with women-owned suppliers around the world. UN Women has set up a digital platform—Buy from Women—that connects smallholder farmers (men and women) to agricultural supply chains. Development partners are also active in this field. Among the many examples, UNCTAD eTrade for Women provides masterclasses that equip women entrepreneurs from developing countries with the skills necessary to operate in the digital landscape. From the policy angle UNCTAD, through its online course on e-commerce from a gender and development perspective, supports policymakers to better understand the opportunities that e-commerce provides to women entrepreneurs, but also the challenges they face, and offers policy recommendations on how to leverage e-commerce for economic growth and women's empowerment.

Figure III.D.14
Percentage of female and male populations using the Internet
(Percentage)



Source: UNCTAD calculation based on ITU (2022); Estimates for 2020 and 2021, forecasts for 2022.

Note: Internet users are individuals who have used the Internet (from any location) in the last three months. The Internet can be used via a computer, mobile phone, personal digital assistant, games machine, digital TV, etc.

its importance, businesses in many developing countries encounter significant hurdles in obtaining trade finance, often due to exaggerated country risk perceptions. The inability to access trade finance not only hampers trading opportunities but also prevents companies from capitalizing on international markets for which they are otherwise well prepared.

The global trade financing gap has increased sharply in recent years. The Asian Development Bank has estimated that global unmet demand for trade financing has increased to US\$2.5 trillion annually, from initial estimates eight years ago of US\$1.5 trillion per year.²⁸ Moreover, current trade finance disproportionately favours established commodity exporters and bulk importers. SMEs on the other hand, especially those led by women, struggle with rejection rates exceeding 50 per cent. Many traders refrain from seeking trade finance in the first place due to high costs, collateral requirements and potential rejection risks. In West Africa, for instance, only 25 per cent of the trade in goods is covered by trade finance. Increasing this coverage to the continental average of 40 per cent could boost West Africa's annual trade flows by 8 per cent.²⁹

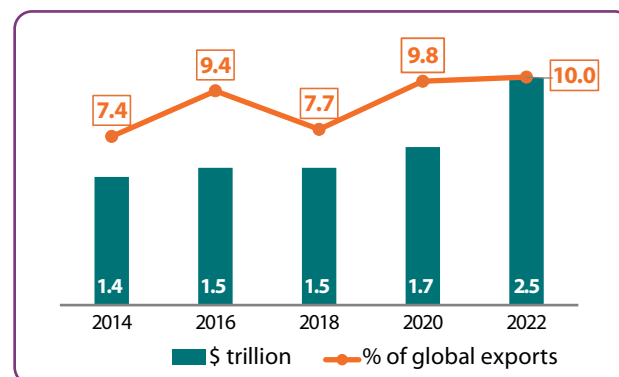
Trade finance serves as a crucial enabler for the dissemination of climate-related technologies and equipment. A deficiency in trade finance flows may result in delays or cancellations of significant climate-related initiatives. While data on the trade finance gap specifically for climate-related goods is limited, addressing this gap is essential to boost trade in products vital for transitioning to a low-carbon economy. The intersection of climate finance and aid for trade financing, particularly in renewable energy infrastructure, underscores the catalytic role of aid for trade and key stakeholders in mobilizing finance for green projects. Additionally, technical assistance from development agencies can focus on trade finance facilitation programmes for developing economies, strengthening their financial institutions in this domain. This is particularly true for SMEs which require support in the form of climate strategy building, for instance through the International Trade Center's Green Performance Toolkit, an online solution designed to enhance the environmental performance of small businesses.

The provision of traditional trade finance has long been the purview of large international banks, yet private banks are not well positioned to narrow the trade finance gap for underserved

Figure III.D.15

Global trade finance gap

(United States dollars, percentage of global exports)



Source: ADB, "2023 Trade Finance Gaps, Growth and Jobs Survey" and WTO data.

firms, creating a key role for public actors. Firms in developing and emerging markets and SME suppliers face the greatest challenges in accessing trade financing. These constituencies are most likely to be reached by institutions whose mandates are at least partly defined on the basis of policy or the public good. These include some export credit agencies and MDBs, which already play an important role in the provision of supply chain financing in developing countries. MDBs are also uniquely positioned to respond to crisis situations such as trade and supply chain disruptions related to COVID-19. To further strengthen their role, there are several cross-MDB efforts to collaborate on issues of global and mutual interest in trade financing, including in collaboration with the WTO (box III.D.3), on issues such as risk sharing, co-financing, and capacity-building.

5.2 Aid for trade

Aid for trade seeks to support developing countries, particularly LDCs, to expand trade by building the capacity and necessary infrastructure to implement and benefit from WTO agreements.

Box III.D.3

The Asian Development Bank's Trade and Supply Chain Finance Program

The Asian Development Bank's Trade and Supply Chain Finance Program (TSCFP) complements its core financing, guarantee and risk mitigation solutions in trade and trade financing with a portfolio of special projects and initiatives aimed at amplifying development impacts, fighting poverty and driving greater engagement in green, climate-friendly and sustainable trade that aligns with environmental, social and governance considerations. The TSCFP is active in combating trade-based money laundering, enabling the adoption of environmental and social management systems among its local partner banks across the Asia-Pacific region, and facilitating detailed transparency and traceability of carbon emissions across supply chains. It also helps to accelerate the digitalization of international trade and promote the deployment of

deep-tier supply chain finance solutions to help narrow the global trade finance gap.

During the first nine months of 2023, the TSCFP supported trade of over \$3.5 billion through more than 17,300 transactions, with about 5,600 transactions linked to SMEs. This core activity is complemented by activities such as the carbon tracking initiative, being developed in partnership with globally recognized standards and regulation partners such as GS1 and its unique barcode and QR code technology, together with the IFRS Foundation, widely known for setting accounting standards and practices but now aiming to do the same for sustainability reporting, including in the climate space. Together, these three organizations are working on a technology solution that will assist in tracking carbon emissions end to end across global supply chains, while also helping companies and supply chains to report results digitally, to demonstrate compliance against standards and regulatory requirements.

Since 2006, commitments and disbursements of aid for trade have grown steadily (figure III.D.16). In 2020, the most recent year for which data is available, global disbursements of aid for trade increased to \$48.7 billion, from \$47.3 in 2019. Commitments have increased sharply to \$64.6 billion from \$54.8 billion in 2019.

The 2022 Aid for Trade Monitoring and Evaluation (M&E) exercise took place amid simultaneous crises of unprecedented magnitude, including the war in Ukraine, high food and energy prices, tighter monetary policies, supply chain disruptions and COVID-19. Responses to the joint Organisation for Economic Co-operation and Development (OECD)-WTO M&E questionnaires indicate an increase in the perceived importance of aid for trade, for both developing countries and donors. The next Aid for Trade Global Review, entitled Mainstreaming Trade, will be held at the WTO in Geneva in mid-2024.

In the face of such recent multiple crises, aid for trade can act as a key facilitator of economic resilience and export diversification.

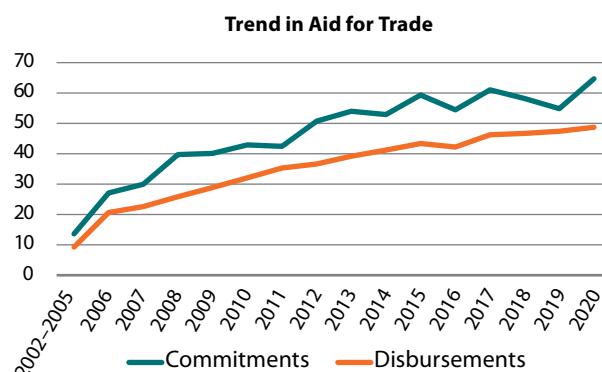
Various studies have identified diversification as an important source of supply chain and economic resilience. Indeed, studies show that the degree of concentration of suppliers and products can amplify or dampen international shocks and that aid for trade can promote export diversification in order to advance economic growth through lower trade costs and higher diversification.³⁰ A recent empirical study on the impact of aid for trade on export diversification, focusing on sub-Saharan exports, concluded that aid for trade was conducive to such diversification. The findings suggest that aid for trade contributed to export diversification in sub-Saharan Africa and imply that increasing aid for trade resources could

be effective in promoting a further broadening of exports to advance economic growth through lower trade costs and higher diversification.³¹ Aid for trade has also had positive impacts on FDI inflows and could support more diversified inflows.³²

Aid for trade increasingly takes SDG considerations into account.

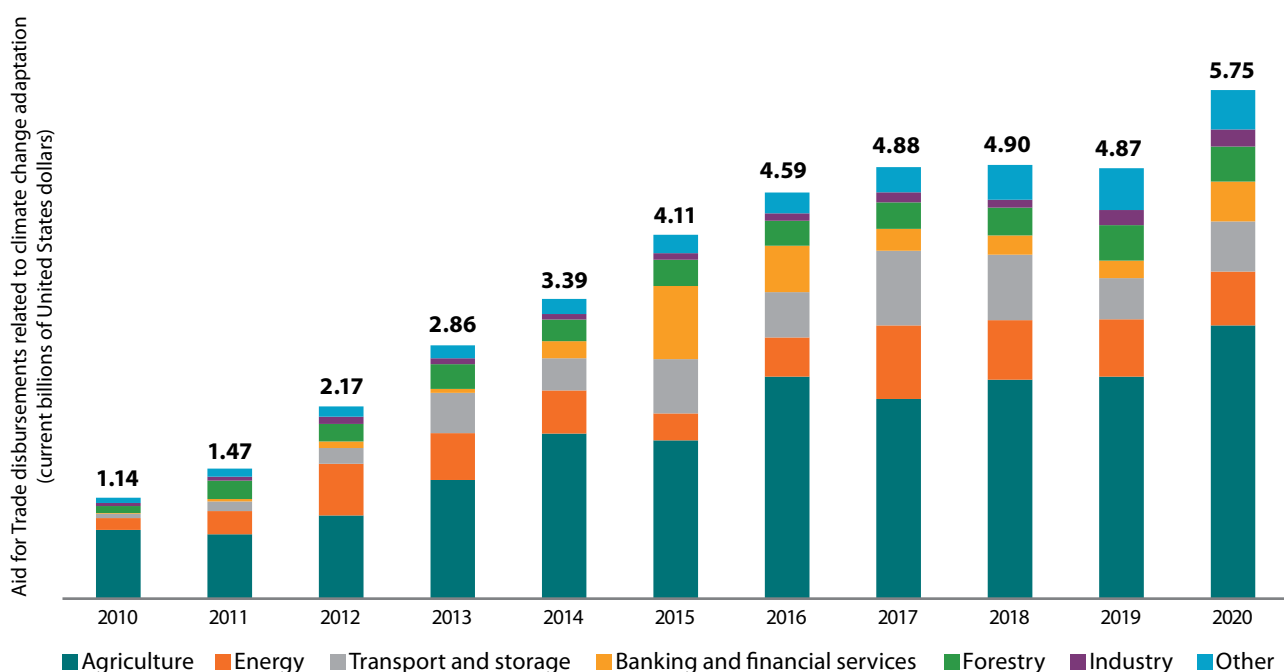
Responses to the 2022 Aid for Trade M&E exercise by the OECD and WTO suggest a shift towards sustainability considerations, including climate and gender equality, pointing to the potential of aid for trade to further

Figure III.D.16
Trends in aid for trade
(Billions of United States dollars)



Source: OECD/WTO data.

Figure III.D.17
Aid for trade disbursements, climate change adaptation and agriculture
(Current billions of United States dollars)



Source: WTO, 2022.

support progress towards the SDGs. This new emphasis is also partly due to growing demands embodied in international commitments, notably the Paris Agreement. In 2020, 51 per cent of aid for trade commitments included climate-related objectives, representing 56 per cent of total climate-related official development assistance commitments in 2020. LDCs and other low-income countries are the primary beneficiaries, accounting for 37 per cent of total climate-related commitments made in aid for trade sectors.

While aid for trade disbursements with climate objectives reached \$15 billion in 2020, constituting 31 per cent of total aid

for trade, only a limited portion (12 per cent) was allocated to adaptation projects. Notably, these projects focused on the agriculture (54 per cent), energy, transport, banking and forestry sectors (figure III.D.17). Despite the relative scarcity of funds, projects like those supported by the Enhanced Integrated Framework showcase the potential of adaptation investments to enhance resilience and inclusivity. Strengthening the integration of trade dimensions into national adaptation strategies and fostering alignment between aid for trade and climate finance programmes could further optimize support for climate change adaptation in developing countries.

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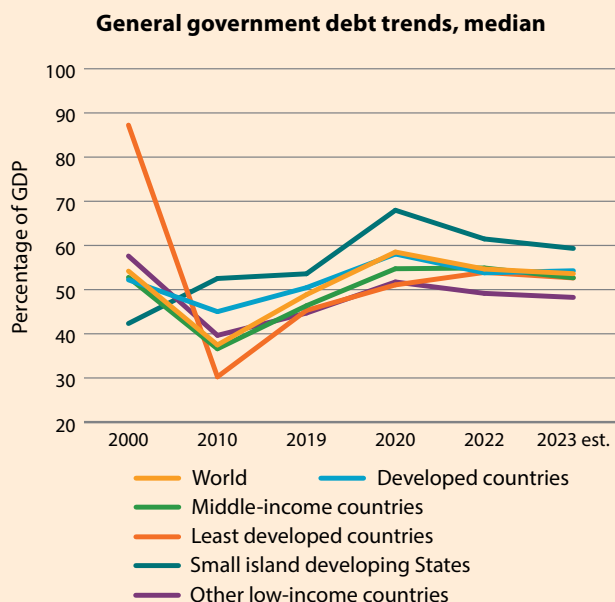
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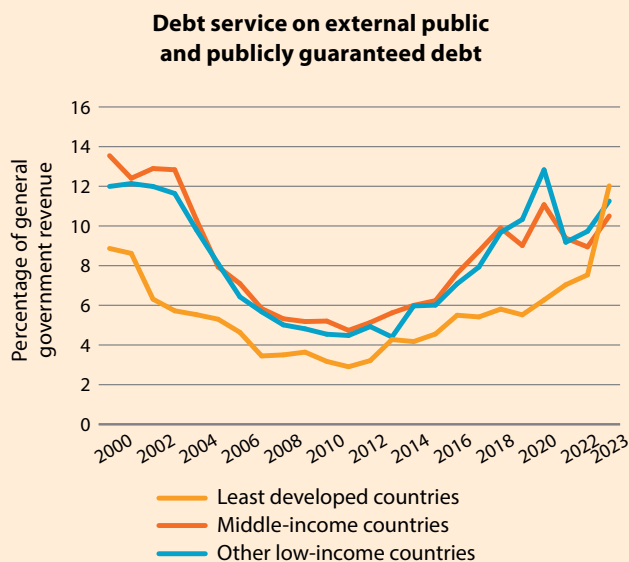


Debt and debt sustainability *in numbers*

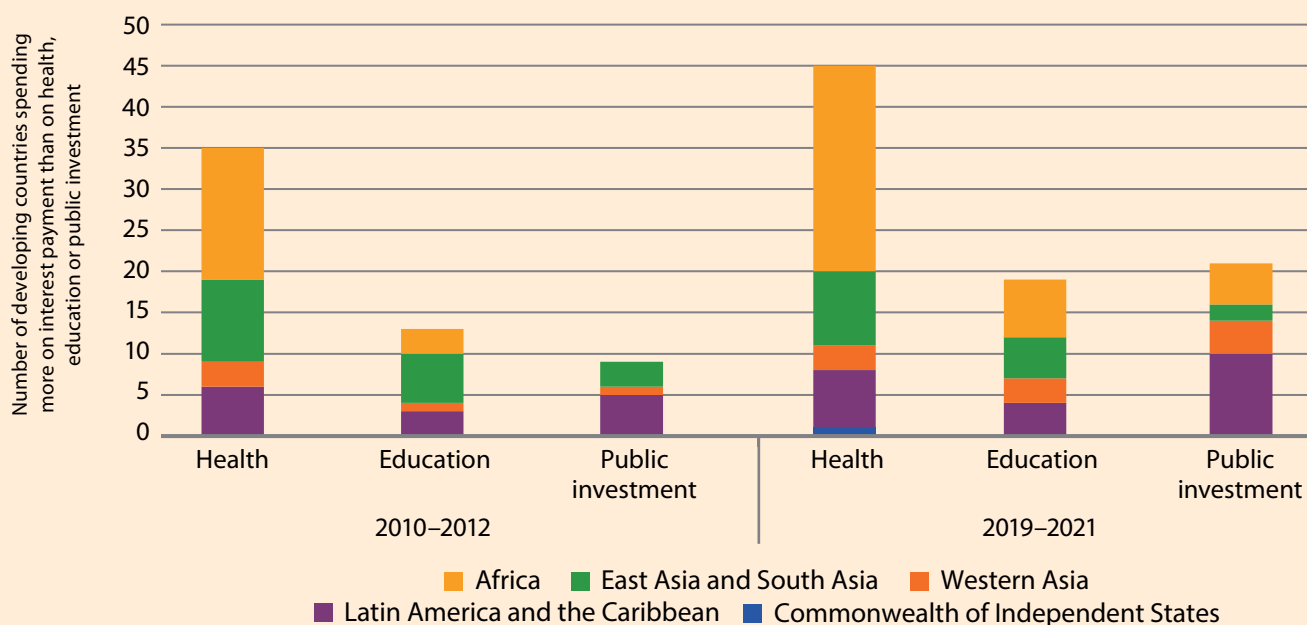
After a sharp rise in public debt during the pandemic and a steady increase in the preceding decade, public debt levels have stabilized.



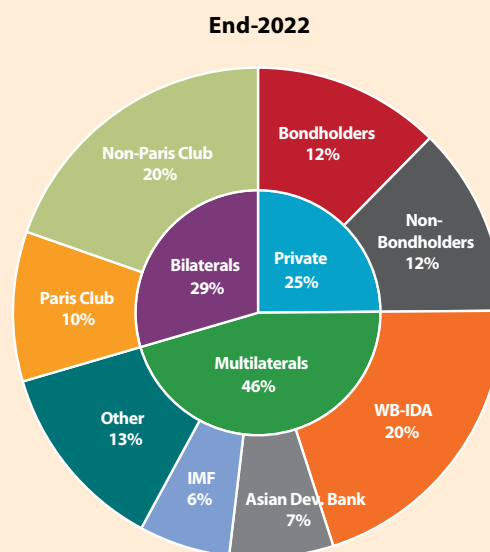
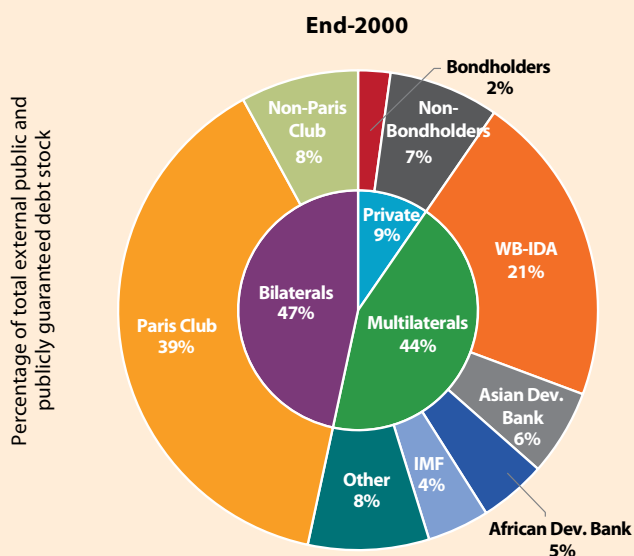
High levels of debt have translated into high debt service burdens, now reaching levels last seen in the early 2000s.



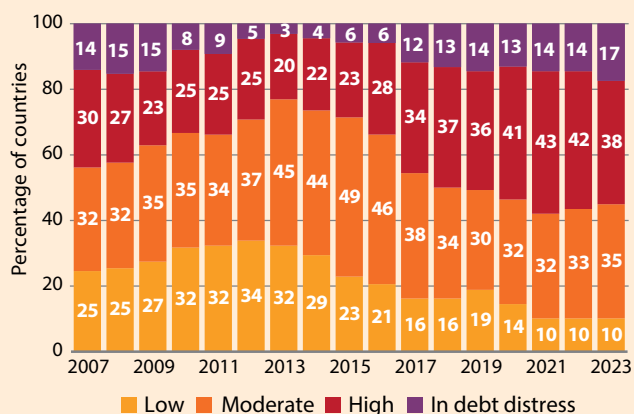
Over the last decade, an increasing number of developing countries spend more on servicing public debt than on health, education and public investment.



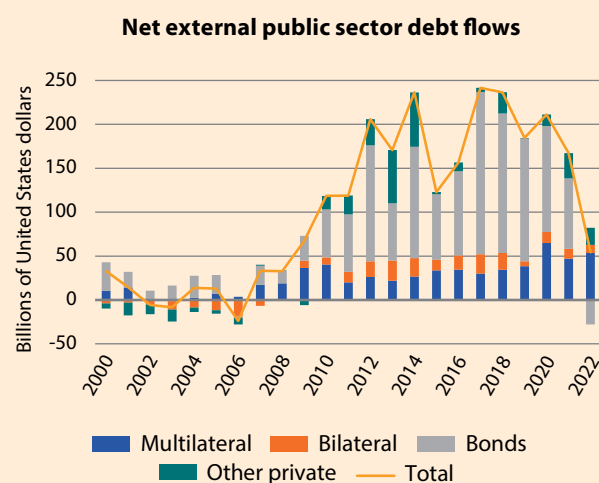
Rising debt service burdens are in part due to changing debt composition: for LDCs and LICs, the shares in external public debt held by commercial creditors and non-Paris Club official creditors more than doubled between 2000 and 2022.



Fifty-five per cent of LDCs and other LICs are at high risk of or in external debt distress, higher than the levels in any year from 2007 to 2019.



Amid tight global financing conditions since 2022, only debt financing from multilateral institutions prevented a drying up of net debt inflows to developing countries.





Chapter III.E



Debt and debt sustainability

1. Key messages and recommendations

Developing countries, especially the poorest and most vulnerable, face continued elevated debt challenges. More than half the countries that use the joint International Monetary Fund (IMF)-World Bank Debt Sustainability Framework for Low-Income Countries are at high risk of or in debt distress. Debt service burdens could crowd out vital investments and constrain progress towards the Sustainable Development Goals (SDGs) in many developing countries. While debt levels have broadly stabilized after spiking in the first year of the pandemic, the high costs of servicing and refinancing debt amid tight global financial conditions add to the debt vulnerabilities of many developing countries. Supporting these countries in navigating their debt challenges is essential given the significant financing needs associated with reaching the SDGs, achieving structural transformation, adapting to climate change and increasing resilience in the face of future shocks.

While median debt levels generally fell across the globe in the first decade of the new millennium, this trend reversed in the second decade. Debt levels around the world have now broadly stabilized near their 2000 levels. Nevertheless, significant variations across countries and country groupings remain. Debt in least developed countries (LDCs), most of whom participated in the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI), has increased since the mid-2010s as access to debt markets was restored. The debt increase reversed some, though not all, of the gains from the relief initiatives.

There has been a significant shift in the debt composition of developing countries since 2000, with access to new financing translating into rapidly growing debt service burdens. For LDCs and other low-income countries (LICs), commercial debt now represents a quarter of external debt, up from just 10 per cent in 2010, driven mostly by countries accessing international

bond markets for the first time and the rise of syndicated bank and commodity-backed loans. The share of non-Paris Club creditors in the total external debt stock of LDCs and other LICs now exceeds that of Paris Club creditors. While the broader shift of the financing mix towards private creditors and non-Paris Club creditors has led to greater access to finance, it has also resulted in greater debt servicing burdens—with external debt service alone consuming more than a fifth of tax revenue in 25 developing countries. The greater diversity of creditors also exacerbates creditor coordination challenges in the event of debt restructurings.

High debt service burdens can hamper the implementation of the SDGs. Around 3.3 billion people live in countries where governments spend more on interest payments than on health or education. In a growing number of developing countries, public debt interest service surpasses public spending in crucial sectors. Challenges are particularly pronounced for countries that are most vulnerable to climate shocks. They face high borrowing costs and—when hit by extreme weather events—high recovery costs, which increase debt vulnerability. At the same time, it is essential that countries do more to optimize spending, increase revenues and target growth-enhancing reforms.

With debt service burdens projected to remain elevated for several years amid dwindling new financing options, more needs to be done to reduce the risks of liquidity crises. Global financing conditions remain tight; since 2022, net debt inflows to developing countries as a whole would have turned negative if not for the sustained debt financing by multilateral institutions. High refinancing costs and limited access to international financial markets combined with continuously high external debt repayments in 2024 and 2025 will put significant liquidity pressures on countries. Today, 55 per cent of LDCs and other LICs are assessed as having a high risk of or in debt distress.

Against this backdrop, it is critical to urgently address the debt challenges of developing countries. Intensified action is needed across three priorities: (i) strengthening debt crisis prevention, including through sound debt management and transparency; (ii) finding solutions for countries that face severe fiscal constraints, debt overhangs and insufficient reforms to address underlying problems, to invest in the SDGs; and (iii) a more effective debt crisis resolution mechanism.

In today's more complex environment, debt management is more essential than ever. Technical assistance by various institutions and the sharing of good practices are supporting progress in public debt management. Nevertheless, progress remains gradual and uneven across countries. Fragile and conflict-affected States as well as small developing countries face particularly large resource and capacity constraints.

Debt transparency can play an important role in supporting continued financing flows to developing countries and is the shared responsibility of both borrowers and creditors. While progress has been made in recent years, gaps remain. Borrowers should continue to strengthen their institutional and operational frameworks to enable timely and comprehensive debt reporting. Creditors should follow through on initiatives to support more transparency.

Countries that are solvent but face very high debt service burdens over the next several years will need more systematic support.

With fiscal space already eroded and very high debt service payments coming up amid tight financing conditions, LICs and lower-middle-income countries under tight liquidity pressures face the prospect of further reduced SDG investments or even solvency challenges unless they receive additional support and implement important reforms to address fiscal constraints and weak growth. This will require additional concessional financing, including the sustaining of large volume of highly concessional financing from multilateral lenders, and could include the use of financial instruments such as debt swaps or credit enhancements to enable the rollover of commercial debt, as well as measures to prevent leakage of fresh concessional financing to service non-concessional debt.

The international community needs to continue advancing progress on the resolution of debt distress situations, monitor developments closely, and enhance the toolkit to ensure it has the appropriate tools to support countries when risks materialize. In that context and despite recent important progress, including resolution of debt distress in a few countries, continued efforts to enhance the efficiency of the Group of Twenty (G20) Common Framework are needed, together with exploring other options to mitigate the risks that a financing squeeze might trigger a debt crisis in additional countries.

The Fourth International Conference on Financing for Development provides an opportunity to tackle the challenges of high borrowing costs and debt service burdens and address gaps in the debt restructuring architecture. There is broad recognition of the need to address the fiscal and external constraints of many developing countries that are unable to invest in the SDGs due to high debt service burdens; and of the need to further improve debt resolution processes. Many proposals have been put forward to address these challenges, including financial instruments and contractual innovations that could deliver fiscal space for the SDGs (such as debt swaps, credit enhancements or state-contingent clauses), enhanced analytical tools, stepped up capacity support, domestic

law reforms and enhancements to the Common Framework and other institutional innovations at the international level. However, there still remains no political agreement on a package of reforms that would align the debt architecture with the SDGs. Preparations for the Fourth International Conference on Financing for Development will provide an opportunity to identify relevant elements of such a package and deliver it in 2025.

The rest of this chapter first provides an overview of global debt trends in the past two decades, followed by a section on the interaction between sustainable debt financing and the SDGs. The chapter will conclude by discussing progress made in debt crisis prevention and resolution, while highlighting key challenges that have to be addressed.

2. Overview of global debt trends

2.1 Debt and debt vulnerabilities: Trends and drivers

After declining in the first decade of the new millennium, public debt ratios increased steadily up to 2020, before tapering off more recently. Public debt-to-GDP ratios in developed countries rose sharply starting from 2007 and, after stabilizing in the 2010s, reached a new high during the COVID-19 pandemic when countries financed large-scale fiscal response packages. After decreasing for much of the 2000s in a favourable global economic environment, public debt in middle-income countries (MICs) levelled off after the 2008 world financial and economic crisis, before resuming an upward trend in 2014, which gathered pace during the pandemic. LICs experienced a similar, if more pronounced, trajectory. Debt levels in all country groups have broadly stabilized since 2020 (figure III.E.1).

The decline and subsequent rebound of public debt was most pronounced in vulnerable countries, particularly LDCs and other LICs.¹ In the late 1990s and early 2000s, many LDCs and other LICs benefited from strong economic growth along with debt relief under the HIPC Initiative and MDRI, which significantly lowered external debt-to-GDP ratios across the two country groups (figure III.E.2).² Over the past 10 to 15 years, many of these countries embarked on ambitious, externally financed infrastructure drives, which contributed to a doubling of the stock of external public debt in nominal United States dollar terms since 2010 (figure III.E.3). Debt in small island developing States (SIDS) rose from 42.3 per cent of GDP in 2000 to around 60 per cent of GDP in 2022, after peaking around 2020, as these countries—many of which rely on tourism—were severely impacted by the pandemic (figure III.E.1). SIDS also saw liquidity buffers erode, making them even more vulnerable to external shocks.

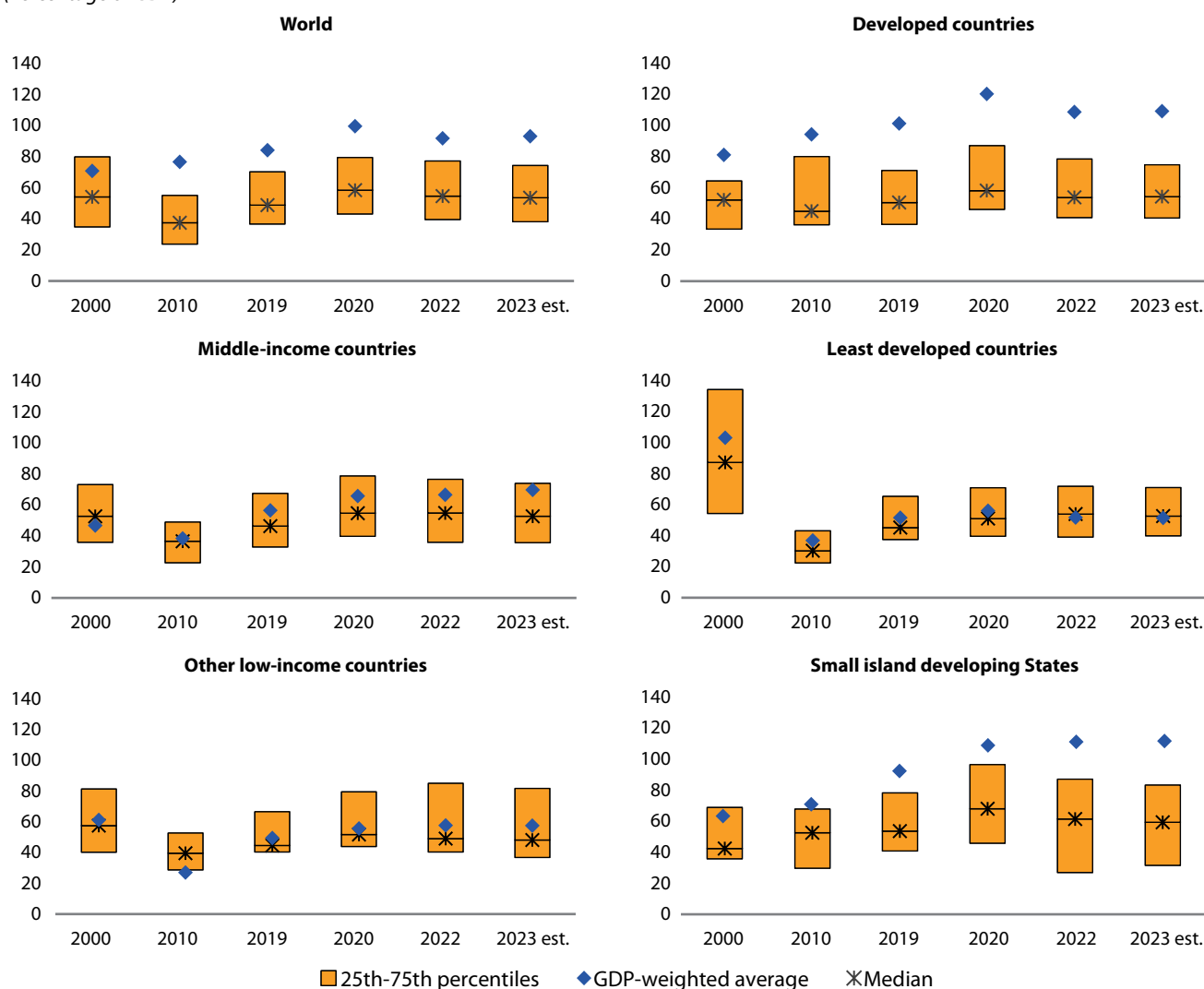
Over the last 20 years, the creditor landscape has become more diverse for many developing countries. For LDCs and other LICs, the shares of external public debt held by commercial creditors—including bondholders and other private creditors—and non-Paris Club official creditors more than doubled, from 17 per cent at end-2000 to 45 per cent at end-2022, with the shares of Paris Club and multilateral creditors declining from 83 per cent to 56 per cent, respectively (figure III.E.4). Similar trends were observed among MICs and SIDS.³

The complexity and riskiness of debt instruments has also increased. Across developing countries, debt with more complex lending terms (e.g. collateralization⁴), more frequent repricing (due to

Figure III.E.1

Overall general government debt evolution in developed and developing countries, 2000–2023

(Percentage of GDP)

**Source:** IMF staff calculations based on IMF WEO database (October 2023).**Note:** Overall general government debt includes both domestic and external debt.

shorter maturities and greater prevalence of variable interest rates) and/or indirect forms of financing, such as state-owned enterprise-related or public-private partnership-related transactions, proliferated.⁵ With access to international bond markets drying up in recent years, many developing countries shifted to syndicated loans, resulting in a significant increase in such loans in this grouping. The increased prevalence of syndicated loans poses challenges as they are typically less transparent, have shorter maturities and include fewer safeguards against holdouts in debt resolution (although efforts have been made to introduce majority voting provisions to such loans; and there are typically far fewer creditors in the case of syndicated loans when compared to bonds, which may facilitate debt resolution). In parallel, domestic debt has become an increasingly important financing source across developing countries, including LDCs and other LICs (figure III.E.2). Development of domestic debt markets can

help to diversify the investor base and support the mitigation of exchange rate risk. However, an increase in domestic sovereign borrowing can also lead to a reduction in available credit for the private sector and enlarge the sovereign-bank nexus, potentially exacerbating the risk of negative feedback loops.

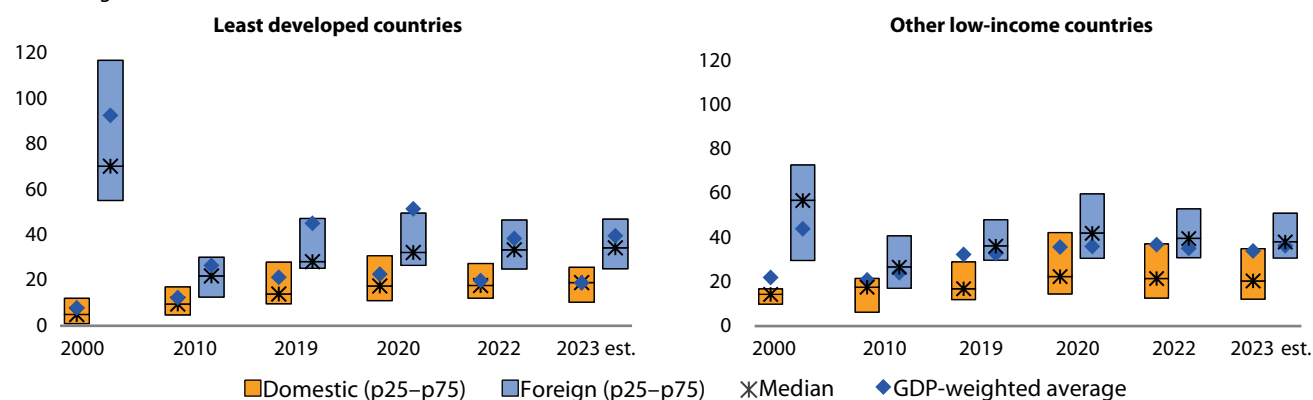
In the most recent post-pandemic period, many developing countries have faced external liquidity pressures, with only scaled-up multilateral financing preventing a collapse in external financing.

LICs and especially LDCs started to see a decline in external financing inflows in 2019, driven by the drop in private inflows and net financing from non-Paris Club official creditors. This downward trend was exacerbated by the pandemic. By the second half of 2022, developing countries with the weakest credit ratings effectively lost access to international bond markets.⁶ Debt financing provided by multilateral institutions prevented

Figure III.E.2

Currency composition of general government debt of LDCs and other LICs, 2000–2023

(Percentage of GDP)

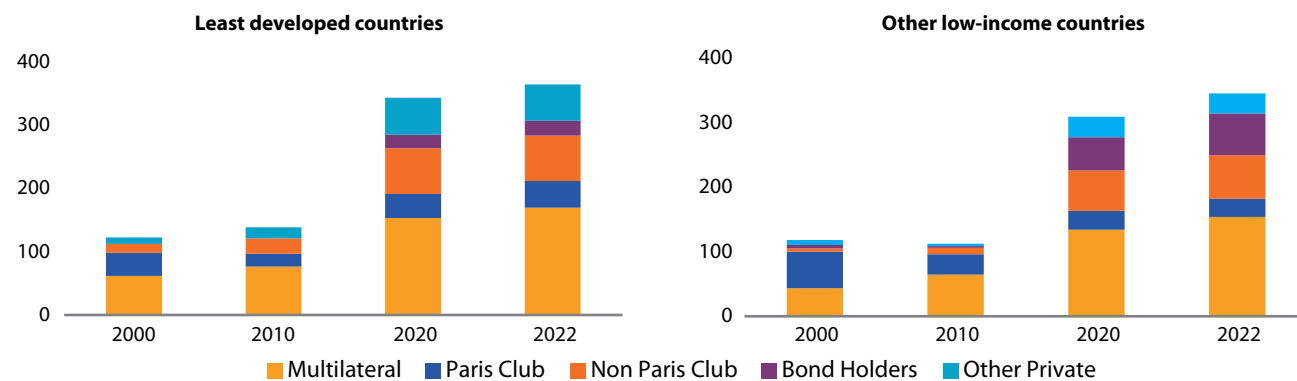


Source: IMF staff calculations based on IMF WEO database (October 2023).

Figure III.E.3

External public and publicly guaranteed debt stock in LDCs and other LICs, by creditor type, 2000–2022

(Billions of United States dollars)

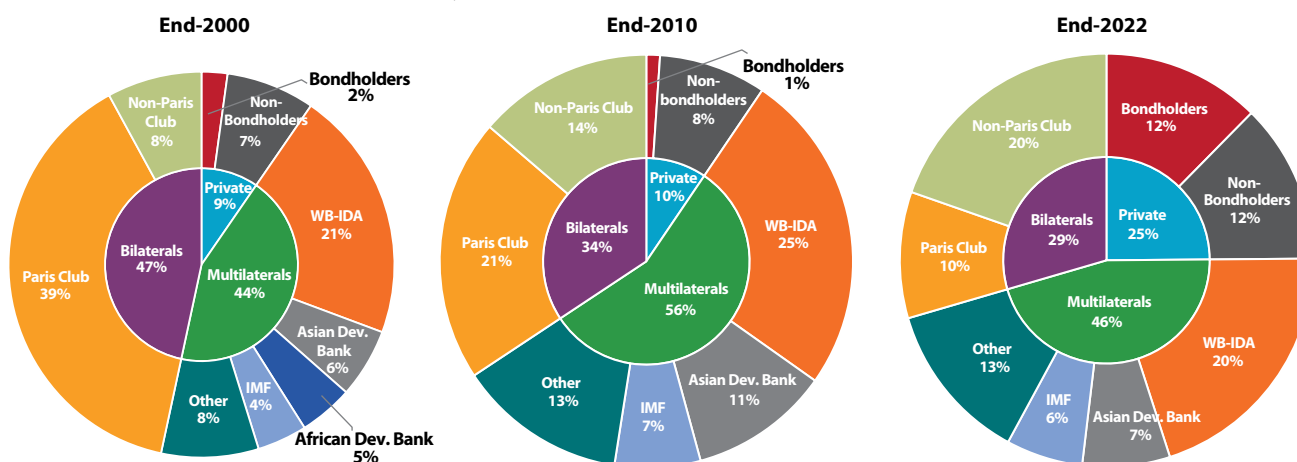


Source: IMF staff calculations based on World Bank International Debt Statistics database.

Figure III.E.4

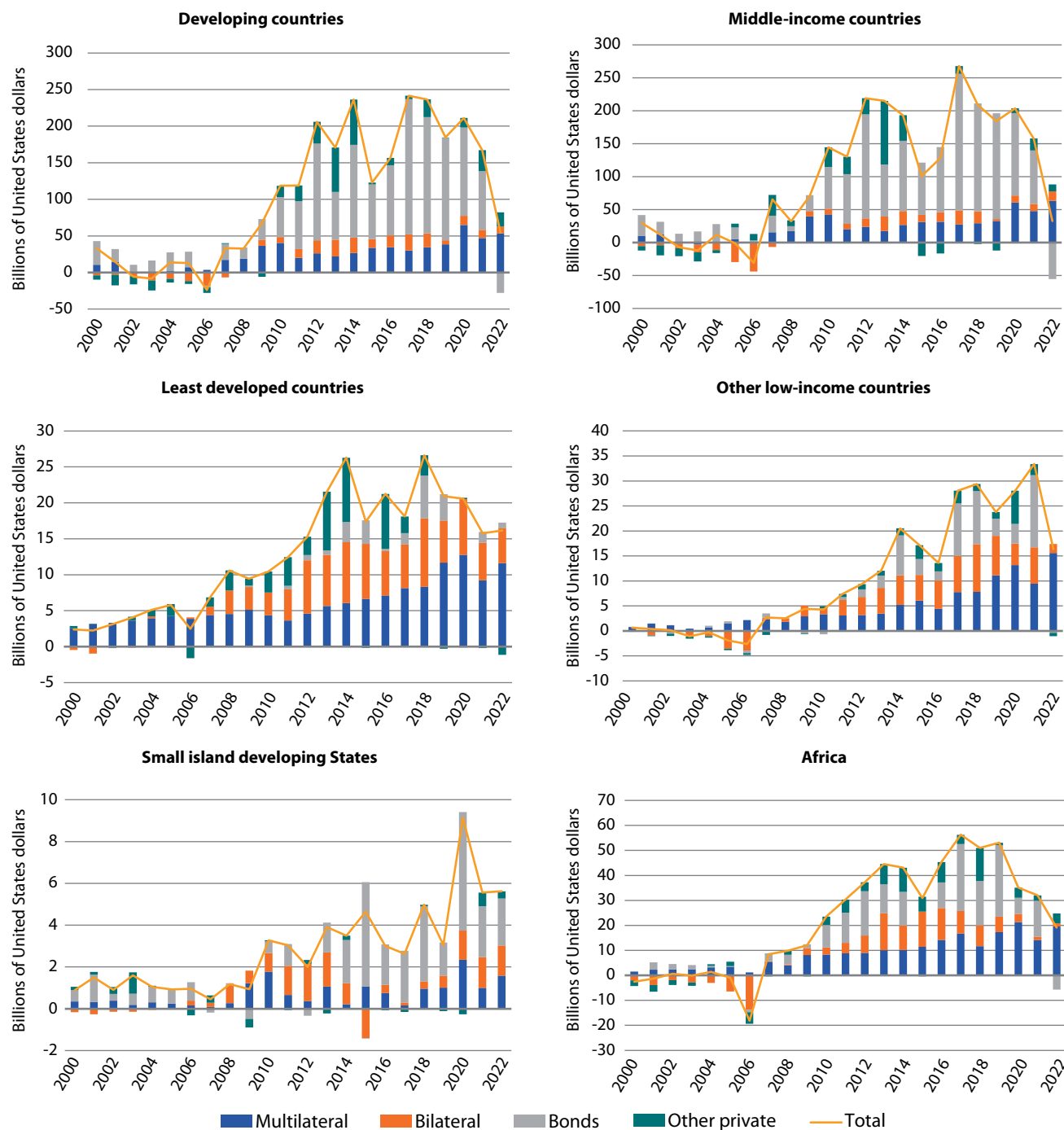
External creditor landscape in LDCs and other LICs

(Percentage of total external public and publicly guaranteed debt stock)



Source: IMF staff calculations based on World Bank International Debt Statistics database.

Figure III.E.5

Net external public sector debt flows, by country group, 2000–2022*(Billions of United States dollars)***Source:** UN DESA calculations based on World Bank International Debt Statistics database.**Note:** Data shows net flows on external public sector debt, measured as new disbursements minus principal repayments.

an overall net debt outflow for MICs in 2022, counteracting the net outflows to bondholders. Multilateral institutions also played a key role in sustaining net debt inflows to LDCs and Africa—where over 70 per cent of all LDCs are located—in the post-pandemic period, as net financing from private creditors was negative (figure III.E.5). In the case of SIDS, net bond inflows were positive in 2022, reflecting an improvement in the external sector as the tourism industry rebounded.

Drivers of debt and debt vulnerabilities

Primary deficits related to large spending needs and external shocks have been one of the key drivers of debt dynamics.⁷ While debt dynamics vary across countries, most LDCs and other LICs have experienced consistent primary deficits (figure III.E.6). Significant spending needs, including for investment in infrastructure, climate actions and other SDGs, were further accentuated in the context of rising international food and energy prices and a weakening of domestic currencies vis-à-vis the United States dollar. Many countries introduced fiscal support measures to mitigate the effects of the crises, putting additional pressure on their fiscal balances and debt. Tax revenue has not kept pace with expenditure (see chapter III.A); neither has concessional financing, with some developing countries experiencing a decline in the amount of concessional finance received.⁸ Other developing countries saw a loss of access to concessional financing altogether as their income level increased, while remaining highly vulnerable to climate and other shocks. Most recently, tightening global financial conditions have increased borrowing costs. At the same time, the differential between the real interest rate and real GDP growth ($r-g$) has remained favourable for debt dynamics in LDCs and other LICs, despite pressures from increasing country risk premia and global interest rates, acting as a countervailing force to persistent primary deficits. Overall, rising debt levels have translated into fast-rising debt service burdens, potentially diverting resources from SDG investment (section 2.2) and increasing liquidity and solvency risks (section 2.3).

2.2 Debt service burdens

Rising debt levels, changing creditor composition and tighter financing conditions have translated into greater debt service

burdens. From 2022 to 2023, the issuance of hard currency bonds by LDCs and other LICs almost dried up and those that were issued carried very high coupon rates; MICs experienced a similar, if less pronounced, deterioration of financing conditions (figure III.E.7). This increase in borrowing costs adds to already rising debt service burdens attributed to growing debt stocks and the associated amortizations as the accumulated debt starts falling due. As a result, debt service payments—including both interest and principal repayments—relative to government revenues have increased dramatically across LDCs and other LICs (figure III.E.8). The median debt service burden for LDCs rose from 3.1 per cent of government revenues in 2010 to 12 per cent in 2023—the highest level since 2000; for other LICs, it rose from 4.5 per cent to 11.3 per cent during the same period. MICs and SIDS also dedicate a growing share of revenue to debt service, although the increases are less pronounced. As reported in the *Financing for Sustainable Development Report 2023*, 25 developing countries (this number remained unchanged in 2023) dedicate more than a fifth of their total revenues to servicing public external debt, the highest number since 2000, which also marked the beginning of the HIPC Initiative, the last large-scale debt relief initiative for developing countries.

Higher debt service costs reduce available fiscal space for development financing. Around 3.3 billion people live in countries where governments spend more on interest payments than on education or health.⁹ Forty-five developing countries, including 29 LDCs and other LICs, spend more on debt servicing than on health; 19, including 8 LDCs and other LICs, spend more on debt service than on education; and in 21, including 4 LDCs and other LICs, public investment is falling behind interest payments on public debt (figure III.E.9).¹⁰ Across regions, this crowding out of development spending is strongest in Africa and Western Asia.

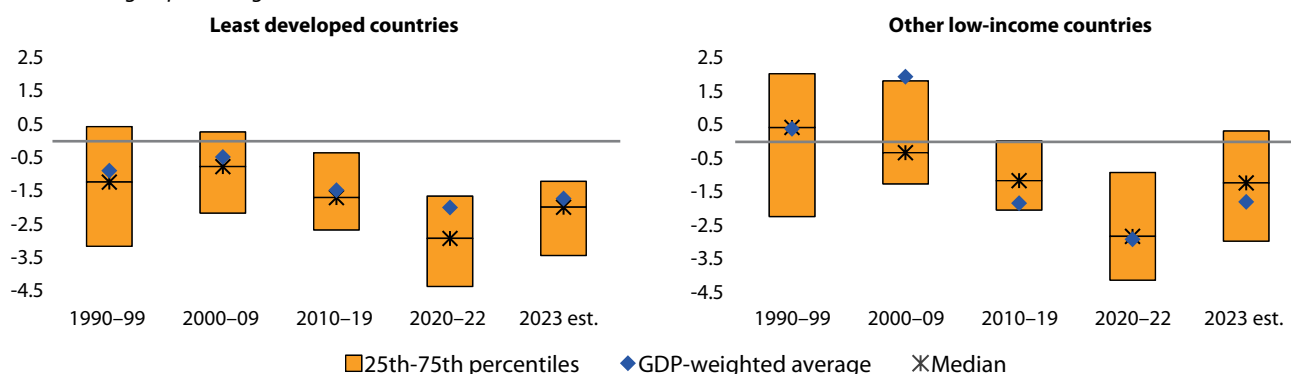
2.3. Elevated debt sustainability risks

High debt levels and tight financing conditions have translated into growing liquidity and solvency risks. Debt service burdens on external debt will remain elevated for LDCs and other LICs as well as many lower-middle-income countries through 2024 and 2025, and ease only gradually after that (figure III.E.10). In LDCs, for example, external debt service will hover around \$40 billion annually between 2023 and 2025, up

Figure III.E.6

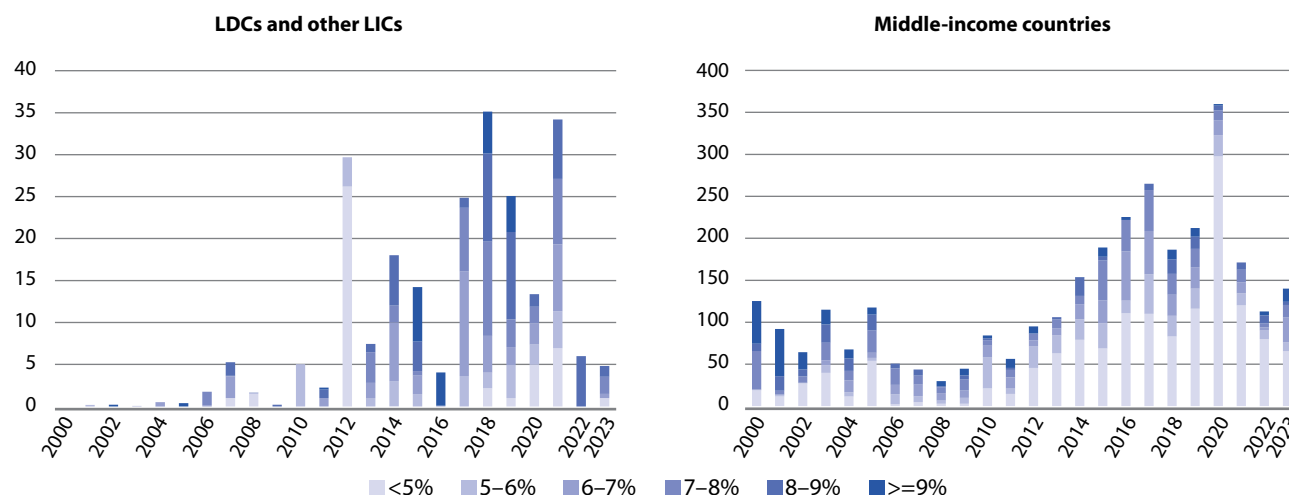
LDCs and other LICs: General government primary balance, 1990–2023

(Period averages, percentage of GDP)



Source: IMF staff calculations based on IMF WEO database (October 2023).

Figure III.E.7

Sovereign bond issuance in hard currencies, by coupon rate, 2000–2023*(Billions of United States dollars)***Source:** UN DESA calculations based on LSEG data.**Note:** Data includes sovereign bond issuance in pounds sterling, euros, Japanese yen and United States dollars.

from \$26 billion in 2021. In a context of very high refinancing costs and limited access to international financial markets, these soaring external debt repayments will put significant liquidity pressures on countries; without a mix of adjustment, reforms to accelerate growth and robust access to concessional financing, there is a risk that they may turn into solvency crises.

The risks of fiscal crises and debt distress in developing countries remain high, particularly in LDCs and other LICs. More than half of all LDCs and other LICs are assessed as having a high risk of or in debt distress, twice the level in 2013, according to the IMF-World Bank Debt Sustainability Framework for Low-Income Countries (figure III.E.11). The debt risk ratings of 15 countries have been downgraded since the beginning of the COVID-19 pandemic; however, in most cases, the vulnerabilities manifested well before the pandemic. Since 2020, five countries have had debt risk rating upgrades, mostly reflecting positive results from debt restructuring. Among the countries assessed as having a high risk of debt distress or in debt distress, four have requested a Common Framework debt restructuring: Chad (completed, with a Memorandum of Understanding signed in December 2022), Ethiopia, Zambia and Ghana. Somalia has completed and Sudan is undertaking a debt restructuring under the HIPC Initiative. Several other countries are engaged (Malawi) or have announced their intention or interest to restructure their debt through bilateral negotiations (Djibouti and Lao PDR).

investments enhance an economy's resilience in the long run, including through reducing debt-related vulnerabilities. The terms on which countries can access debt and other sources of financing, along with how effectively these resources are utilized, will determine whether countries can achieve a virtuous cycle of investment-driven recoveries and resilient development pathways, which will also create the resource base to service debts in the long run. Conversely, countries faced with rising debt burdens and without additional support by the international community may need to forego investments in resilience and long-term development, which will only further undermine their prospects. This challenge is particularly pronounced for climate-vulnerable countries (see section 3.1 below). Better understanding, managing and addressing this interplay between long-term investments in the SDGs and climate action, the closing of financing gaps for SDG investments, the efficient use of debt financing while safeguarding long-term debt sustainability, and implementation of key growth-enhancing reforms will be critical to achieving the SDGs and climate action. Section 3.2 lays out a range of proposals that have been made to this end.

3.1 The debt and climate vicious cycle

The vicious cycle of rising debt and constrained productive investment is especially pronounced in climate-vulnerable countries.

Rising climate vulnerabilities, as reflected by more frequent and severe natural disasters, exert significant pressure on countries' national budgets. The financing needs to address damages, recover from disasters and adapt to climate change are very large—the annual cost of adapting public assets alone has been estimated to exceed 1 per cent of GDP annually for the next 10 years in 50 LICs, while for some small countries it runs to more than 2.5 per cent of GDP.¹¹ Disasters also significantly disrupt economic activities and diminish countries' ability to mobilize domestic and external resources for climate adaptation. To meet urgent needs,

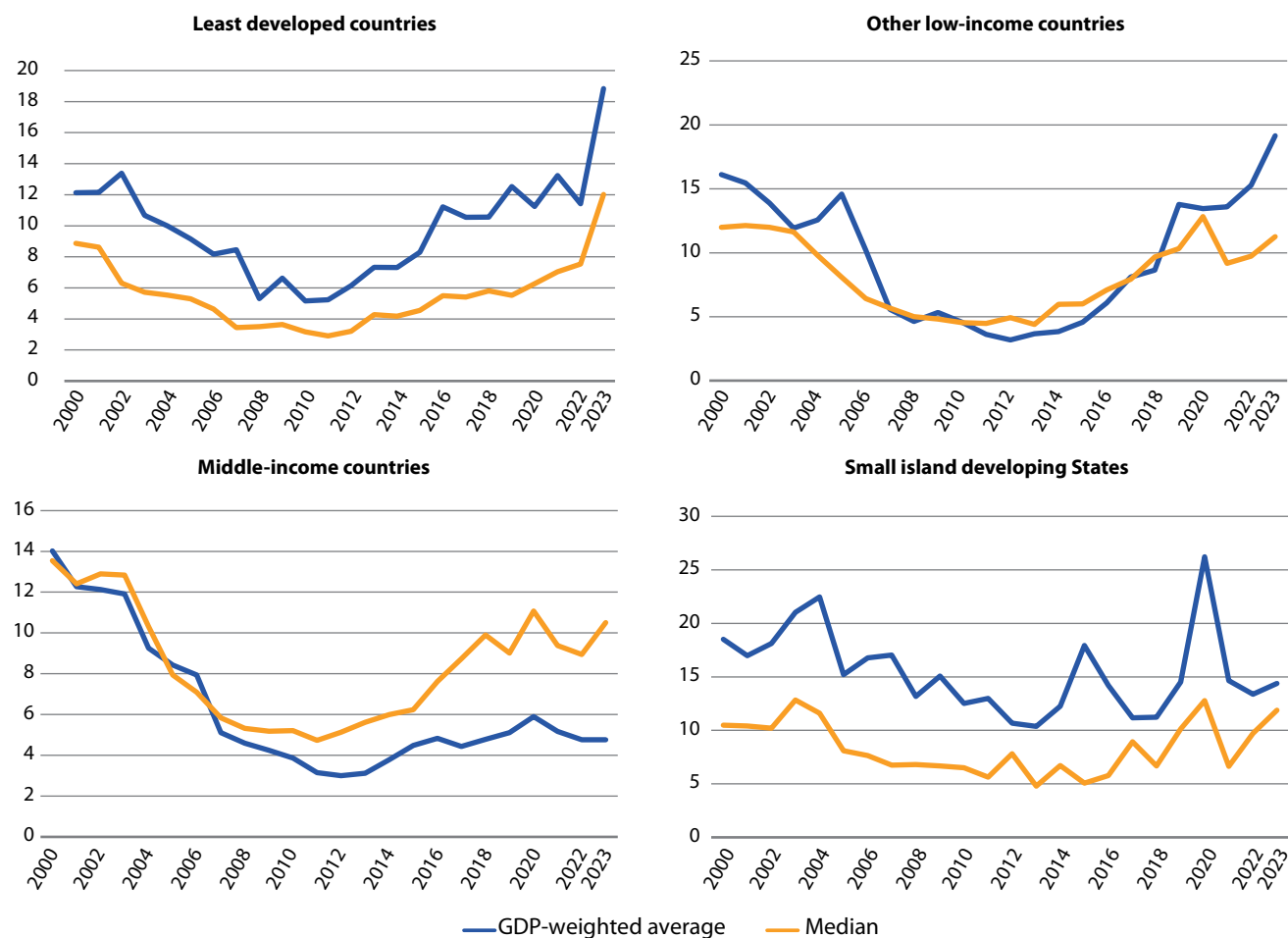
3. Sustainable debt financing and the SDGs

In the wake of multiple global shocks, many countries face difficult trade-offs between maintaining fiscal sustainability and investing in structural transformation, including productive investment, climate action and other SDGs. Effective SDG

Figure III.E.8

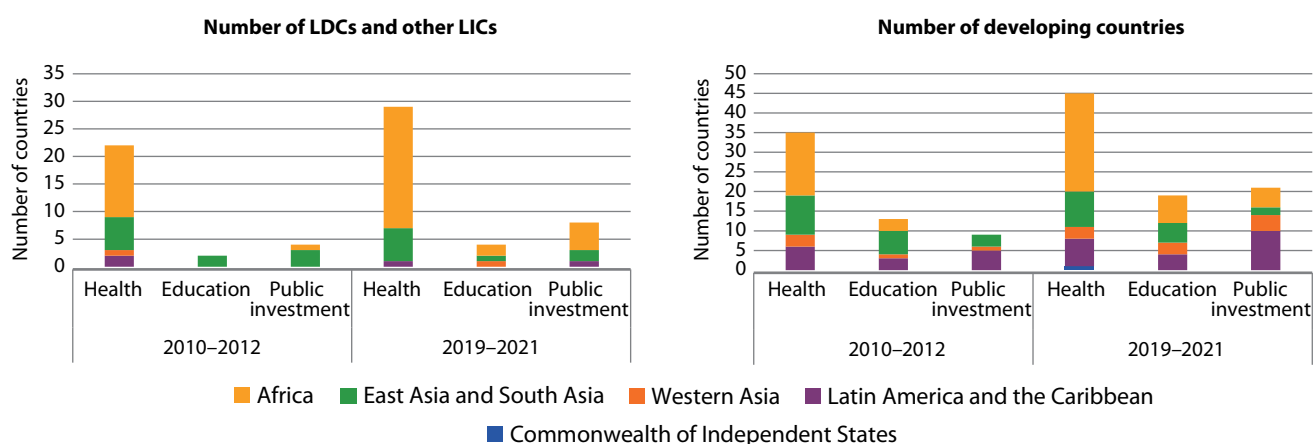
Debt service on external public and publicly guaranteed debt, 2000–2023

(Percentage of general government revenue)



Source: UN DESA calculations based on World Bank International Debt Statistics database and IMF WEO database (October 2023).

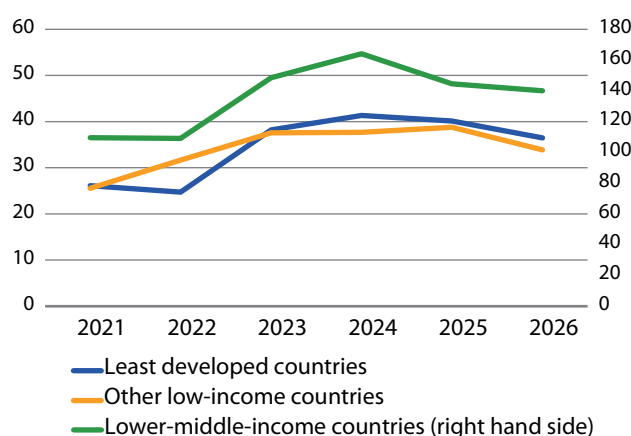
Figure III.E.9

Developing countries that spend more on servicing public debt than on health, education, and public investment, 2010–2012 versus 2019–2021

Source: UN DESA, adapted from United Nations Global Crisis Response Group (2023).

Figure III.E.10

Debt service on external public and publicly guaranteed debt
(Billions of United States dollars)



Source: UN DESA calculations based on World Bank International Debt Statistics database and IMF WEO database (October 2023).

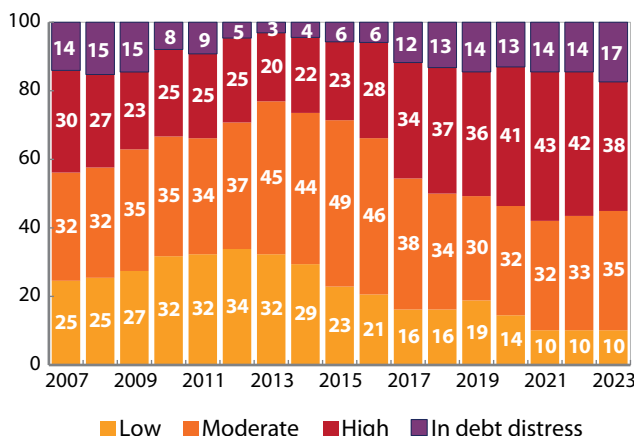
vulnerable countries often have to resort to increased borrowing, leading to a build-up of debt and an increasing share of national budgets allocated to debt servicing. This, in turn, limits their ability to invest in long-term resilience and the SDGs, making them even more vulnerable to future shocks. Consequently, the cycle of borrowing and debt accumulation not only constrains future investment opportunities but also exacerbates vulnerabilities to climate change, creating a self-perpetuating loop of debt and climate challenges.

Climate and debt vulnerabilities increasingly overlap. Some assessments suggest that over half of the debt upsurge in vulnerable countries stems from funding disaster recoveries.¹² As figure III.E.12 shows, 30 out of 68 countries eligible to access concessional finance under the IMF's Poverty Reduction and Growth Trust (PRGT) (44 per cent of the total) are at the intersection of high debt and climate vulnerabilities. This intersection of climate and debt vulnerability is not limited to PRGT-eligible countries. Several lower- and upper-middle-income countries have high climate vulnerability according to the Notre Dame-GAIN Climate Vulnerability Index, and are encountering either serious challenges to their external debt sustainability or are already in debt distress.¹³ Vulnerability to climate shocks is also associated with higher borrowing costs, as creditor perceptions of greater country risk drives risk premia.¹⁴

On the climate mitigation side, developing countries also face greater financing needs associated with the transition to a low-carbon economy, which could further increase debt levels and exacerbate fragile external positions in the short run. Many developing countries are more reliant on brown activities, with less diversified economies.¹⁵ Consequently, the needs for investment in climate mitigation and other green activities as well as in economic diversification are much higher. Closing the investment gap will require increases in external finance, including debt, which will exacerbate their fragile external positions. At the same time, a global green transition could mean that demand for and the product prices of emission-intensive sectors

Figure III.E.11

LDCs and other LICs: External debt distress ratings, 2007–2023
(Percentage of countries)



Source: IMF staff calculations based on IMF/World Bank Debt Sustainability Framework.

Note: Data as of 30 November 2023.

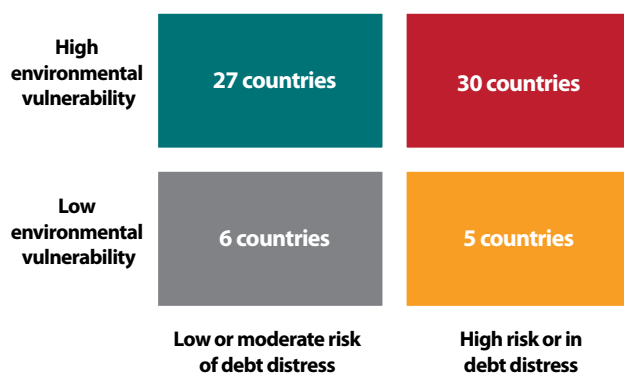
will fall, with adverse implications for the foreign currency revenues of countries that rely on these sectors and their capacity to service external debt burdens.

To break this debt-climate vicious cycle, an ambitious policy agenda at national and international levels is imperative. This agenda should encompass policy recommendations that are discussed throughout this report and noted below—across the action areas of the Addis Agenda. The policy agenda must include the scaling up of affordable international climate finance alongside increases in domestic public and private capital. Smart ways of leveraging domestic and international capital will be needed to help countries achieve the SDGs and climate goals. The size of the financing requirements implies that vulnerable developing countries will need external financing, and on concessional terms, to adapt and build resilience to climate change and avoid further debt build-up (see chapter III.C).

3.2 Scaling up SDG investments while maintaining sustainable debt

High debt service burdens and large unmet financing needs for the SDGs underline the need for progress across the action areas of the Addis Agenda. Creating fiscal space for investment in the SDGs in this very challenging macro-context will require policy action in many areas beyond debt: strengthened fiscal management (increased domestic public resource mobilization and efficient spending) (chapter III.A); development of domestic debt markets that can contribute to financial resilience and help to mitigate exchange rate risks at a time of tightening external conditions (chapter III.B); scaled-up concessional financing, which is particularly important for the poorest and most vulnerable countries (chapter III.C); but also domestic and international macroeconomic and capital account management to address external pressures (chapter III.F). Section 4 discusses the role of debt management and debt transparency

Figure III.E.12

Overlap of debt and climate vulnerabilities in LDCs and other LICs, 2023

Source: UNCTAD Secretariat calculations based on IMF LIC DSA country list (November 2023) and Notre Dame Gain Climate Vulnerability Index (ND-GAIN).

Note: Among the 70 countries currently PRGT-eligible, data is not available for two countries (Eritrea and Kiribati).

in preventing debt crises and efforts to close gaps in the debt resolution architecture so that crises can be addressed more speedily and effectively when they do occur. At the same time, there have been more targeted efforts and proposals to provide affordable debt financing for SDG and climate investments, both through specific instruments and more programmatic approaches.

SDG-linked debt instruments

Large financing needs for climate action and the SDGs have increased interest in financial instruments that more closely link debt financing to sustainability considerations. Such instruments aim to exploit (public and private) creditors' interest in supporting global priorities such as climate action and the SDGs.

For countries that remain solvent but struggle with limited fiscal space for investment in sustainable development, a range of debt instruments could help to mobilize resources for SDG and climate investments. Debt-for-climate and debt-for-SDG swaps allow countries to redirect debt service payments toward investments in sustainable development and climate action. They are useful for countries that have limited fiscal space for SDG investments, but are not a means to restore debt sustainability in countries with solvency challenges. There have been many debt-for-health and debt-for-nature swaps since the late 1980s; after a hiatus, they have regained popularity since 2015. Included in this are bilateral official debt swaps and more complex instruments that involve third parties providing funds with credit enhancements in order to buy back commercial debt at a discount.

Despite some successful examples, the uptake of debt swaps has remained limited, partly due to high transaction costs. Countries have to overcome a number of challenges, including capacity gaps, reporting and monitoring requirements, and the difficulty in identifying potential transactions alongside finding creditors willing to engage in such swaps. Additionally, limited market size can constrain the feasibility of issuing thematic bonds as part of large debt swap operations. Their design

must also assure sovereignty and country ownership over the investments undertaken. Several regional and thematic debt swap initiatives are advancing on these issues, including, for example, the United Nations Economic and Social Commission for West Africa's Climate/SDGs Debt Swap—Donor Nexus Initiative.

The past two decades have seen increasing interest in thematic bonds such as sustainability bonds (e.g. green, blue, social) and sustainability-linked bonds (SLBs). Sustainability bonds are “use-of-proceeds” bonds that aim to finance earmarked green or sustainable activities. SLBs tie the cost of borrowing to improvements from issuers on predefined sustainability indicators within a specific time frame. Since Poland's first issue of sovereign green bonds in 2016, sovereign issuance of bonds to fund decarbonization goals has expanded significantly, reaching \$80.8 billion in 2022.¹⁶ To date, European sovereigns account for most issuances, with developing countries accounting for \$4.1 billion of the 2022 total.¹⁷ The sovereign SLB market is still at a nascent stage, with Chile issuing the first SLB in March 2022.

The purpose of the issuance of sustainability and SLBs should be well defined and integrated into a sovereign's debt management strategy and issuance plans. Commonly cited objectives for sustainable debt issuance include: (i) raising the issuer's profile in the global arena; (ii) building markets for sustainable debt instruments inside a country; and (iii) accessing cost-effective funding and diversifying the investor base. The cost-effectiveness of thematic bonds depends on the size of the so-called greenium, that is, the difference in yields between thematic bonds and conventional sovereign bonds. Despite the growth of the market, the greenium has remained small—from 2.74 basis points for developed countries' bonds to 11.55 basis points for developing countries' dollar- and euro-denominated bonds.¹⁸ The cost savings are thus not on a scale that would make such bonds a suitable instrument for countries that already have high debt levels and that face high spreads in global markets. Countries must also take pre- and post-issuance costs associated with sustainable bonds into account, as well as the costs (and potential benefits) associated with changes to government operations that are needed to issue such bonds.¹⁹ In countries that continue to have borrowing space, donors could consider supporting the issuance of SLBs, for example, by providing support to the development of localized standards and guidelines, or providing a grant element or a guarantee, essentially allowing them to furnish a form of budget support for SDG-linked investments.²⁰

Programmatic approaches

There have also been calls for more systematic support for countries that are not insolvent, but face liquidity pressures over the next several years that are obstacles to investing in recovery, the SDGs and climate action. As noted earlier in this chapter, external debt service burdens are elevated for many developing countries, particularly LDCs, LICs and lower-middle-income countries. While many of them may not need or wish to restructure because they remain solvent, liquidity constraints inhibit their ability to invest in the SDGs, climate action and recovery. Several proposals have been made to provide stepped-up and systematic support to such countries. For example, there have been proposals for a new generation of adjustment programmes that would combine additional new financing from international financial institutions and suspension of principal repayments—a “debt pause”—to avoid leakage of

funds (essentially, the use of highly concessional donor resources to service less-concessional debt) in exchange for a commitment by debtor countries to engage in investment-focused structural reforms that put them on a new and sustainable growth path²¹ (see box III.E.1 for the historic example of the Republic of Korea and an investment-focused debt strategy). Such an approach also falls within the spirit of proposals put forward by the United Nations Secretary-General in the SDG Stimulus and his policy brief on international financial architecture reform, to scale up long-term, affordable financing for SDG and climate investments, while addressing high sovereign borrowing costs and rising risks of debt distress (box III.E.2).

4. Debt crisis prevention and resolution: Progress made and challenges ahead

Amid rising debt vulnerabilities, improvements are needed in both debt crisis prevention and resolution. Both domestic efforts and international actions are needed to create fiscal space for sustainable development investments, address liquidity challenges, mitigate systemic risks and support quick and fair debt restructurings when necessary. In addition to improved debt management and transparency, continued progress towards an architecture that allows for more effective and fair restructurings remains critical, particularly in view of a more heterogeneous creditor landscape, greater reliance on commercial finance, especially by LDCs and other LICs, and geopolitical uncertainty.²² The current architecture needs continued improvement to deliver on all of these objectives.

4.1 Debt crisis prevention

Further strengthening public debt management and advancing public debt transparency are key to mitigating the risk of debt crises.

Debt management and capacity support

Rising debt coupled with a more complex debt landscape have underscored the importance of sound public debt management.

The increased heterogeneity of the creditor base and complexity of debt instruments (see section 2 above) have posed significant challenges for public debt management. While fiscal policy is the primary determinant of public debt levels, effective public debt management is a critical component of sound macroeconomic policies. Effective debt management helps to minimize debt vulnerabilities, promote stable access to financing and support the development of a more resilient domestic financial sector, while ineffective management can generate significant fiscal costs and propagate crises. To be effective, public debt management requires a clear mandate built on a sound legal and institutional framework, appropriate human resources and information technology, good governance, political support and effective coordination with other (particularly fiscal and monetary) policies. Another key priority for domestic debt has been the development and deepening of domestic markets, including increased liquidity and more predictable and transparent debt issuances.²³

Steady progress has been made in public debt management practices. Debt Management Performance Assessments have been carried out in 69 developing countries over the past decade. These countries, which

have developed and are pursuing debt management strategies, document improvements in areas such as the legal framework, managerial structure, quality of the debt strategy, publication of statistical bulletins, coordination with the central bank, documented procedures for domestic market borrowing, and staff capacity. Improvements to information technology (IT) systems for debt recording and management are under way across a growing number of countries. However, accomplishments have been slow in other areas and have occasionally faced setbacks, such as during the pandemic. Fragile and conflict-affected States and small developing countries face particularly strong resource constraints, both in terms of staffing and physical/IT equipment. Capacity development in public debt management will remain gradual and—in many contexts—rely heavily on external support.

The IMF and the World Bank provide technical assistance to LICs and MICs through various means, including through the jointly administered Debt Management Facility. The Debt Management Facility programme, which was launched in 2008 by the World Bank, offers advisory services, technical assistance, training and peer-to-peer learning to 86 developing countries. This assistance covers Debt Management Performance Assessments, reform plans and support for strengthening debt management institutions and functions as well as the design of debt management strategies and the development of domestic markets. Additionally, the Government Debt and Risk Management programme provides customized advisory services to enhance public debt and risk management capacity in select MICs. In recent years, delivery of debt management capacity development to LICs has been further enhanced by a growing network of regional advisors located in Regional Technical Assistance Centres, which help the IMF to be responsive to emerging authority needs, including tailoring capacity development to regional challenges and providing sustained on-the-ground support.

The United Nations Conference on Trade and Development (UNCTAD) supports 60 developing countries in building effective debt management capacity, focusing on downstream aspects of debt recording, monitoring and reporting. These efforts complement the technical assistance provided in upstream areas. The UNCTAD Debt Management and Financial Analysis System Programme assists in ensuring the availability of high-quality debt data for reporting and decision-making, enhancing the accuracy and completeness of public debt records and facilitating comprehensive and timely reporting. It also assists in the implementation of debt reorganization initiatives.²⁴ In addition to the UNCTAD programme, there have been other downstream initiatives, including one from the Commonwealth Secretariat that supports developing countries through Meridian, its Debt Recording and Management System.

Debt transparency

In light of increasing public debt vulnerabilities, ensuring debt transparency remains a priority. Transparency is crucial to ensure that governments make informed borrowing decisions based on a comprehensive view of the entire public sector's debt burden and debt-related fiscal risks. Transparency fosters investor confidence and better cooperation with lenders, ultimately increasing the availability of resources and lowering the cost of funding. It also enhances accountability by allowing the public to monitor how public debt is managed. Despite its importance, debt is sometimes incompletely reported in official statistics or hidden through

Box III.E.1**Republic of Korea's strategy to avoid debt distress during economic take-off**

During its economic take-off from the 1960s to the 1980s, the Republic of Korea encountered development financing challenges that are common to developing countries, including persistently high current account deficits, fast-accumulating external debt and low tax revenue. As was the case with many of its peers at that time, development assistance and concessional loans during the cold war era partially mitigated development financing gaps in the country. However, what distinguished the experience of the Republic of Korea was its ability to leverage financing for rapid and sustained development while effectively managing its debt sustainability risks.

A key factor behind the country's success was its emphasis on the productive investment and efficiency criterion for debt-financed development—that is, the marginal economic productivity of its investment had to be higher than the real interest rate payable on the borrowing. The Government of the Republic of Korea played a central role in enforcing this principle through both its own spending decisions and its oversight of the economy. It helped to ensure that development assistance and external debt did not fund short-term consumption, wasteful investment or private capital flight, but instead primarily financed productive investment and increased foreign exchange reserves.

The country's investment ratio more than tripled, from 9.6 per cent of GDP in the late 1950s to 32.2 per cent in the 1970s, while the marginal productivity of capital was maintained at levels that were well above real interest rates paid on foreign debt. Sustained high real economic growth, averaging 8.3 per cent between 1961 and 1980, contributed to keeping the country's debt burdens manageable. For example, if the Republic of Korea had achieved only a 5 per cent growth rate, its foreign debt-to-GDP ratio would have approached 90 per cent of GDP at the beginning of the 1980s, compared to less than the 50 per cent of GDP that was reported. The country's strong economic performance supported growing public revenues and domestic savings, reducing the need for excessive public or external borrowing.

To enforce this successful debt strategy, the Government strengthened institutions and employed a host of policies: a credible, consistent and coherent economic development blueprint as the cornerstone of its national investment and associated debt strategy; productive investment as the top priority throughout its economic take-off; and centralized appraisal of investment and borrowing to ensure the productive and efficient use of funds in both the public and private sectors. The Government also maintained excellent debt statistics throughout the period, which played an important role in supporting informed decision-making.

Source: UN ESCAP.

the use of overly broad confidentiality clauses.²⁵ Since 2018, the Joint IMF-World Bank Multipronged Approach to Address Debt Vulnerabilities has emphasized the importance of public debt transparency, while tracking progress and supporting a broad set of initiatives that are ongoing.

Transparency in debt is also indispensable for facilitating efficient debt restructuring. Accurate and comprehensive debt data is essential for estimating the level of debt relief required to restore a borrower's debt sustainability. Moreover, only maximum disclosure can foster the trust necessary for creditors to achieve equitable burden-sharing. Where accurate information is not readily available, debt reconciliation may lengthen the restructuring process with detrimental costs on the borrower's economy.

Enhancing transparency is the shared responsibility of both borrowers and creditors. Borrowers should strengthen their legal frameworks and improve their debt recording and reporting systems as well as capacity and information-sharing procedures to enable timely and comprehensive reporting. Creditors should encourage transparent financing practices and provide detailed information about their lending portfolios, which can fill in gaps in borrowers' statistics. They should also refrain from including confidentiality clauses in their loan contracts. As the *Financing for Sustainable Development Report 2022* noted, improved reporting and transparency, along with more robust credit analysis, could decrease uncertainty and enhance the effectiveness of debt markets, potentially leading to lower borrowing costs for countries. In this context, the role of credit rating agencies, which supply markets with information and credit assessments and can incentivize disclosure through their rating methodologies, is also important.

Borrowers have made progress in debt reporting, although numerous challenges persist. A review of 60 developing countries found

that less than half require the preparation of key debt-related publications in their domestic legal framework.²⁶ In practice, across the countries eligible to borrow from the World Bank's International Development Association (IDA), 23 per cent do not disclose any debt data, a significant improvement from 40 per cent three years ago. The World Bank debt reporting heatmap has shown the impressive progress some countries have made on debt disclosure.²⁷ Such efforts by borrowers were supported by the IDA's Sustainable Development Finance Policy introduced in 2020, which led to the implementation of over 400 performance and policy actions across more than 60 countries in areas related to debt transparency, debt management and fiscal sustainability. However, progress has been uneven, with some countries regressing in their debt reporting standards due to inadequate debt recording and reporting systems, weak legal and institutional frameworks, or insufficient capacity.

Reporting by creditors on their lending has been mixed. Key bilateral creditors articulated the importance of lender reporting in the Principles and Operational Guidelines for Sustainable Financing adopted by the G20 in 2017. Since then, the Group of Seven (G7) countries have started publishing details of every official sector loan to sovereigns on government websites, although the level of detail varies considerably. The Institute of International Finance published Voluntary Principles designed to enhance transparency in private sector lending in 2019. Subsequently, the OECD's Debt Transparency Initiative built a repository for Institute of International Finance members to disclose their loans to developing countries. However, to date, very few private banks have disclosed any loans.

International organizations can also help to strengthen the coordination of and simplify reporting processes. There is a range of global databases on debt with varying degrees of coverage and data

disaggregation. The World Bank's International Debt Statistics, which is the most comprehensive database for external debt, has significantly increased the comprehensiveness of its coverage, in part due to a new lending policy that promotes the disclosure of public debt data and the reconciliation undertaken with several key creditors.²⁸ Exploring innovative IT solutions which automate data exchange and validation between creditors and borrowers could potentially improve the quality and scope of existing data and greatly simplify reporting efforts.²⁹ Capacity-building support will remain critical. The IMF and the World Bank have stepped up efforts to provide capacity development support with activities, including training courses, that aim to: (i) enhance reporting of public debt data in official publications and investor relations functions; (ii) produce and publish medium-term public debt management strategies and annual borrowing plans; (iii) strengthen legal frameworks and institutional capacity in creditor and debtor countries to support public debt transparency; (iv) improve coverage of contingent liabilities and systematically track lending commitments as well as disbursements; (v) strengthen cash management; and (vi) improve management of fiscal risks.³⁰

Linking debt service to countries' capacity to pay in the face of exogenous shocks

State-contingent debt instruments can serve as a countercyclical and risk-sharing tool to help countries deal with shocks.

State-contingent debt instruments have payouts that are higher in good states than in bad states. They aim to reduce debt payments during periods of low fiscal revenue—for example, by tying debt payments to GDP, commodity prices or catastrophic events—thus creating countercyclical liabilities linked to the sovereign's debt-service capacity. These clauses provide insurance against exogenous risks and may become increasingly important given growing climate risks and other environmental concerns. The G20 Debt Service Suspension Initiative aimed to provide such breathing space to LICs to tackle the pandemic-related economic fallout. But the suspension initiative required each borrower and creditor to agree on debt contract modifications in lengthy processes that proved burdensome for both creditors and borrowers. State-contingent clauses provide an ex ante solution.

Public creditors are pioneering climate-resilient debt clauses in their lending. Climate-resilient debt clauses automatically defer debt payments following the occurrence of certain climate events and natural disasters (such as droughts, earthquakes, flooding and extreme weather). The Inter-agency Task Force has long called on official creditors to take the lead in adopting such clauses in their lending; now several official creditors (the African Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank, the World Bank, Canada, the United Kingdom and France) have committed to do so. Before that, similar clauses had only been introduced in the context of restructurings, for example, in bond contracts by Barbados and Grenada, deferring repayment obligations in case of natural disasters.

4.2 Debt crisis resolution

Amid rising debt vulnerabilities, the international debt architecture needs to be strengthened so that it can efficiently and effectively help countries to restructure unsustainable debt in a timely manner. This improvement would help to prevent delays in debt

restructurings that can lead to significant development setbacks. When restructuring episodes following a default last longer than the median duration, the average cumulative loss in GDP is estimated to be around 26 per cent relative to the GDP of the year before the restructuring, over the first five years after a country defaults.³¹ In contrast, when restructuring episodes are expected to be shorter than the median duration, they are associated with an average cumulative GDP increase of 2.8 per cent compared to the pre-restructuring year's GDP, over the same time frame. There are also significant social costs associated with delayed debt restructuring, such as prolonged, reduced social spending and its consequences for human development that result from reduced economic output and government revenue.

Strengthening debt analytics

Timely recognition of debt sustainability problems is critical to support debt restructurings when they are needed. As part of its mandate to foster economic and financial stability, the IMF plays a central role in the prevention and resolution of sovereign debt crises. The core functions of the IMF are to: (i) conduct surveillance of its members' policies for systemic stability, including through debt sustainability analyses prepared jointly with the World Bank for those countries using the IMF-World Bank Debt Sustainability Framework for Low-Income Countries; (ii) assist members in solving their balance-of-payments problems through IMF-supported programmes to restore the member's medium-term external viability, and (iii) in particular, in cases of unsustainable debt and a request for an IMF-supported programme, assist the member in designing a macroeconomic adjustment framework and establishing the debt restructuring envelope that is necessary to put debt on a sustainable path while being consistent with the IMF-supported programme's parameters.³² The World Bank offers low-interest loans and grants to developing countries, customizing financing terms according to their debt vulnerabilities. It extends substantial positive net flows to countries facing debt distress, including during debt restructuring, and provides grants to the poorest among them.

The IMF and the World Bank continue to strengthen the analytical tools to assess debt sustainability. In most LICs, debt sustainability assessments are carried out using the joint IMF-World Bank Debt Sustainability Framework for Low-Income Countries. For all other countries the IMF uses the Sovereign Risk and Debt Sustainability Framework for Market Access Countries (MAC SRDSF).³³ The assessment framework for market access countries was revamped in 2021 and has since been rolled out. The new SRDSF signals sovereign stress more accurately and better assesses debt sustainability in market access countries than the previous version, which is a prerequisite for lending by most international financial institutions. In October 2023, the IMF published the SRDSF template for public use. In late 2023, a review of the IMF-World Bank Debt Sustainability Framework for Low-Income Countries was launched to formally assess the effectiveness of the existing framework and re-examine its fundamental features. The review is expected to be a multi-year process. In the interim, a supplementary guidance will be prepared in 2024 to address some of the most pressing issues within the existing framework. There have also been efforts by other stakeholders to develop complementary tools and frameworks, each emphasizing different facets of debt sustainability.

More efficient information-sharing can help to support effective sovereign debt restructurings. Difficulties such as asymmetric

Box III.E.2**The SDG Stimulus and reform of the international financial architecture**

In his proposals for an SDG Stimulus and reform of the international financial architecture, the United Nations Secretary-General put forward proposals for both immediate actions to address the debt challenges of developing countries and for longer-term reforms of the sovereign debt architecture that the Fourth International Conference on Financing for Development could address. These proposals aim to strengthen debt crisis prevention, alleviate fiscal constraints for countries that face extremely high debt service burdens and elevated borrowing costs, and address continued challenges in effectively and fairly resolving sovereign debt crises when they occur.

Recommendations to prevent debt crises from occurring include the following: fulfilling the long-standing commitment of the international community to work towards a global consensus on guidelines for sovereign debtor and creditor responsibilities; improving debt management

and debt transparency, such as by developing a publicly accessible registry of debt data for developing countries; enhancing the information environment and understanding of long-term debt sustainability and SDG financing needs, which can build on ongoing work in the United Nations and beyond; and improving debt contracts and increasing the use of state-contingent debt instruments.

In regard to debt crisis resolution, the Secretary-General proposed strengthening the Common Framework by complementing it with a mechanism that could help to overcome creditor coordination challenges with both sticks and carrots to enforce and incentivize private creditor participation in restructurings for comparable treatment with official creditors. Such a mechanism could also be open to countries with liquidity challenges, helping them to refinance existing high-cost market debt without excessive compensation to private creditors.

Source: UN DESA based on: “United Nations Secretary-General’s SDG Stimulus to Deliver Agenda 2030” and United Nations, “Our Common Agenda Policy Brief 6—Reforms to the International Financial Architecture”.

information and a lack of common understanding and coordination amid creditor fragmentation can impede timely resolution of debt restructurings. Such delays further discourage countries that could benefit from debt restructuring from resorting to it in a timely manner. As part of efforts to support an effective process, including reducing information asymmetries, the IMF and the World Bank have published guidance to staff on information-sharing in the context of sovereign debt restructurings.

Evolution of contractual approaches

In the late 1990s and early 2000s, the international community confronted the difficult prospect of sovereign defaults on bonds held by the private sector. Unlike debt defaults and restructurings during the 1980s debt crisis, which primarily involved the restructuring of syndicated loans held by foreign banks, sovereign bonds were widely held by hundreds, and sometimes thousands, of bondholders, making the “collective action problem” inherent in all restructurings decidedly more difficult.

Although a supranational sovereign bankruptcy mechanism (i.e. the Sovereign Debt Restructuring Mechanism) was proposed in 2001 as a statutory means through which sovereign debt crises could be resolved,³⁴ this proposal did not garner sufficient political support. Instead, a contractual—or “market-based”—approach to sovereign debt restructuring was relied on.³⁵ The market-based approach included incorporating contractual provisions in sovereign bond contracts to help facilitate negotiations between the debtor and its creditors in restructuring agreements. A notable example are collective action clauses (CACs) that facilitate orderly debt restructuring by relying on qualified majority voting by creditors. The uptake of enhanced CACs continues to be high, with 92 per cent of new issuances of international sovereign bonds between June 2020 and December 2022 including such clauses. As of December 2022, 70 per cent of the outstanding stock of bonds included enhanced CACs.

Over a dozen sovereign debt restructurings of private claims were completed between 2014 and 2020 relying on the contractual

approach, but a number of issues remain and threaten to complicate future restructurings. Compared with previous periods, restructurings between 2014 and 2020 generally proceeded more smoothly, were largely pre-emptive and had a shorter average duration and higher average creditor participation, mainly due to the use of CACs. However, sovereign debt restructurings in a few LICs were protracted, incomplete and non-transparent. There have also been more serial restructurings as a result of shallow haircuts.³⁶

New coordination challenges have arisen as the creditor base has become more varied and fragmented. The use of collateral and collateral-like instruments has increased and complicated the reaching of agreement in recent restructurings. Secured creditors may have the ability to seize collateral, attach dedicated revenue streams (for example, relating to oil or natural gas) or draw on amounts deposited in escrow accounts. This leverage puts a ceiling on the amount of debt relief that can realistically be negotiated and leads to particularly acute inter-creditor equity concerns. In addition, informational asymmetries may complicate reaching a restructuring deal given the lack of a clear understanding as to the restructuring perimeter and classification of claims. Creditors may be unwilling to agree to a deal without clarity on those issues given inter-creditor equity concerns.

Domestic law approaches

Several jurisdictions have discussed or advanced efforts in domestic law to help resolve debt crises more effectively. There are several examples of initiatives introduced in the past decade that aim to restrict creditor actions in specific circumstances. In 2010, the United Kingdom passed the *Debt Relief (Developing Countries) Act* (“2010 Act”),³⁷ which limited the recoverable amounts for creditors of countries participating in the HIPC Initiative. At the time, it prevented an estimated loss of £145 million for these countries,³⁸ which otherwise might have accrued due to holdout litigation. In 2015, Belgium implemented legislation that restricts the rights of creditors in relation to debtor countries by limiting their claim to the amount they initially paid to

acquire the debt.³⁹ This law specifically targets situations where creditors seek unjust benefits after purchasing claims on the debtor country at a discounted price on the secondary market. In 2016, France enacted a law that protects certain developing countries from having their assets seized by creditors who bought debt when the debtor countries were in, or near, default.⁴⁰ The law offers protection for the first four years following a default, or if two thirds of the holders of the debt have accepted a restructuring.

More recently, there have been efforts to introduce relevant legislation in the United Kingdom and the United States of America, where most sovereign debt contracts are governed. In the United Kingdom, the International Development Committee of the Parliament issued a recommendation to introduce legislation compelling private creditor participation in international debt relief initiatives, although the bill was rejected.⁴¹ Three legislative bills were previously considered in the New York State Assembly, which envisage establishing a sovereign bankruptcy procedure in New York,⁴² limiting the recoverable amount for creditors in New York courts⁴³ and voiding debt transfers acquired for the purpose of filing lawsuits.⁴⁴ In early 2024, new draft legislation that combines two of the three aforementioned proposed bills was submitted to the New York State Assembly. This new proposed bill would limit the recoverable amount for creditors to what the United States Government would receive if it were a creditor holding an eligible claim, or allow debtor countries to submit their own restructuring plans through the New York courts.⁴⁵

Domestic debt restructurings

Rising debt vulnerabilities and the growing share of domestic debt have increased the risk of more domestic debt restructurings. Domestic currency public debt increased from 8 per cent of GDP in 2000 to 20 per cent of GDP in 2022 for LDCs and from 22 per cent of GDP to 37 per cent of GDP for other LICs, on a GDP-weighted averaging basis (see figure III.E.2 above). From 1990 to 2020, there were roughly 30 stand-alone domestic debt restructurings, compared to 27 external debt restructurings.⁴⁶ With more than half of all LDCs and other LICs at high risk of debt distress, domestic restructurings may be needed more frequently to restore debt sustainability.

While domestic debt restructurings avoid certain costs involved in external debt restructurings, they also pose unique challenges.⁴⁷ Sovereigns have considerable flexibility in restructuring domestic debt, including through changes in domestic laws, as a result of which domestic restructurings typically take less time to conclude. Domestic debt restructurings can also potentially limit the external reputational costs and help to retain external market access. At the same time, because domestic debt is disproportionately held by domestic banks and pension funds, sovereign stress can easily spread to other parts of the economy, with potentially serious adverse effects on the economy. A restructuring of central bank holdings of public debt can adversely affect the central bank's position to conduct monetary operations and regulatory functions. Thus, domestic debt restructuring should be designed to achieve the necessary debt relief while minimizing risks to the domestic financial system and broader economy; a decision framework to identify options that minimize potential economic costs, including financial system disruptions, was presented by the IMF to this end in 2021.⁴⁸

The global architecture

Recent actions taken by the creditor community in regard to the debt challenges faced by developing countries bear some similarities to the responses of the late 1980s and 1990s, but differ in important respects, reflecting the difference in circumstances.⁴⁹

While debt distress indicators in LICs have steadily risen over the last decade, they remain substantially below their levels in the mid-1990s and do not yet indicate a systemic crisis of the type that would require a wholesale, coordinated HIPC-style initiative. As a result, the post-2019 efforts of the creditor community have first focused on rolling out the G20 Debt Service Suspension Initiative to provide immediate cash-flow relief to eligible countries through extended rescheduling and reprofiling of debt. In a second stage, the G20 Common Framework was put in place to provide deeper relief for qualifying countries that request treatment on a case-by-case basis. While creditors have moved faster this time to consider deeper debt treatment, many challenges remain.⁵⁰

Several areas of improvement have been highlighted to strengthen the Common Framework to deliver more quickly.⁵¹ The IMF and the World Bank have highlighted the need for: (i) greater clarity on the steps and timelines of the Common Framework process, enabling the early resumption of essential financing and support for the implementation of a reform programme; (ii) introduction of a debt service suspension for the duration of the negotiation to alleviate liquidity constraints, avoid the accumulation of arrears and incentivize quicker resolutions; (iii) clarity on the parameters and processes to assess and enforce comparability of treatment; and (iv) expanding coordinated debt treatments to highly indebted non-Common Framework-eligible countries that would benefit from such coordination, as they are recipients of large financing from both official and private sector creditors. These calls have been echoed by the Inter-agency Task Force and complemented by additional recommendations. These include recommendations by the Secretary-General in his policy brief on reform of the international financial architecture, which proposed the development of a mechanism that could help to overcome creditor coordination challenges with both credit enhancements (or other carrots) and sticks to ensure comparable treatment of private creditors (see box III.E.2 above).

The Global Sovereign Debt Roundtable (GSDR) is aimed at promoting common understanding among key stakeholders. The GSDR was set up in February 2023 and is co-chaired by the IMF, the World Bank and the G20 Presidency. The GSDR focuses on processes and practices to foster common understanding of key bottlenecks and ways to address them. Participation in the GSDR is broad-based and includes official bilateral creditors, private creditors and borrowing countries. Both traditional creditors such as the Paris Club and new official bilateral creditors have attended its policy meetings and workshops. In October 2023, the GSDR issued a progress report, welcoming the positive momentum in resolving individual debt restructuring cases and reaching common understanding on ways to address key impediments to debt restructuring.

Enhanced international collaboration and further improvement in the global debt restructuring architecture remain important, and bolder reforms can be contemplated should the current liquidity squeeze morph into a more systemic crisis. A strengthened Common Framework can provide an efficient, rules-based framework for

sovereign debt resolution that ensures timely, orderly, effective and fair debt restructurings. However, in its current format, it may not be well equipped to tackle widespread debt distress in a systemic crisis. The current architecture also has gaps in addressing the “development dimension”

of the current debt crisis, with no systematic support available to countries whose high debt service burdens hamper SDG expenditure. To close these gaps, UNCTAD has put forward proposals towards a development-centred sovereign debt workout framework (box III.E.3).

Box III.E.3

UNCTAD proposal for a global debt authority

A sovereign debt workout framework that is development-centred would combine contractual and statutory approaches. This would include: provisions noted above, such as automatic standstills for countries declaring distress to prevent holdouts and encourage debtor countries to not delay initiating the restructuring process; enhanced debt sustainability analyses to reflect the need to achieve the SDGs and climate transition, as well as empower country negotiators with improved data on the potential for growth and fiscal consolidation, including models from developing countries themselves; improving innovative financial instruments such as debt-for-climate swaps or debt-for-nature swaps that can enhance the fiscal space of countries with sustainable debts; and the building of a broader institutional framework that fosters sovereign debt resilience in the face of pressing ecological, social and geopolitical challenges, for example, through mechanisms such as the Loss and Damage Fund.

Additional institutional changes include mechanisms to: determine the perimeter of legitimate debt (relating to rules regarding unconstitutional debt resulting from corruption, opacity, secrecy and flawed authorization or reckless creditor practices); make capital controls and other regulations that affect capital flows key elements of the ordinary financial regulatory toolkit of developing countries; and establish a borrower’s club. Since 1956, official creditors have coordinated their efforts through institutions such as the Paris Club, while various private creditor groups also exist. A borrower’s club would enable debtor countries to discuss technical issues and the use of novel debt instruments (such as green bonds). It would also facilitate mutual learning and allow

countries with recent debt workout experience to advise those in distress. Such a club could lead to a more stable and resilient global debt architecture, benefiting both borrowers and creditors.

The most ambitious institutional initiative proposed by UNCTAD is the creation of a global debt authority to oversee sovereign debt workouts and implement the substantive changes listed above. While this endeavour seems largely aspirational in the current geopolitical space, progress could occur in at least two phases: In the first phase, the global debt authority would function as a coordinating and advisory institution operating under a non-binding charter adopted by a smaller group of interested countries. It would consist of a limited team of staff affiliated with an existing international organization and rely on ad hoc committees of experts who would identify existing sovereign debt-related issues and make recommendations for the global debt authority to provide guidance on soft law, domestic legislation and contractual approaches. Through the work of these ad hoc committees, the global debt authority would establish its network with experts, international institutions, domestic lawmakers and civil society groups, among others. Regarding sovereign debt workout data, global debt authority staff and ad hoc committees would develop and maintain databases of previous agreements, debt sustainability analyses and effective communication strategies. By undertaking these actions, the global debt authority would initiate its operations, build its network for further expansion and develop the resources to play a pivotal role in sovereign debt workouts. In a second phase, the legal basis for the global debt authority as an autonomous entity, neither borrower nor creditor, would be established.

Source: UNCTAD, *Trade and Development Report 2023*, chapter V.

Endnotes

- 1 LDCs and other LICs include 73 CF-eligible countries plus Eritrea, Sudan, and Zimbabwe.
- 2 The IMF and World Bank launched the HIPC Initiative in 1996, expanded it in 1999, and supplemented in 2005 by the MDRI to provide comprehensive debt relief to the poorest heavily indebted countries. By 2007, the average debt-to-GDP ratio of the 36 countries recipients of the full amount of debt relief under HIPC and MDRI fell by around 70 per cent, relative to the early 2000s.
- 3 UN DESA calculations, based on World Bank International Debt Statistics database.
- 4 The presence of collateral can raise the risk of debt distress by reducing budget flexibility (through the earmarking resources) and impairing access to non-secured financing, particularly after adverse shocks.
- 5 IMF (2020). “Reform of the Policy on Public Debt Limits in IMF-Supported Programs,” IMF Policy Paper 2020/061.
- 6 World Bank (2024). Global Economic Prospects January 2024.
- 7 The public debt dynamics equation can be expressed as:

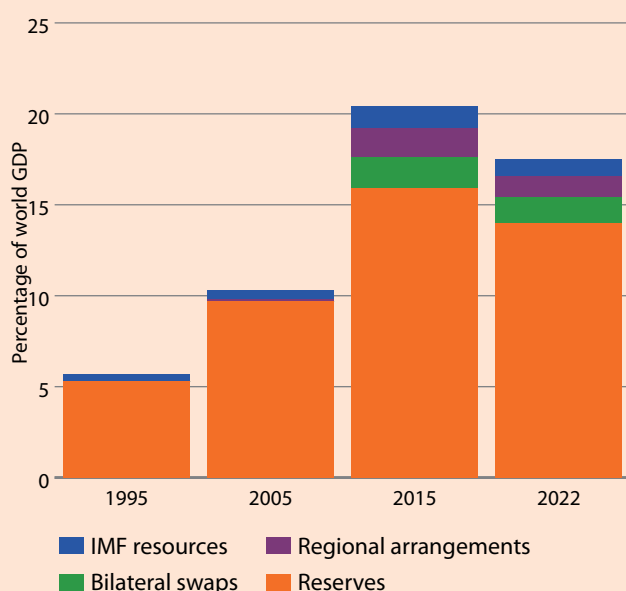
$$\Delta d_t = d_t - d_{t-1} = \frac{r-g}{1+g} d_{t-1} + \varepsilon(1+r^f) d_{t-1}^f - pb_t$$
 where d is public debt in percentage of GDP; r is the real interest rate on overall public debt; r^f is the real interest rate on FX-denominated external debt (deflated by US inflation); g is the real GDP growth; ε is the change in the real exchange rate, expressed in local currency per U.S. dollar unit (with $\varepsilon > 0$ indicating depreciation of the domestic currency), pb is the primary balance in percentage of GDP.
- 8 For more discussions on recent trends in developing countries’ access to concessional official development finance, see UNCTAD. (2024). *Trade and Development Report 2023: Growth, Debt and Climate: Realigning the Global Financial Architecture* (Trade and Development Report). UN Publishing.
- 9 UN Global Crisis Response Group. (2023). *A world of debt—A growing burden to global prosperity*. United Nations.
- 10 Alternative estimates that used data from multiple sources, including national budget or debt management documents and international sources have shown an even higher number of countries that spend more on debt service than on various social spending. See: Martin, M. (2023). *The Worst Ever Global Debt Crisis*. Development Finance International.
- 11 Massetti and Bellon. 2022. Planning and Mainstreaming Adaptation to Climate Change in Fiscal Policy. IMF Staff Policy Note 2022/03
- 12 Songwe V, Stern N and Bhattacharya A (2022). *Finance for climate action: Scaling up investment for climate and development*. Grantham Research Institute on Climate Change and the Environment. London School of Economics and Political Science.
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- 15 Magacho, G., Espagne, E., Godin, A., Mantes, A., and Yilmaz, D. (2023). Macroeconomic exposure of developing economies to low-carbon transition. *World Development*, 167:106231.
- 16 Data source: <https://www.climatebonds.net/market/data/#issuer-type-charts>
- 17 Ibid.
- 18 Ando, M. S., Fu, M. C., Roch, M. F., & Wiriadinata, U. (2023). *How Large is the Sovereign Greenium?* (No. 23/80; IMF Working Papers). International Monetary Fund.
- 19 While there are costs associated with changes in government operations, at least some of these changes, such as a move towards SDG budgeting and better reporting of government activities’ impact on SDGs, would create positive development impact.
- 20 OECD (2022). “Green, social, sustainability and sustainability-linked bonds in developing countries: How can donors support public sector issuances?” OECD Publishing, Paris.
- 21 Diwan, I., Kessler, M., & Songwe, V. (2024). *A bridge to climate action: A tripartite deal for times of illiquidity* (No. 14; Policy Note). Finance for Development Lab.
- 22 IMF (2022b). Macroeconomic Developments and Prospects in Lower Income Countries. November.
- 23 WB (2023a). ‘Domestic Debt Securities Heatmap.’
- 24 Debt reorganization can take many forms but includes debt assumption, debt payments on behalf of others, debt forgiveness, debt restructuring and rescheduling, debt conversions, and debt prepayments and buybacks.
- 25 WB (2021). Debt Transparency in Developing Economies; and IMF (2023) Making Public Debt Public.
- 26 IMF (2023). Making Public Debt Public. This study highlighted the following areas for improvement: (i) strengthening domestic legal frameworks for public debt, including borrowing authorization, reporting, and related accountability mechanisms; (ii) standardizing clauses that promote transparency in public debt contracts; (iii) putting in place frameworks for disclosure and reconciliation of loan-level information by borrowers and creditors; and (iv) introducing direct incentives from IFIs. Concrete achievements in these fronts will take time and resources. The country classifications of emerging market and developing economies as well as low-income countries adhere to the IMF country classification.
- 27 WB (2023b). ‘Debt Reporting Heatmap.’
- 28 WB (2022). ‘International Debt Report’.
- 29 For discussion of a proposal of digitalizing loan transactions through an international loan repository, please see: UNCTAD. (2024). *Trade and Development Report 2023: Growth, Debt and Climate: Realigning the Global Financial Architecture* (Trade and Development Report). UN Publishing.
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- 43 Assembly Bill A2970 / Senate Bill S4747
- 44 Assembly Bill A5290 / Senate Bill S5623.
- 45 Assembly Bill A2970A / Senate Bill S5542A.
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- 48 Ibid.
- 49 C. Chuku *et al* (2023). 'Are We Heading for Another Debt Crisis in Low-Income Countries? Debt Vulnerabilities: Today vs the pre-HIPC Era,' IMF Working Paper WP/23/79.
- 50 Rivetti, D. (2022). Achieving comparability of treatment under the G20's Common Framework. *Equitable Growth, Finance and Institutions Notes*, Washington, DC: World Bank Group.
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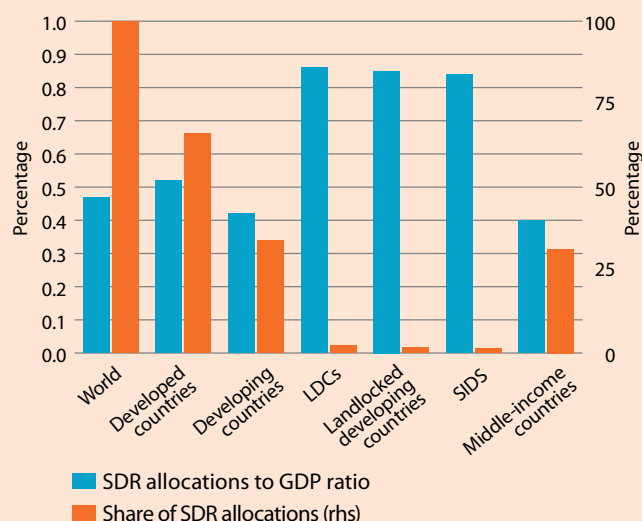


Addressing systemic issues *in numbers*

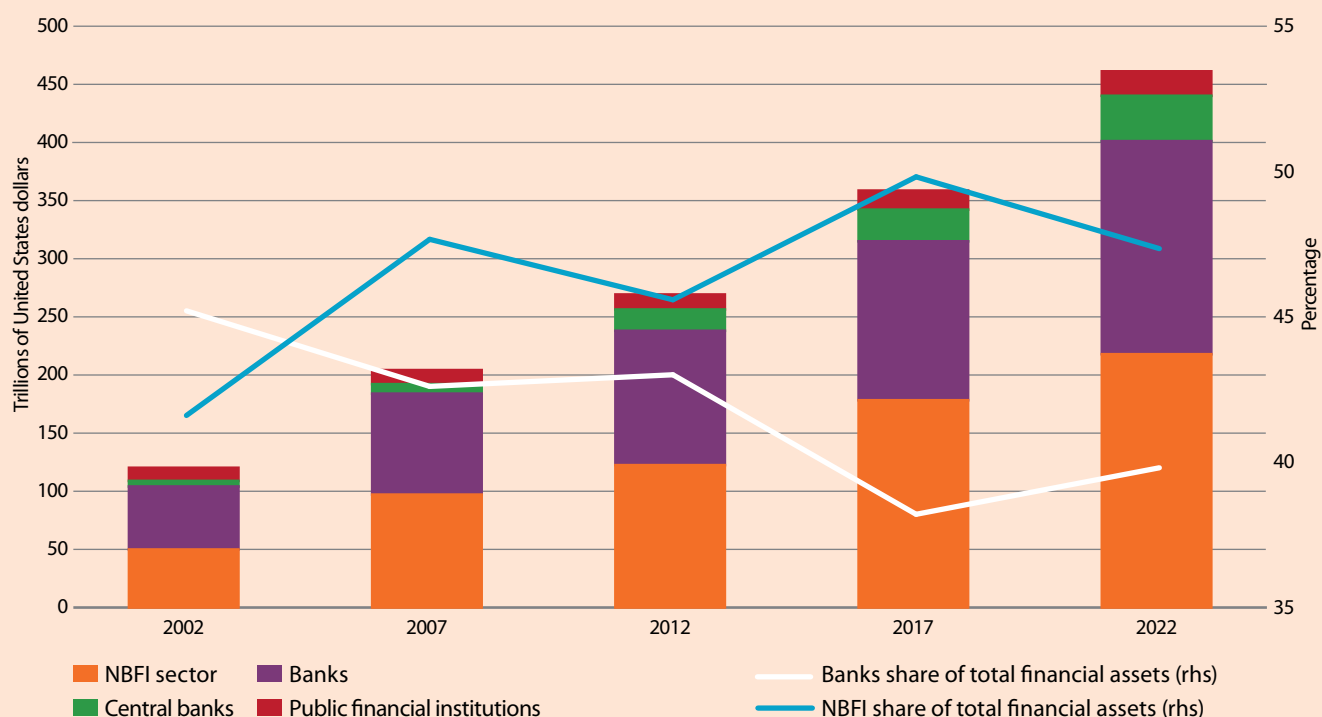
The global financial safety net has grown to over 17.6% of world GDP, but recent crises have revealed gaps in the architecture and uneven coverage



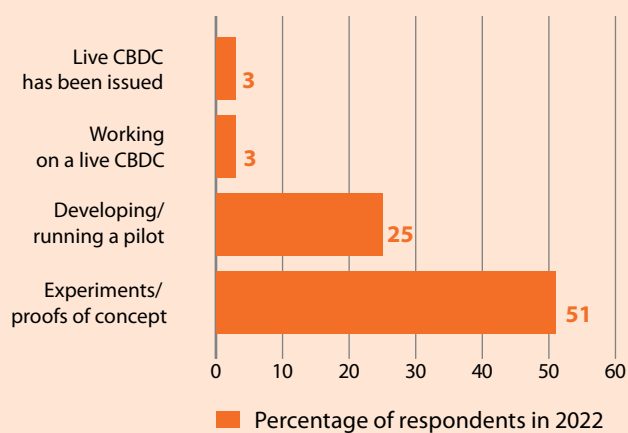
Developing countries received around one-third of the \$650 billion 2021 allocation of special drawing rights, which represented 0.42 per cent of their GDP.



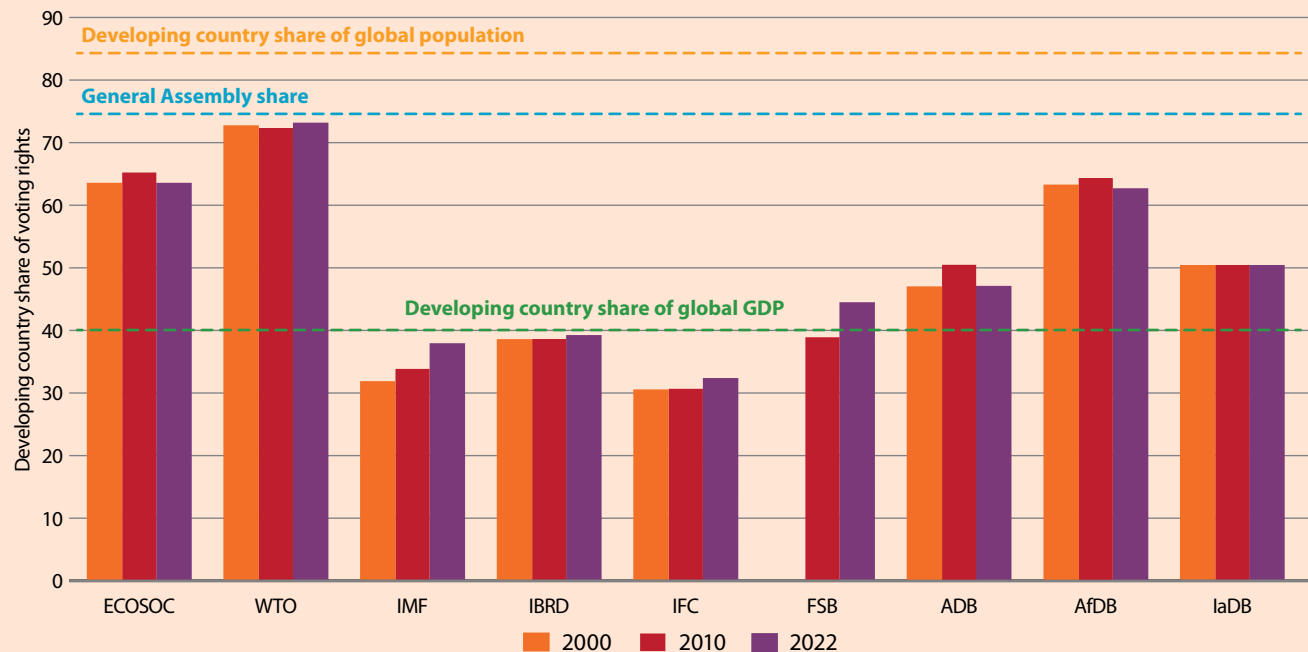
Non-bank financial intermediation, also known as shadow banking, has grown to almost \$218 trillion, almost half of global financial assets.



93 per cent of central banks were engaged in some form of central bank digital currencies work, and almost a quarter of central banks are piloting a retail CBDC.



Developing countries' representation has not significantly changed in many international financial institutions, regional development banks and standard-setting bodies.





Chapter III.F



Addressing systemic issues

1. Key messages and recommendations

There is universal recognition of the need to better align global financial and monetary systems with the Sustainable Development Goals (SDGs). The need for reform of the international financial architecture and strengthening the coherence and consistency of institutions and platforms is now universally recognized, with Member States endorsing such calls for reform in various forums, not least the financing for development outcomes. Some have used the term “non-system” to describe the various international financial and monetary frameworks, rules, institutions and markets that have evolved since 1945, often in an uncoordinated and ad hoc fashion, with different phases of economic globalization. The lack of coherence and coordination has often resulted in disjointed responses to economic, financial and other crises. Such shortcomings have become more acute with the increase in non-economic risks, foremost those of climate change, which is increasingly impacting economic and financial stability. The Addis Ababa Action Agenda is the first financing for development outcome to recognize the need to enhance policy coherence across all three dimensions of sustainable development and to thus take into account challenges such as climate change, pollution and the loss of biodiversity.

The financial volatility that has characterized the current global financial system has undermined efforts to achieve the SDGs; efforts to set up the structures that can deliver the necessary financing and stability have thus far fallen short. Since the end of the Bretton Woods exchange rate system in the 1970s, the global economy has seen growth in the size of the financial sector, progressively deeper integration of global financial markets, rapid technological change that has allowed more interlinkages, increasingly complex financial instruments and intermediaries and with that, growing

systemic risks. The Bretton Woods system included mechanisms that sought to moderate the accumulation of financial and trade imbalances through exchange rate adjustment; since the 1980s, countries have at times developed large surpluses or deficits. The strength of regulatory frameworks for banks has oscillated over the decades, but a growing share of financial activity has moved to unregulated or lightly regulated markets and instruments which are more likely to generate volatility. The world has experienced recurrent financial crises, with increasing cross-border transmission of instability, generating strong impacts on developing countries and the poorest people who tend to be deeply affected by the associated economic disruptions.

Global financial stability is especially sensitive to policies and developments in a few systemically important markets and instruments, with spillovers to developing countries. As noted in chapter II, monetary and financial policies in major developed countries have significant spillover effects on developing countries. This was borne out in the 2008 world financial and economic crisis, ripple effects from market instability at the onset of the COVID-19 pandemic, and strong impacts from monetary policy decisions in developed countries, especially in 2022. In the current environment of relatively high interest rates, stretched asset valuations and greater economic uncertainty, the risks of abrupt movements and higher volatility of asset prices are elevated. Continued geopolitical tensions also raise the risk of further volatility in commodities prices. Overall, over the course of the last two decades systemic risks appear to be growing, partly driven by the increase in climate-related risks such as an increase in the severity and frequency of disasters.

The global financial safety net, with the International Monetary Fund (IMF) at its centre, has come

under enormous strain in recent years, revealing both gaps in the architecture and uneven coverage. As countries have moved to liberalize financial flows, capital flow volatility provides a channel to generate or amplify financial and non-financial shocks. The global financial safety net, a multilayered arrangement for responding to crises, has been repeatedly tested, especially by the 2008 world financial and economic crisis and the 2020 COVID-19 pandemic. Those countries that were able to accumulate sufficient reserves, predominantly in United States dollar assets, have used them to cushion volatility, but this has opportunity costs in terms of foregone consumption and investment, which can be large in countries facing pressing investment needs to deliver on the SDGs. Meanwhile, access to other layers of the safety net has been very uneven. Bilateral swap arrangements (BSAs) among developed countries have become the tool of choice for fighting the spread of financial crises, with only a small volume of resources available to most developing countries through multilateral and regional arrangements. Special Drawing Rights (SDRs) were successfully allocated twice in crisis situations in the last 20 years, but a larger role for the SDR in buffering external adjustment or providing a flexible source of finance capacity would require architecture reforms. Sustainable development cannot be achieved without a conducive international institutional environment built on solidarity and multilateralism, including a strong global financial safety net, with the IMF at its centre. The international community could consider how the Fourth International Conference on Financing for Development, to take place in 2025, can help to address these challenges and support further strengthening of the global financial safety net.

Recent bank failures show that financial sector stability remains a challenge despite the progress achieved after the 2008 crisis; at the same time, the tasks of regulators are becoming more complex as they are increasingly called on to incorporate climate change and establish related incentives for investors in their regulatory work. A range of national financial regulations and international standards was updated in the wake of the 2008 world financial and economic crisis, but implementation is uneven globally, and certain risks remain outside the regulatory perimeter or scope of regulation. There are also industry pressures to roll back the implementation of stricter banking standards. Meanwhile, some types of non-bank financial institutions are not subject to the same level of prudential requirements as banks. New digital financial instruments, including cryptoassets, present new risks. In addition, financial regulatory norms are only gradually—and not yet sufficiently—addressing climate-related risks. Regulators, supervisors and financial institutions alike face challenges quantifying the forward-looking nature of climate-related risks given the long time horizons and high uncertainties of their manifestation. Market actors with short-term horizons can underestimate the systemic risks of climate change in their business-related and risk management decisions. Addressing the externalities of financial sector credit allocation decisions requires public policy instruments to set appropriate incentives for stability and sustainability. A refocusing of financial sector policies on climate impact would facilitate progress in mobilizing private capital for climate and could take account of the specific challenges faced by developing countries. The Fourth International Conference on Financing for Development could bring together relevant stakeholders, including regulators, governments, international organizations, financial institutions and other private sector actors and civil society, to create financial markets that are accessible, stable and sustainable.

While digitalization has reshaped finance and introduced new risks, it also provides opportunities to enhance the efficiency of outmoded financial infrastructure, such as the payments system.

The rise of digital payments and recent experimentation with central bank digital currencies (CBDCs) could further reshape the plumbing of all economic transactions. The Fourth International Conference on Financing for Development could explore how these changes impact sustainable development, support knowledge-sharing and address questions regarding the interoperability of payment systems to increase the speed and reduce the cost of cross-border transactions for developing countries.

Despite repeated commitments to increase the voice and representation of developing countries in global economic governance, and some progress being made in this area, significant reforms to institutional arrangements proved hard to achieve since the Monterrey Consensus. The governance of international financial institutions reflects decisions taken almost 80 years ago at a United Nations conference with only 44 delegations present. Since then, colonialism has ended and newly independent nations emerged. The expansion of the membership of the international financial institutions significantly diluted the voting shares of some of their original members. Nevertheless, global economic governance has not kept pace with ongoing changes, including the rise of the global South and other economic and geopolitical changes, and is not aligned with today's global economy. All international conferences on financing for development have included commitments to governance reform. Some improvements to increase developing country voice and representation were made between 2005 and 2015, but the pace and scale of change have left many countries dissatisfied. The Fourth International Conference on Financing for Development, taking place in a context of widespread recognition of the need to strengthen the legitimacy of global governance arrangements, presents an opportunity to address these shortcomings.

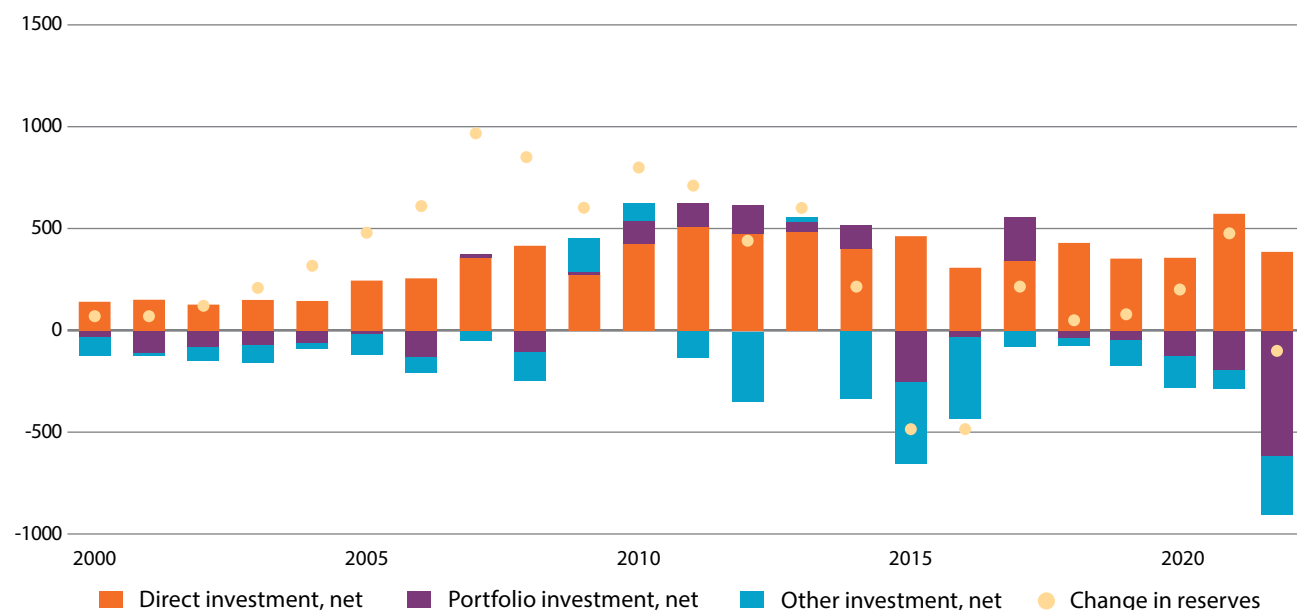
The rest of this chapter first gives an overview of the global financial safety net in the past two decades, followed by a section on financial market regulation and supervision. It then has a discussion on the development of the payments system and market infrastructure. The chapter concludes by discussing reforms to global governance and efforts to enhance policy coherence.

2. The global financial safety net

2.1 Trends in capital flows and capital account management

Push factors beyond the control of recipient countries, such as global risk aversion and global interest rates, are among the main drivers of international capital flows. The increase in the magnitude and volatility of capital flows can have adverse impacts on countries' exchange rate and financial stability, as well as affect access to long-term finance and debt sustainability—for example, when sudden stops impede the refinancing of foreign currency debt. In net terms for all developing countries, portfolio capital flows and other investment flows have seen numerous surges and reversals over the last two decades (figure III.F.1). In general terms, periods of very low interest rates in developed

Figure III.F.1

Net financial flows to developing countries, 2000-2022*(Billions of United States dollars)***Source:** UN DESA calculations based on IMF data.**Notes:** Positive values reflect a financial inflow.

markets from 2008 to 2022 tended to see investors in those markets search for yield in developing countries. In periods of instability or high interest rates, there is a flight to safety, with assets placed in developed markets. The annualized aggregate figures conceal some of the sudden surges, reversals and stops in short-term capital flows, which can manifest over periods of hours or days, and risk instigating financial crises. Capital flows also increased between developing countries, as they developed larger financial sectors.

Policymakers in recipient countries should be able to draw on a full range of policy tools to effectively address how capital flow volatility impacts their domestic economy and financial systems. Tools to counter the volatility of capital flows include monetary and fiscal policies; exchange rate policies, including foreign exchange intervention; macroprudential measures; and capital flow management (CFM) measures. Views on the appropriateness of these macroeconomic tools have varied over time. The IMF articles of agreement include clear recognition of the right to use capital controls, in keeping with the design of the Bretton Woods exchange rate system. In the latter half of the 1990s, the IMF considered, but did not adopt, a proposal to include promotion of capital account liberalization as a mandate of the IMF.¹ In the wake of the 2008 world financial and economic crisis, the risks from large and volatile flows prompted the IMF board to conduct extensive discussions on the policy towards capital flow liberalization and management before establishing an institutional view in 2012 which recognizes that CFM measures can be useful in certain circumstances but should not substitute for warranted macroeconomic adjustment.² In the Addis Agenda, Member States agreed that when dealing with risks from large and volatile capital flows, necessary macroeconomic policy adjustment could be supported

by macroprudential and, as appropriate, CFM measures. In its 2022 review of the institutional view, the IMF recognized a potential role for measures that combine elements of both CFM and macroprudential measures to reduce the volatility of capital inflows and to limit the build-up of financial vulnerabilities. As a result, the new IMF guidance sees a role for pre-emptive measures not only when capital inflows surge but also at other times to reduce systemic risks.³ Given the difficult trade-offs faced by policymakers in dealing with volatile capital flows, which under certain conditions warrant the use of multiple tools, the IMF's Integrated Policy Framework can provide guidance on the policy mix.⁴

2.2 Components of the global financial safety net

The global financial safety net is a set of institutions and mechanisms that aims to provide financial protection against crises and help to mitigate their impact. The safety net seeks to provide countries with insurance against crises, short-term liquidity finance when shocks hit, and incentives for sound macroeconomic policies, thus helping to avoid spillovers and alleviate moral hazard concerns. The stability of the world economy can be considered a global public good as it can help to protect vulnerable countries against shocks. The global financial safety net has four main layers of resources: countries' own international reserves; BSAs among central banks to exchange currencies; regional financing arrangements (RFAs), through which countries pool resources to increase financing in a crisis; and the IMF. Multilateral development banks and official bilateral creditors are usually not considered as part of the safety net as they mainly provide long-term financing for development needs, but their financing can be provided countercyclically to help countries close financing gaps during crises.

The global financial safety net has become more multilayered over the past two decades. Since 2000, the total stock of international reserve holdings has increased more than six times, reaching US\$14 trillion at end-2022, while the size of external resources available through other safety net layers grew nearly 16 times, to around \$3.5 trillion (figure III.F.2). Already in the Monterrey Consensus, Member States had underlined the need to enhance the stabilizing role of regional and subregional reserve funds, swap arrangements and similar mechanisms. This was accomplished with the introduction of BSAs among reserve currency-issuer countries at the onset of the 2008 world financial and economic crisis, the activation of limited BSAs with other countries during global crisis episodes, and the large scaling-up of the lending capacity of the IMF and RFAs during the world financial and the European debt crises (e.g. Bank of England, 2016). The expansion of Chinese BSAs since 2009 was another notable development.

Global financial safety net coverage has remained uneven, however, with only the IMF providing near universal access to external financing. Bilateral swaps are mainly extended by major central banks to selected countries, while regional arrangements provide liquidity only to their members. Developed countries are best served by the safety net as they can rely on the unlimited BSA network among the reserve currency-issuer countries. Other systemic countries with strong global financial links also have access to BSAs during global crises, although with relatively low limits in some cases. Countries from strongly integrated

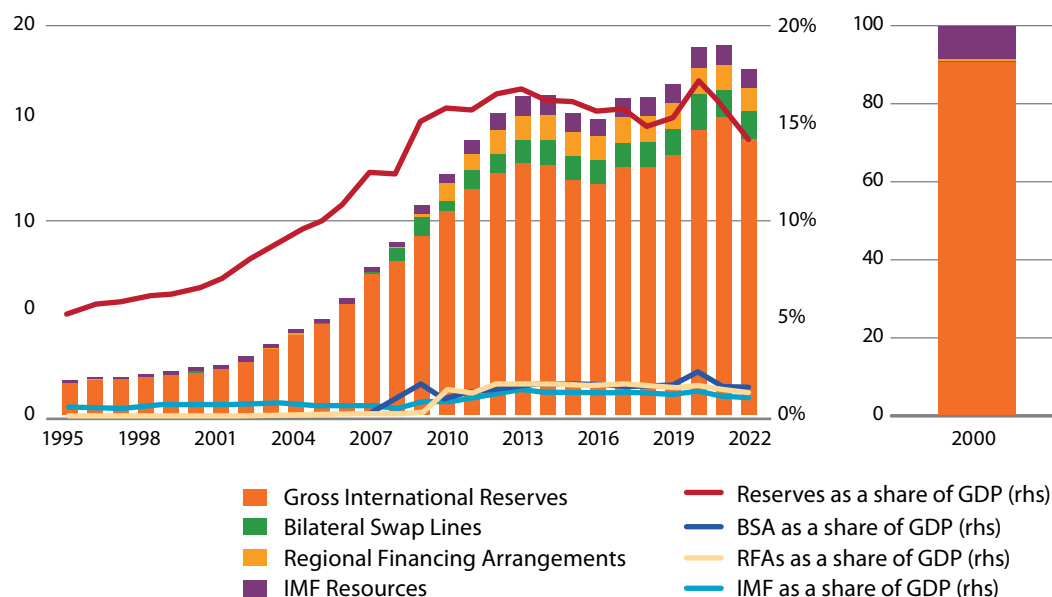
regions are covered by RFAs, with the European Union providing the highest coverage, followed by the Eurasian Economic Union and the Chiang Mai Initiative Multilateralization, although the latter has never been activated. Most developing countries, however, rely only on their own reserves and IMF resources (figure III.F.2).

Countries' gross reserves are by far the largest component of the global financial safety net. The predictability of many safety net resources (in particular RFAs) remains inadequate, while other elements, for example some BSAs, provide only geographically limited and time-bound support, which may not cover all countries nor the full duration of shocks. Many countries would therefore need to use several elements of the safety net to fully cover their financing needs, which could raise coordination issues. These considerations incentivize countries to self-insure by accumulating foreign reserves, although reserve accumulation can be attributed to multiple motives.⁵ The benefits of reserve accumulation in terms of avoided crises should be weighed against the costs.⁶ Regardless of the motives, accumulation of reserves carries quasi-fiscal costs and opportunity costs, which could be in the order of magnitude of 1 per cent of GDP if countries are using their reserves as self-insurance, or lower if they are using them to actively manage capital flow volatility.⁷ However, large reserve accumulations also entail potential systemic costs and can create coordination problems that can generate financial fragility and cross-border transmission channels for instability, undermining the resilience of the international monetary system.⁸ These include potential

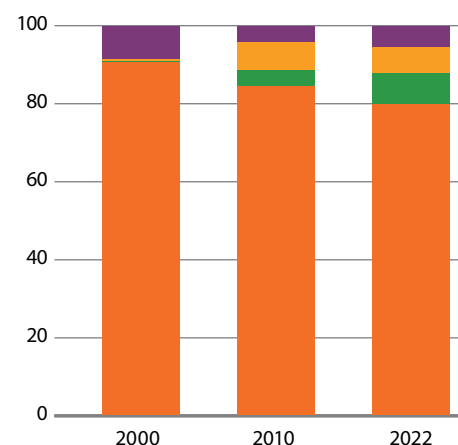
Figure III.F.2

Global financial safety net size and composition, 1995–2022**(a) Size of the GFSN and share of global GDP**

(Trillions of United States dollars, percent of world gross product)

**(b) Shares of the GFSN**

(Percentage)



Source: IMF.

Note: Bilateral swap lines includes permanent-unlimited swap lines (major advanced economy central banks) and limited-amount swap lines. The estimated amount of unlimited swaps is based on known past usage or, if undrawn, on average past maximum drawings of the remaining central bank members in the network. Regional financial arrangements based on explicit lending capacity/limit where available, committed resources, or estimated lending capacity based on country access limits and paid-in capital. IMF resources based on lending capacity, which includes quota and borrowing resources for countries in the Financial Transaction Plan (FTP) after deducting prudential balances.

deflationary impacts if the major reserve issuing country no longer runs deficits, the risk of sudden loss of confidence in the sustainability of the debt of the major reserve issuing country, and possible excessive risk accumulation by financial intermediaries as large reserve accumulations push down yields on the sovereign bonds of the major reserve issuer.⁹

The volume of foreign exchange reserves has risen enormously in the last two decades. Central banks around the world continued to accumulate reserves throughout the period, with an acceleration around the 2008 world financial and economic crisis and the COVID-19 pandemic (figure III.F.1). In total, global reserves increased from around \$2 trillion in 2000 to \$14 trillion in 2022. Over the same period, emerging markets added \$5 trillion to their reserves and low-income economies accumulated more than \$4 trillion.

Reserve coverage varies widely across countries. Advanced economies and large emerging markets hold most international reserves, with a high reserve coverage (figure III.F.3). Low-income countries, mostly in Africa, however, have limited reserve coverage, leaving them vulnerable to external shocks.

Bilateral and regional arrangements

The global network of swap lines expanded dramatically, but unevenly with the 2008 world financial and economic crisis and the COVID-19 pandemic—from six swap lines opened among advanced economy central banks in the early 2000s to more than 180 lines by 2021. It appears that scaled-up and reactivated swap arrangements helped to cushion the pandemic shock.¹⁰ In particular, the increased number of BSAs, primarily United States Federal Reserve swaps, provided prompt liquidity support, helping to stabilize the global financial markets and capital flows to emerging and developing economies. With some temporary pandemic-related lines expired, there are currently 160 swap lines in existence, totalling \$1.6 trillion.¹¹ The Inter-agency Task Force mapped out the swap lines in its *2023 Financing for Sustainable Development Report*, showing that very few developing countries have access to these facilities.¹²

RFAs have so far played a more limited role in the global financial safety net. Emerging and developing economies have access to five RFAs¹³ with a combined lending power of \$360 billion in 2022, only a fraction of the bilateral currency swaps. Some of these facilities have explicit requirements for the existence of an IMF programme in order to access larger volumes of liquidity. The use of these arrangements has been marginal, in part because during the COVID-19 pandemic, demand for RFA financing was contained thanks to supportive macroeconomic policies in advanced economies and timely financing from other safety net layers. European Union RFAs were untapped as European Union countries benefited from European Central Bank (ECB) swap/repo lines and United States Federal Reserve swaps, the ECB quantitative easing and ample European Union support through other channels. Some of the larger RFAs, notably the Chiang Mai Initiative Multilateralization and the Contingent Reserve Arrangement of the New Development Bank, remain untested and untapped.¹⁴

Multilateral mechanisms

The IMF is designed to be at the centre of the global financial safety net, and its lending volumes have grown significantly.

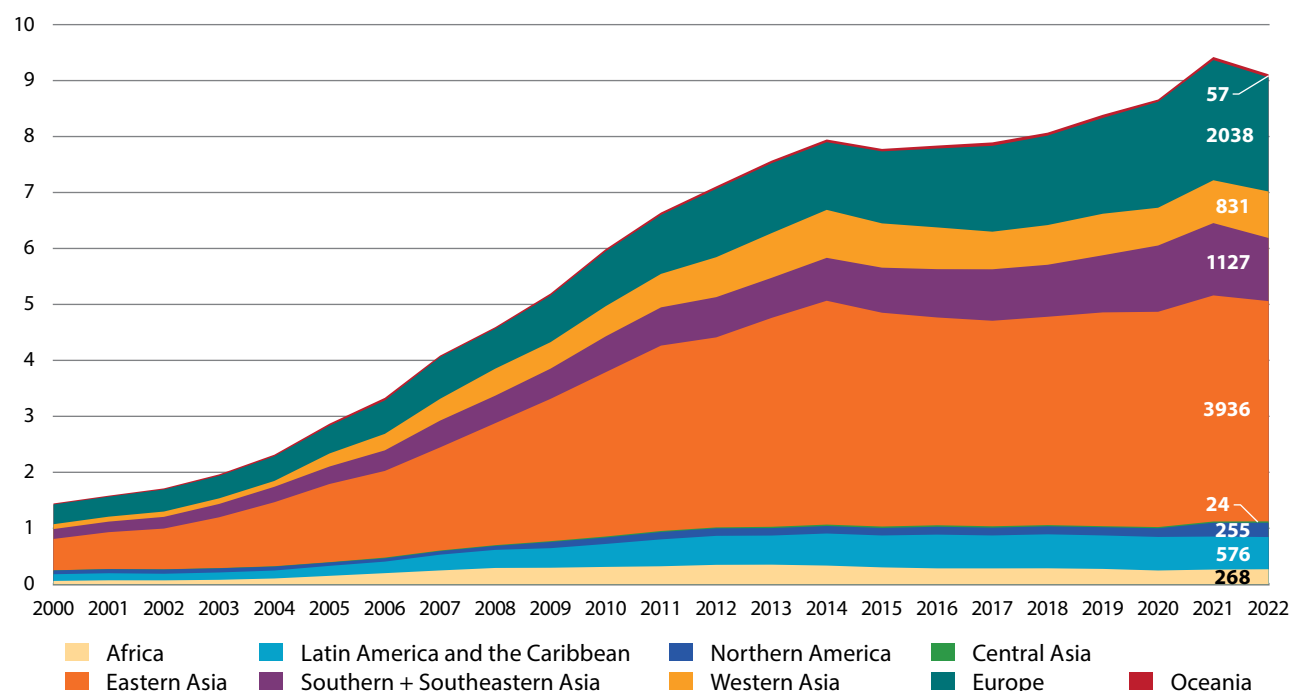
Unlike other layers of the safety net with uneven coverage, the IMF has a near-universal membership. The IMF works to prevent and address country-specific, regional and global crises through surveillance, lending and capacity development. Its unique quota-based financing model allows it to pool a portion of its members' reserves efficiently and at very low cost, with transparent burden sharing. It has also played a catalytic role in unlocking additional resources and better financing conditions for countries seeking financial assistance. While IMF lending was low in the early years of the new millennium, demand for IMF loans significantly increased in the wake of the 2008 world financial and economic crisis, both in terms of the volume and number of loans (figure III.F.4). Since then, it has approved an annual average of 17 new IMF-supported programmes, half of which focus on providing concessional financing to developing economies. In addition, through the Rapid Financing Instrument and Rapid Credit Facility disbursed emergency assistance, the IMF has lent to 97 countries (including 70 low-income countries) since the pandemic, bringing total disbursements since 2020 alone to around \$270 billion. The increase in lending and the large size of some programmes has led to an increase in the number of countries paying IMF surcharges, which apply only to high and prolonged borrowing of non-concessional resources and which are designed to discourage large and prolonged use of IMF resources.

The IMF has several lending windows that have evolved over the years to strengthen the global financial safety net in the face of more prevalent, protracted and diverse external shocks. The IMF provides crisis response, emergency, concessional and precautionary lending instruments, with lending facility design repeatedly evolving in the last two decades as the institution sought to learn lessons from shocks and quickly provide liquidity to all countries. Following the 2008 world financial and economic crisis, the IMF strengthened its lending toolkit by reforming its non-concessional lending to enhance crisis-prevention tools. The Flexible Credit Line, Precautionary and Liquidity Line and Rapid Financing Instrument were added as new lending instruments to the traditional Standby Arrangement and Extended Fund Facility, aiming to bolster confidence and reduce balance-of-payments pressures during periods of heightened systemic risk. In April 2020, the IMF further expanded its non-concessional lending toolkit by establishing a new Short-Term Liquidity Line for countries with very strong policies and fundamentals. These precautionary instruments have been effective in providing insurance against external risks.¹⁵ In September 2022, the IMF established a temporary Food Shock Window in its emergency financing instruments to support countries facing urgent balance-of-payment needs related to the global food crisis.¹⁶

The recently concluded 16th General Review of Quotas will boost IMF permanent resources without changing its overall resource base. In December 2023, the IMF Board of Governors approved the 16th General Review of Quotas which will boost IMF members' quotas by 50 per cent. Once implemented, this will bring the IMF's total quotas, which are permanent resources, to 715.7 billion SDRs (\$960 billion). It will maintain the current lending capacity of the IMF through a combination of the approved quota increase and a reduction in resources borrowed bilaterally from member countries. To be implemented, member countries holding 85 per cent of IMF voting rights must now consent to their respective quota increases, which in many cases involves legislative approval.

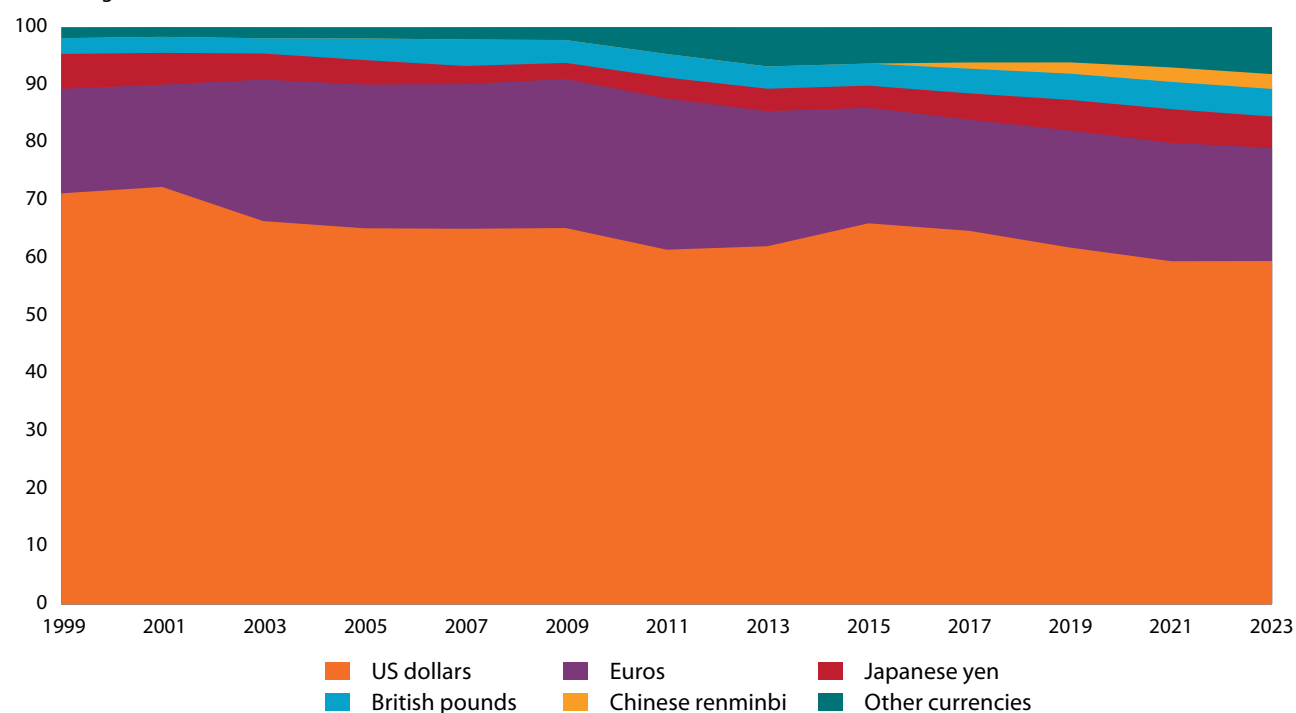
Figure III.F.3
International reserves, 2000-2022

(a) Value of reserves
(Billions of SDRs)



Source: UN DESA calculations based on IMF data.

(b) Currency composition of reserves
(Percentage)



Source: IMF.

IMF concessional and development-oriented lending has been reformed and expanded. The IMF Poverty Reduction and Growth Trust (PRGT) provides concessional lending to lower-income countries, many of which are affected by fragility and conflict. More recently, the new Catastrophe Containment and Relief Trust (CCRT) was established to help the poorest and most vulnerable countries hit by catastrophic natural disasters or by epidemics with potential international spillovers. Two new concessional facilities have been established—the Standby Credit Facility for short-term balance-of-payments needs, and the Rapid Credit Facility to provide low-access financing for urgent balance-of-payments needs—while protracted balance-of-payments needs continued to be addressed through the Extended Credit Facility. In the period from the pandemic until January 2024, the IMF approved around \$44.2 billion for 57 PRGT-eligible countries in PRGT and General Resources Account financing. Overall, the IMF has quintupled its interest-free lending to low-income countries through the PRGT, compared to pre-pandemic annual levels. Around \$50 billion has been disbursed through emergency financing (Rapid Credit Facility/Rapid Financing Instrument and augmentations under existing arrangements) to 81 countries. The Resilience and Sustainability Trust (RST), created in 2022 and funded in part by the SDRs of G20 countries, provides longer-term lending through an associated facility for low-income and vulnerable middle-income countries. This instrument focuses on helping countries to build resilience to external shocks and promote sustainable growth. It supports policy reforms that aim to reduce macroeconomic risks arising from longer-term structural challenges, including climate change

and pandemic preparedness. Around three quarters of IMF member countries are eligible for RST support, including all small island developing States (SIDS).¹⁷

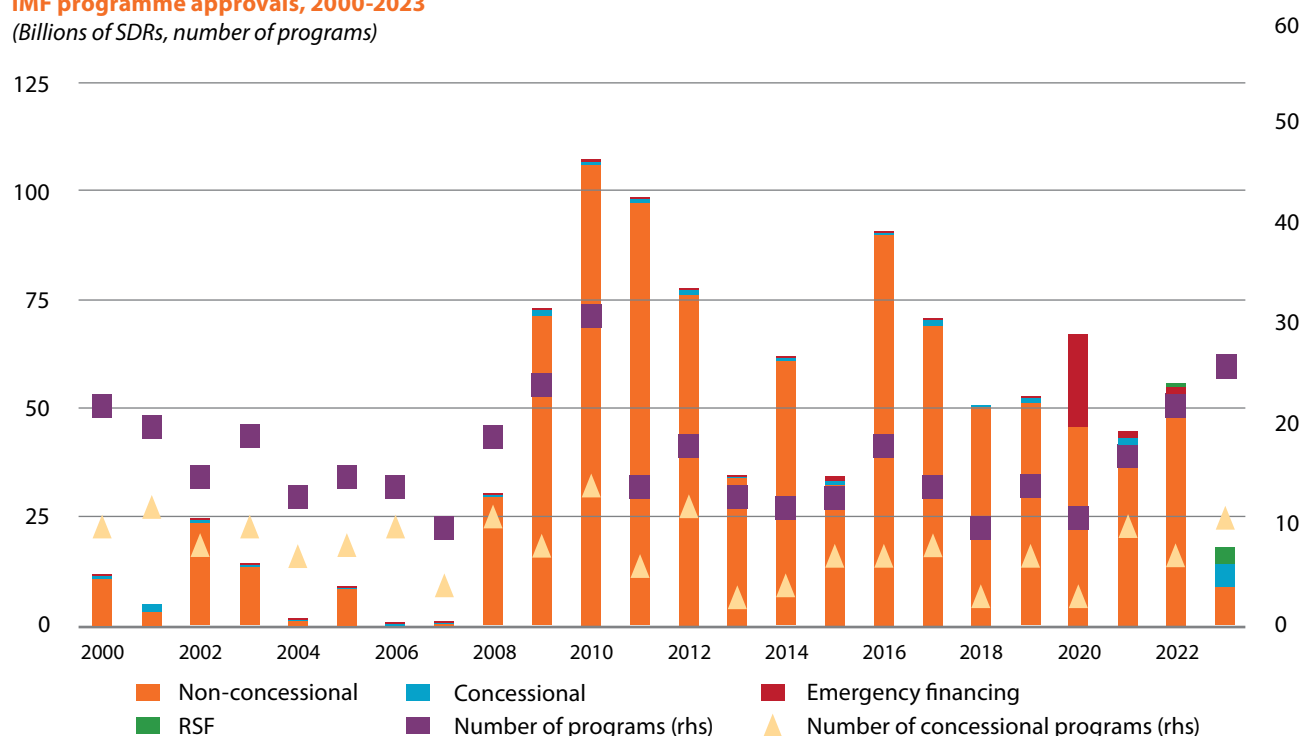
Implications for the international monetary system

The end of the Bretton Woods exchange rate system in the 1970s heralded a more uncoordinated international monetary system, although the United States dollar remains at its centre. Before the 1970s, all IMF members managed their exchange rates, but now countries are free to choose their exchange rate regimes—fixed exchange rates, a free-floating currency or a managed float.¹⁸ As noted above, larger and more volatile cross-border capital flows have led countries to accumulate significant foreign exchange reserves to protect themselves from external shocks. Most of these reserves are kept in dollar-denominated assets (figure III.F.3 panel b). There are multiple motivations for this, such as that international trade, including important commodities, is frequently priced and settled in dollars, and United States financial markets are the biggest and most liquid in the world. However, there have been slow shifts away from the dollar for a mixture of practical, idiosyncratic and geopolitical reasons. SDRs, an international reserve asset created by the IMF in 1969 to supplement its member countries' official reserves, have not taken on this role even though they were created with “the objective of making the special drawing right the principal reserve asset in the international monetary system”.¹⁹

Figure III.F.4

IMF programme approvals, 2000-2023

(Billions of SDRs, number of programs)



Source: IMF.

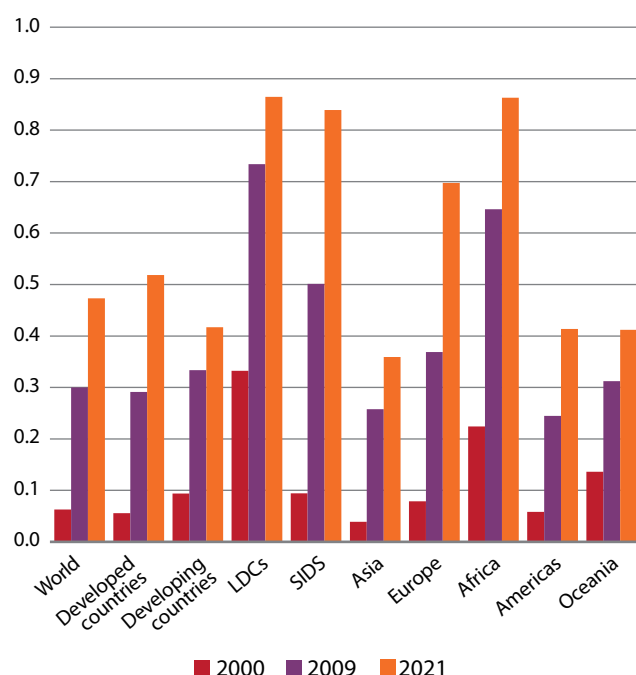
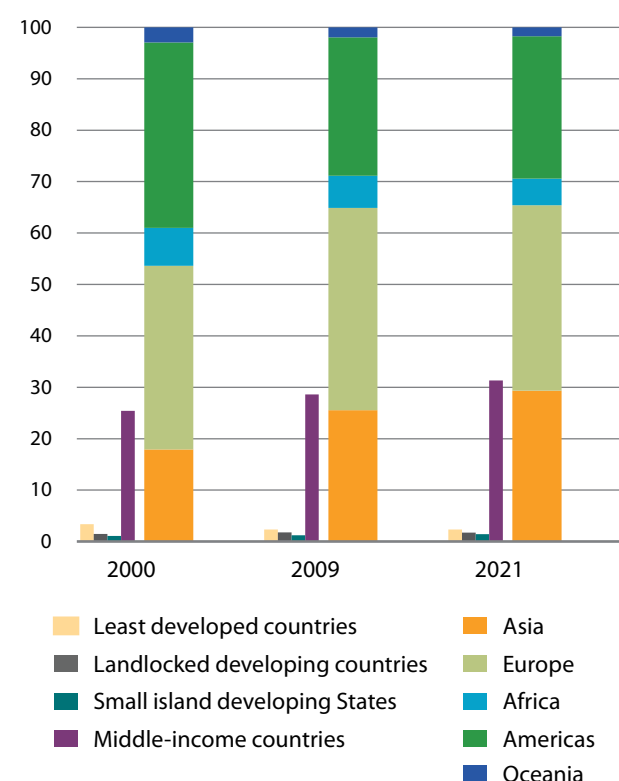
Notes: Based on total approved amounts per arrangements. Concessional programs also include blended arrangements. The numbers of programs approved do not include emerging financing. Resilience and Sustainability Facility (RSF) is funded by resources in the RST.

SDR allocations have boosted the supply of global reserves at times of financial and economic system stress. SDR allocations make new SDRs available to countries without creating additional debt, allowing them to increase their international reserves or cover spending needs. Two allocations have been implemented since 2000, the first during the 2008 world financial and economic crisis (around \$250 billion) and the second during the COVID-19 pandemic in August 2021 (around \$650 billion). These allocations provided IMF members with a critical financing source, injecting much-needed reserves and liquidity during a period of exceptionally high uncertainty, helping to bridge some of the gaps in the global financial safety net. To date, a total of 660.7 billion SDRs (equivalent to around \$943 billion) have been allocated. The quota-based allocation of SDRs, in proportion to countries' quota shares at the IMF, means that developing countries received around one third of the allocations, which represented a large share of their international reserves (figure III.F.5). Countries in special situations and, to a lesser extent, middle-income countries, are the main users of SDRs, for whom they alleviate external and fiscal financing constraints at times of urgent financing needs, while developed countries tend to hold them as part of central bank reserves (figure III.F.6). A review found that the 2021 allocation of SDRs was beneficial for the global

economy as it helped to meet the long-term global need for reserves and supported confidence by reducing sovereign risk premia.²⁰

There are many ideas on how to better use SDRs as a development tool, but some of them would require changes to the structure of the international monetary and financial architecture. While SDRs have not yet become the principal reserve asset, there have been periodic efforts over the last two decades to consider how to strengthen their role. The most recent comprehensive discussion on this topic at the IMF executive board was held in 2016.²¹ In the wake of the 2021 allocation of SDRs, some IMF members with sufficient reserves and strong external positions agreed to the voluntary rechanneling of SDRs to countries that need them. Over \$100 billion has been pledged mainly to the IMF's PRGT and RST. Given that many of the SDRs on central bank balance sheets in developed countries are unused, there have been calls for more rechanneling, including to multilateral development banks (see chapter III.C). A larger role for the SDR in buffering external adjustment or providing a flexible source of finance to bolster IMF lending capacity would require revisions to the IMF Articles of Agreement, although the IMF executive board could on its own agree to triggers that automatically generate a recommendation for SDR issuance, or to standing arrangements to rechannel SDRs on issuance.²²

Figure III.F.5

SDR allocation, by country group and region, 2000–2023**(a) SDR allocations as a share of GDP**
(Percentage of GDP)**(b) SDR allocations as a share of total**
(Percentage of SDRs allocated)

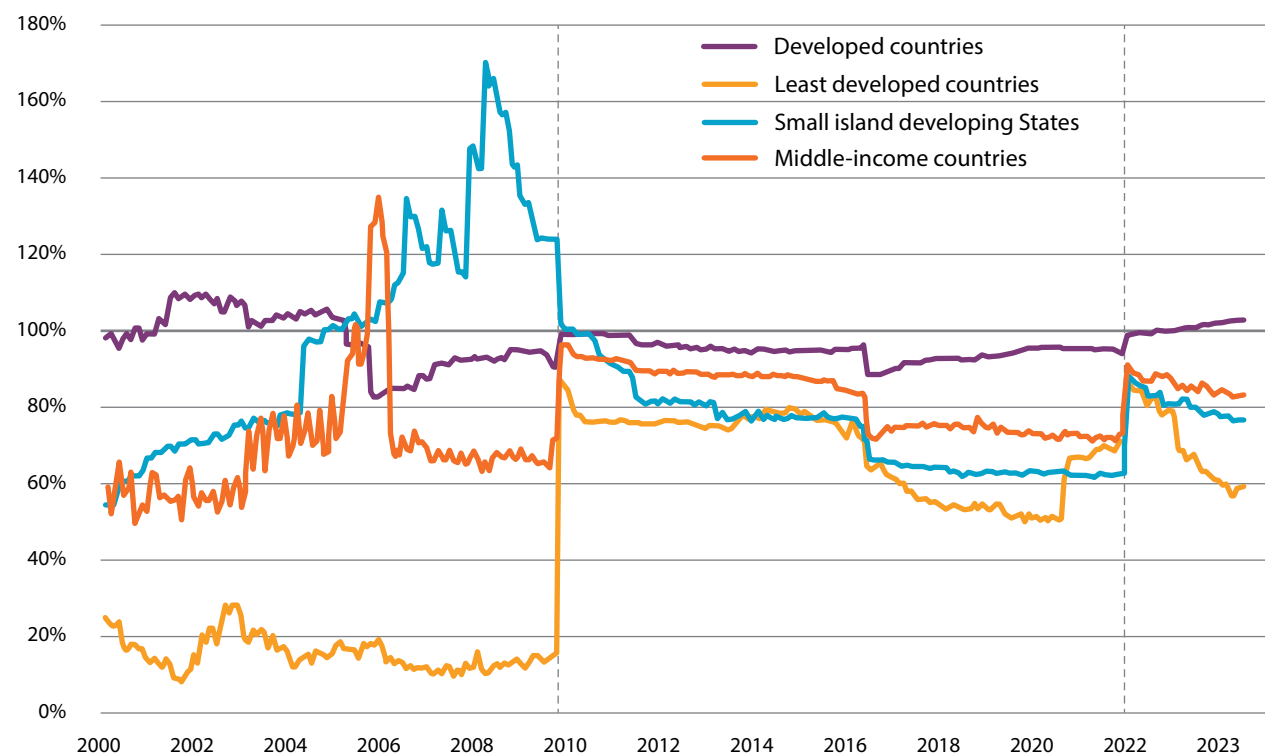
Source: UN DESA calculations based on IMF data.

Note: Regional groupings based on M49. 2000 reflects existing SDR allocations at the end of the year, 2009 and 2021 reflect the shares of new SDRs allocated that year.

Figure III.F.6

Holdings of SDRs as a share of total SDR allocation, 2000-2023

(Percentage)

**Source:** UN DESA calculations based on IMF data.**Note:** SDR holdings by country groups as a percentage of their group's SDR allocation. Below 100 per cent indicates net use of SDR allocation, i.e., SDR holdings were exchanged for other currencies. Dashed vertical lines indicate 2009 and 2021 general SDR allocations.

3. Financial market regulation and supervision for sustainable development

3.1 Banking regulation and supervision since 2000

Banking regulation has been evolving in response to repeated instances of financial instability and the increasing complexity of the financial system. The first international standards for banking regulation were agreed in 1988 in the Basel Accord through the Basel Committee on Banking Supervision (BCBS) and have since become known as Basel I.²³ The Monterrey Consensus did not explicitly reference the Basel Accord but did call for developing country participation in the formulation of financial standards and codes and their implementation on a voluntary basis. Reforms to the international framework were agreed first in 1996 with the market risk amendment, and then in 2004 with the Basel II agreement that introduced risk-sensitive approaches, including allowing banks to use complex proprietary risk-weighting systems. While members of the BCBS were obligated to implement the reforms, other countries used them on a voluntary basis, with only selective implementation in developing countries as a result of the complexity and lack of applicability

to many developing country contexts.²⁴ In the Doha Declaration, which was agreed in the midst of the 2008 world financial and economic crisis, Member States agreed to implement reforms to strengthen the regulatory and supervisory frameworks of financial markets, as needed. In the wake of the financial crisis, a set of reforms that covered banks' capital, leverage and liquidity, named Basel III, were issued between 2010 and 2019. All G20 countries became BCBS members and were thus obligated to implement these rules. The Addis Agenda in 2015 included agreement to hasten completion of the reform agenda on financial market regulation, and further amendments to Basel III were completed in 2018.

The Basel reforms have focused on international standards for banking supervision and the capital adequacy of banks, but have less coverage of other types of risks. A number of high-profile bank failures in the 1970s and 1980s related to fraud, illiquidity and currency risk demonstrated the importance of banking supervision.²⁵ International principles for supervision were first agreed in the early 1980s and consolidated into the Basel Core Principles of Effective Banking Supervision in 1997.²⁶ The original Basel I agreement standardized the capital adequacy rules for banks internationally for the first time, setting a baseline for how banks should address credit risk. However, the framework did not directly address operational risk, interest rate risk, securities investment risk, or liquidity risk. Basel II addressed criticisms of lack of risk sensitivity on credit risk, enabling both more and less complex approaches, and included

operational risk for the first time. Focusing on common equity, Basel III sought to enhance the permanence and loss absorbency of banks' capital, while also introducing additional ratios (such as the leverage ratio, liquidity coverage ratio, and net stable funding ratio) and extra capital buffers for systemically important banks. Globally, banks have been growing with regard to total asset size, but they have grown less than total financial assets, meaning that banks have played a progressively smaller role in global credit allocations (figure III.F.7).

While member jurisdictions continue to make progress in implementing the finalized Basel III reforms, risks are still present in the banking system. The BCBS evaluation of the impact and efficacy of Basel III reforms found that the overall resilience of the banking sector has increased following implementation.²⁷ Notably, this greater resilience did not come at the expense of banks' cost of capital. The report also found no robust evidence that banks with lower initial capital and liquidity ratios had lower loan growth than peers. The Financial Stability Board (FSB) was created in the wake of the 2008 world financial and economic crisis to coordinate implementation of regulatory reforms across banking and other non-bank financial intermediaries (NBFIs). The FSB is responsible for policy measures to address systemically important financial institutions, including the Key Attributes of Effective Resolution Regimes for Financial Institutions. Work is still ongoing to close gaps in the operationalization of resolution plans for banks, which is particularly important to prevent States from stepping in to bail out the largest banks.²⁸ Overall, efforts to tackle the too-big-to-fail problem through increased regulation and supervision of the largest globally systemically important banks have

made progress, but domestic systemically important banks are not evenly covered and information gaps persist.

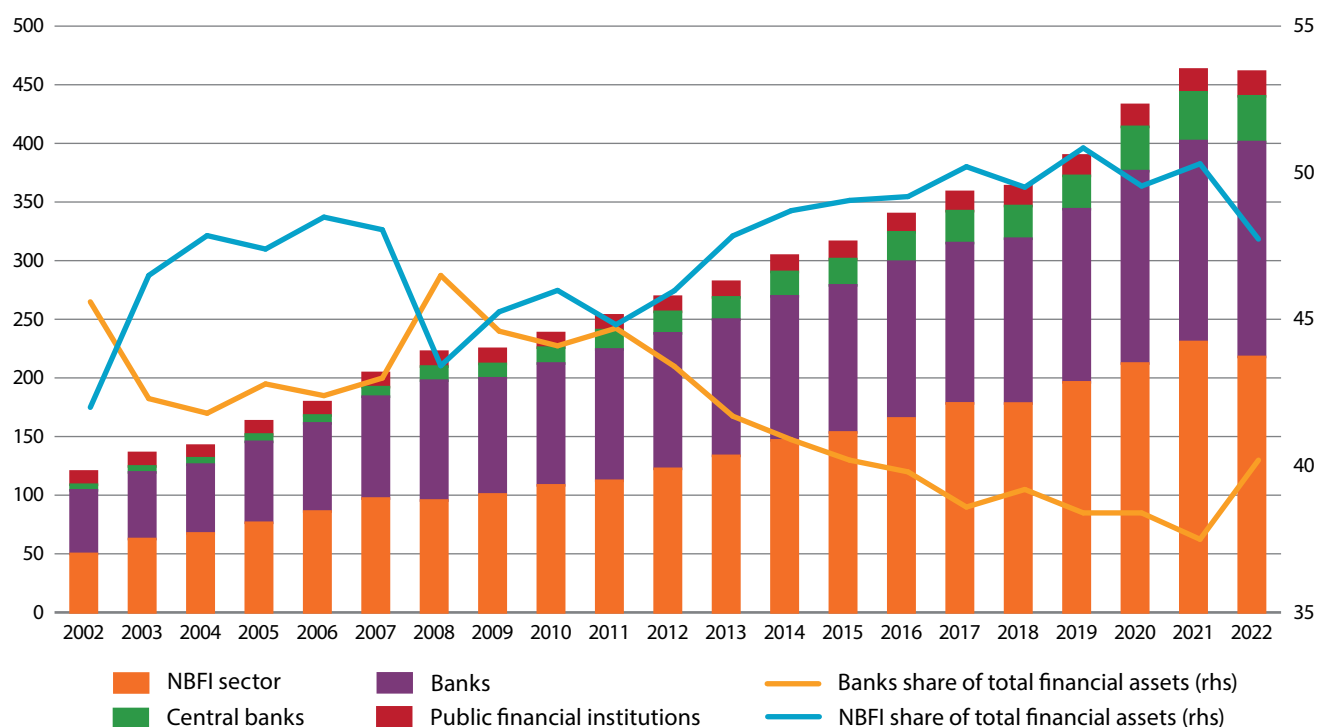
Regulatory fatigue is another challenge, despite recent banking turmoil. In annual monitoring exercises, countries reiterate their expectations of implementing all aspects of the Basel framework in full, consistently and as soon as possible, although implementation in many cases is being pushed to 2024 or later.²⁹ Nonetheless, banks and other industry actors in some jurisdictions are also lobbying against the final implementation of the Basel III reforms, citing potential impacts on credit to households and businesses and potential loss of competitiveness. A string of bank failures and runs in March 2023, including one bank labelled as globally systemically important, resulted in the authorities in two developed jurisdictions using public money to underwrite the banking system. The earlier iteration of the Basel III reforms, which were implemented before the 2023 bank failures, are thought to have helped shield the global banking sector and the real economy from a wider spread of financial instability; at the same time, these crises underlined the importance of effective regulatory implementation and supervision.³⁰ Effective supervision of banks requires political will to give supervisors the ability and resources to act.³¹

3.2 Non-bank financial intermediation

Over the past decade, the global financial system has become increasingly reliant on market-based intermediation. As bank lending declined in the wake of the 2008 world financial and economic crisis, non-bank financial intermediation, also known as shadow banking,

Figure III.F.7

Total global financial assets broken down by type of financial institution, 2002-2022
(Trillions of United States dollars, percentage of assets)



Source: FSB.

has grown to comprise almost half of global financial assets (figure III.F.7), and has become more diverse. As a result, the importance of NBFIs for the financing of the real economy has increased.³² The 2022 decline in the size of the NBFI sector (a 5.5 per cent decrease compared to 2021) was the first notable decrease since 2009. It is largely attributed to the impact of higher interest rates leading to valuation losses in mark-to-market asset portfolios, particularly in investment funds;³³ total financial assets held by banks, largely composed of loans less sensitive to interest rate changes, increased by 6.9 per cent over the same period. The recent changes are not expected to alter the long-term shift away from banks and towards NBFIs.

The 2008 world financial and economic crisis, although involving banks, also implicated many types of NBFIs, particularly securitization and derivatives markets, yet implementation of NBFI reforms continues at a slow pace and is at an earlier stage than other reforms. In relation to securitization, there has been incremental progress in implementing recommendations on incentive alignment approaches and the BCBS securitization framework. Progress continues at a slow pace on global securities financing data collection and aggregations with limited coverage. Overall, implementation of over-the-counter derivatives reforms is well advanced (particularly in the largest markets) but progress has slowed in recent years. Implementation of reforms to mitigate spillovers between banks and NBFIs is still ongoing. The adoption of recommendations to reduce the run risk of money market funds (MMFs) is most advanced in 19 jurisdictions—unchanged since 2021—with at least 95 per cent of MMF assets covered by regulations in line with global rules.³⁴ However, the main risk to financial stability from certain parts of the NBFI sector is illiquidity, and that challenge awaits resolution. Intermediaries such as MMFs and open-ended funds can experience instability in moments of market stress due to liquidity and currency mismatches.³⁵ Reducing excessive spikes in the demand for liquidity and better preparation for margin calls can enhance resilience.

Non-bank financial institutions have also increasingly taken on the provision of credit to developing countries, accentuating procyclicality. NBFIs have played an increasing role in funding developing country external debt (see chapter III.E). Part of this financing has come from investment funds, whose assets more than tripled in the decade after the 2008 world financial and economic crisis. While this development has added to the diversity of funding sources, it has created new challenges for developing countries. Empirical evidence suggests that investment funds—especially those that are either passively managed or follow benchmark indices—may be more susceptible to global financial conditions, accentuating the procyclicality in capital flows.³⁶ Cross-border capital flows from different market actors respond differently to push and pull factors,³⁷ and portfolio debt flows seem to be more volatile.³⁸ Investment funds face investor protection regulations related to fraud and operational risks, but do not face prudential regulations in their home jurisdictions aimed at reducing the volatility of capital flows. Developing countries themselves may want to take macroprudential and other regulatory measures to reduce corporate foreign currency risks and mismatches and deepen the local currency markets and the domestic investor base (see chapter III.B).

Regulatory frameworks need to adapt to new technologies and instruments by ensuring a “same activity, same risk, same rules” approach. In the last two decades there has been enormous financial innovation, with new types of instruments, new markets and new actors

that were often created outside the scope and perimeter of existing regulatory and supervisory frameworks. These are often enabled by new technological developments, and digitalization has opened a new frontier in financial technology (see chapter III.G). While creating new opportunities for efficiency gains and financial inclusion, the large-scale adoption of these technologies also creates new risks, including for financial stability and integrity. One of the key proposals is that authorities should apply effective regulation, supervision and oversight in line with the principle of “same activity, same risk, same regulation”, with financial standards applied based on economic function and risks, rather than on legal form.

3.3 Addressing climate change and the environment in regulation

The escalating climate crisis has led to growing interest in how financial market regulation and supervision can incorporate questions of environmental sustainability. Before the 2015 Paris Agreement on climate change, financial regulators and supervisors paid little attention to environmental issues. Yet accelerating climate change increasingly impacts financial systems, and stakeholders have accepted the need to assess, manage and mitigate the financial vulnerabilities, which are commonly referred to as “climate-related financial risks”.³⁹ These are often characterized as including physical risk (due to both acute and chronic climate-related disasters), transition risk (related to changes in government policies and regulations adopted to combat climate change, technological developments, and changes in consumer preferences and market sentiment), as well as liability risks associated with potential compensation claims from those negatively impacted by climate change. So far the focus of regulators’ work on transitioning to a more sustainable financial system has been on transparency/disclosures, data, vulnerability analysis and developing regulatory approaches and supervisory practices.⁴⁰ The BCBS issued an international standard defining 18 high-level principles for how regulators and supervisors should improve risk management and supervisory practices to address climate-related financial risks.⁴¹ Many businesses are developing transition plans to set out their strategy for addressing climate-related financial risks, which can be an important source of information for financial regulators and supervisors.⁴² Some jurisdictions are planning to mandate the development of transition plans and their use by supervisory authorities. In addition, climate change-related scenario development is a practical tool to help authorities and private sector players assess both the macro-financial risks posed by climate change and the opportunities of timely climate change mitigation.⁴³

Regulatory responses to climate change will not be effective in a vacuum but can contribute to overall climate-related policies and action plans. Fostering financial stability while enabling finance flows aligned with the objectives of the Paris Agreement and the Global Biodiversity Framework are key for a successful transition. The mandate of regulators and prudential supervisors is to promote the safety and soundness of financial institutions and the financial system. The actions of central banks, supervisors and financial institutions can complement and facilitate the implementation of climate policies. However, they are not a substitute for gaps in governments’ climate policies.⁴⁴ For example, the application of different capital risk weightings to banks’ exposure to green and brown assets could create price incentives for banks to shift their exposures, yet it cannot trigger reallocations at the required scale and could

lead to unintended consequences for financial stability. Financial sector policies should be complementary to other tools such as carbon pricing, directed subsidies, or other types of public policy (see chapter III.A).⁴⁵

Regulatory efforts to improve sustainability disclosure can contribute to more effective pricing of climate risks and provide the information needed for regulators and other market actors that have a mandate to ensure climate change mitigation. Efforts since 2015 to improve climate-related disclosures were coordinated out of the voluntary Task Force on Climate-related Financial Disclosures (TCFD), which has now been disbanded, as follow-up efforts are being led by the International Sustainability Standards Board alongside other efforts on sustainability disclosure (see chapter III.B).⁴⁶ Other market actors, including public institutions such as central banks, may want or need reliable and consistent information on both the financial impacts of climate change on financial institutions as well as the impact of the financial sector on the ability of countries to transition to sustainable economies. The BCBS is analysing how a mandatory disclosure framework for climate-related financial risks could enhance financial stability and has issued a consultation document.⁴⁷ However, international standards on environmental disclosures on their own are unlikely to result in real impacts on how the financial sector contributes to climate change, as evidence shows a disconnect between environmental disclosures and lending activities.⁴⁸

4. Payments and market infrastructure

Smoothly functioning payments systems have many positive externalities that can support financing for development, while digitalization may fundamentally alter the international monetary and financial systems. While the previous financing for development outcomes did not directly address payments and market infrastructure, recent developments have shown the importance of these systems to financial stability. Payment and settlement systems were largely left to private banks until the 1980s when an expert committee was formed on payment systems under the auspices of the Bank for International Settlements. More formal coordination was launched in the 1990s, roughly concurrent with the development of international banking standards. However, in recent years, the slow speed and high cost of cross-border payments has become a major issue of concern to developing countries, affecting remittances, trade and other transfers. New digital technologies have opened up the prospect of mediums of exchange and payment systems operating outside of the regulated financial sector, introducing new risks. Digital technologies also provide opportunities to improve the payments system which underpins global financial activity, but design considerations should be cognizant of the needs of developing countries and their place within the international monetary architecture.

4.1 Correspondent banking and cross-border payments

The decline of correspondent banking relationships has been a major concern of developing countries, particularly SIDS. A “correspondent bank” provides local account and payment services for banks based abroad—collectively forming the correspondent banking network

that facilitates cross-border payments. Correspondent banks make their payments by sending SWIFT messages to one another that include instructions to debit or credit their accounts. While none of the financing for development outcomes reference correspondent banking relationships, Member States addressed the issue several times in the intergovernmental follow-up process, as the steep decline in relationships could leave some jurisdictions without any means to receive cross-border payments. Correspondents fell by almost 30 per cent over the last decade, with the decline very unevenly distributed: SIDS, Latin America and the Caribbean and Southern Africa experienced the steepest declines.⁴⁹ The perceived costs of implementing know-your-customer rules mandated by regulators, the development of alternative remittance channels, and the high costs of maintaining channels with low transaction volume all contributed to the decline.

As a result, the costs of sending cross-border payments remain above targets set by the G20. Partially as a response to the concern about correspondent banking relationships, Member States have sought to address inefficiencies in cross-border payments, including through improving the use of technological tools. The G20 target for retail payments, which are defined as payments of less than \$100,000 sent by people or businesses, but which are not remittances (see chapter III.B), is that they cost less than 3 per cent of the payment amount. Globally, approximately one quarter of corridors have average costs greater than 3 per cent, largely because of the cost of payments initiated by individuals. For business-initiated payments, only 3 per cent (51 of 1,564) of payment corridors to other businesses and 6 per cent (108 of 1,715) of corridors to individuals have average costs greater than 3 per cent (see table III.F.1).⁵⁰

Table III.F.1
Global average cost of cross-border payment transactions, 2023
(Percentage of payment amount)

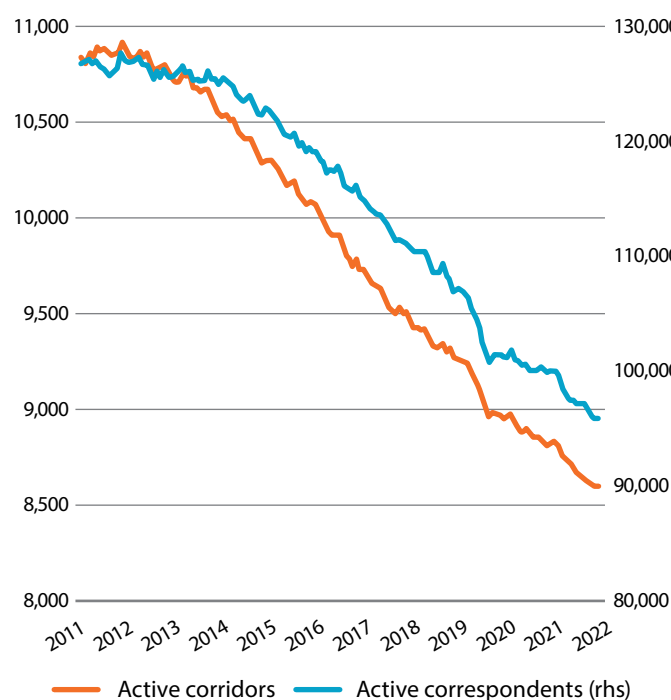
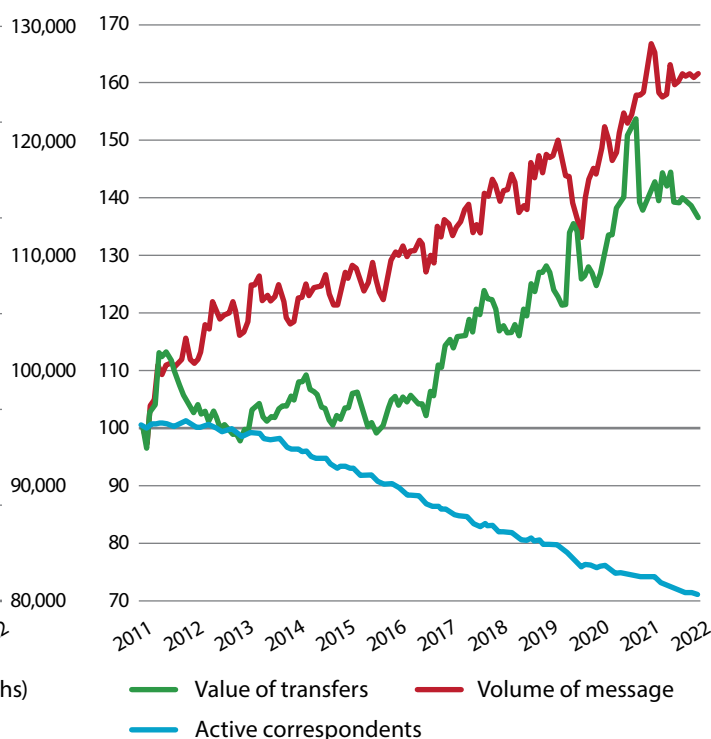
		Recipient	
		Business	Individual
Sender	Business	1.5%	1.7%
	Individual	2.0%	2.5%

Source: FSB.

4.2 Central bank digital currencies

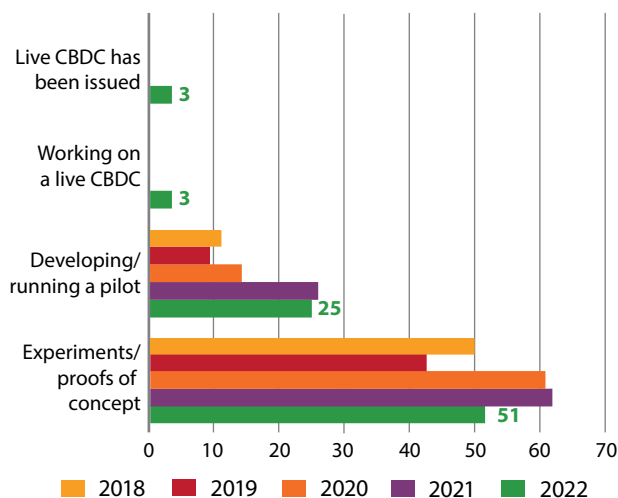
Central banks are experimenting with digital currencies with a view to improving payment systems. CBDC is digital money issued by central banks. A retail CBDC is intended for use by the general public and would operate alongside or in place of cash; a wholesale CBDC is used for transactions between financial institutions and would be used alongside or in place of reserves held in central bank accounts. As of 2022, the overwhelming majority of central banks (93 per cent) were engaged in some form of CBDC work. Progress on retail CBDC is more advanced than on wholesale CBDC: almost a quarter of central banks are piloting a retail CBDC. More than 80 per cent of central banks see potential value in having both a retail CBDC and a fast payment system.⁵¹ A few CBDCs have already been launched. Reasons given by central banks for working on CBDCs include the safety and efficiency of payments, improving financial inclusion, better implementation of monetary policy, and enhancing financial stability.

Figure III.F.8

Correspondent banking relationships, 2011-2022**(a) Active correspondent banking relationships***(Number of corridors, number of correspondents)***(b) Changes in transfers and correspondents***(Index)***Source:** BIS.

Notes: Three-month moving averages, based on SWIFT BI Watch and National Bank of Belgium. An active corridor is defined as a country pair that processed at least one transaction. The count of active correspondents measures, corridor by corridor, the number of banks that have sent or received messages. Volume refers to the number of messages. For index Jan 2011 = 100.

Figure III.F.9

Status of CBDC work by central banks, 2018-2022*(Percentage of respondents)***Source:** BIS, Paper No. 136.

Notes: Chart shows type of work in addition to research work. Based on responses from central banks in 86 jurisdictions.

CBDC issuance has the potential to enhance payments efficiency, but it could introduce new risks, including macro risks such as currency substitution.

There are many design decisions that need to be made in regard to CBDCs, including the role of private banks, the openness of the architecture, limits on transactions and balances, the payment of interest on balances, and the costs of transactions. Payment service markets are often marked by oligopoly, and CBDCs with certain designs can reduce the rents earned.⁵² If cross-border interoperability is implemented, then CBDCs can help speed up and reduce the costs of cross-border payments. The decision to explore and potentially even launch CBDCs should remain jurisdiction-specific, depending on policy objectives and domestic circumstances, such as the degree of digitalization, the structure of the financial system, legal and regulatory frameworks, and the central bank's own capacity.⁵³ There will be new operational risks for central banks to manage: For example, the digital infrastructure for processing CBDC transactions will require significant upfront investment and ongoing maintenance. There are also financial stability risks related to potential bank disintermediation if the CBDC competes with bank deposits. The technical design of CBDCs will determine the balance of benefits and risks. Developing countries should also consider the implications of the potential increased ease of their residents holding CBDC issued by a reserve currency-issuing central bank and transacting in foreign currencies, as this

can reduce seigniorage, worsen the transmission of monetary policy and help users to evade financial regulations.⁵⁴

5. Global governance and policy coherence

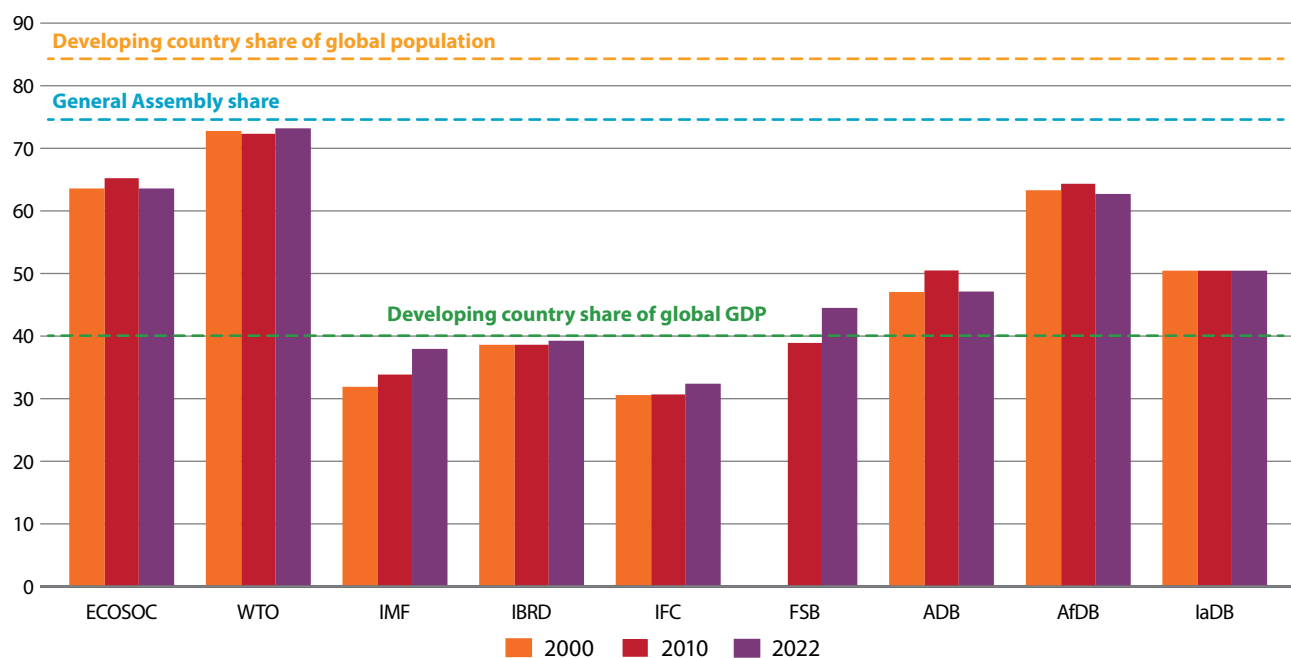
Global economic governance reform has been one of the central topics of international financial architecture reform since the beginning of the financing for development process. The current arrangements for global economic governance have been in place—and remained largely unchanged—for almost 80 years. Such arrangements have not entirely kept pace with changes in the global economy, including the rise of the global South and other geopolitical shifts. Member States have repeatedly sought to address this issue in the United Nations precisely because the organization operates on the principle of universal inclusion and sovereign equality. In the Monterrey Consensus, Member States adopted a commitment to broaden and strengthen the participation of developing countries and countries with economies in transition in international economic decision-making and norm setting. This commitment has been repeated in many intergovernmental agreements over the past two decades, including in the Addis Agenda. Reforms to the governance arrangements, depending on their size, may change the power balance at

international institutions, allowing different policies to be adopted on the issues addressed in this chapter and elsewhere in this report.

Despite repeated commitments and some improvement between 2005 and 2015, developing countries' representation has not significantly changed in many international financial institutions, regional development banks and standard-setting bodies. Member States intensified the discussion of increased participation of developing countries in international economic decision-making after the Monterrey Consensus, and some progress was achieved across several institutions (figure III.F.10). The realignment of voting rights at the IMF was achieved based on agreements adopted in 2005 and 2010. Change at the World Bank Group was accomplished through a selective capital increase agreement in 2017. There was a major revision of voting rights at the World Bank's concessional arm, the International Development Association (IDA), in 2021, its first in over 50 years. For its part, the FSB increased the number of plenary seats allocated to developing countries. Yet, the largest developed countries continue to hold de facto veto powers in the decision-making bodies of international financial institutions. After gains in the period following the 2008 world financial and economic crisis, several international standard-setting bodies have experienced stagnant or declining representation of developing countries on their principal decision-making organs in recent years (figure III.F.11). The recently concluded IMF Sixteenth General Review of Quotas was closed without any agreement to realign voting rights.

Figure III.F.10

Developing country share of voting rights, select institutions, 2000-2022
(Percentage)



Source: UN DESA.

Notes: The International Monetary Fund (IMF), International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), Asian Development Bank (ADB), African Development Bank (AfDB), Inter-American Development Bank (IADB) show the percentage of voting rights. The Financial Stability Board (FSB) does not have voting rights, and thus data shows the number of seats at the plenary. All data is categorized according to the M49 classification of developed and developing regions.

Complementary reforms to increase the voice and improve the participation of developing countries have been adopted, but tangible change on other aspects of governance remain out of reach.

Since 2000, both the World Bank and the IMF⁵⁵ have expanded the size of their boards of executive directors to create space for more developing country representatives. The follow-up process to the financing for development outcomes has also increased the economic and financial dialogues among the major United Nations bodies, the World Trade Organization, the World Bank and the IMF. The specialized standard-setting bodies and the FSB have also improved and institutionalized their consultative structures to receive input from regional bodies.⁵⁶ As suggested in the Monterrey Consensus, the ad hoc groupings of countries, for example the G20, are conducting outreach to non-member countries and finding new ways to incorporate developing country views, such as making the African Union a new permanent member of the G20. The Addis Agenda also contained a commitment to open and transparent, gender-balanced and merit-based selection of international financial institution heads and to the enhanced diversity of staff; while there have now been two women leaders of the IMF, the IMF managing director has always hailed from Europe and the World Bank president has always been a citizen of a single country.

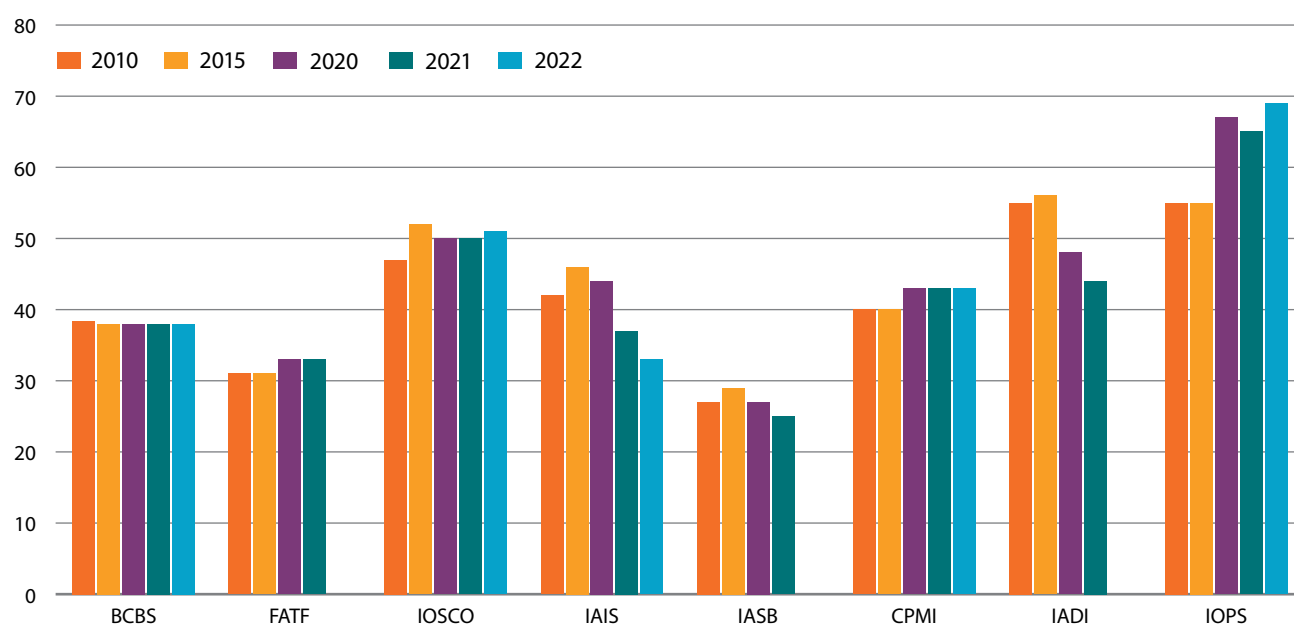
System-wide coordination and policy coherence remain a challenge in a complex geopolitical landscape, with increasing risks of fragmentation.

All the financing for development outcomes have referenced the importance of enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development. The Addis Agenda advanced this understanding to include “all three dimensions of sustainable development”. The follow-up process has enhanced coordination among international institutions, including in the joint work undertaken by the Inter-agency Task Force on Financing for Development and participation in the annual United Nations Economic and Social Council on Financing for Development Follow-up. However, other geopolitical pressures, including war and conflict, have complicated the work of international and intergovernmental bodies. There are significant risks of the world fracturing into multiple rival geopolitical blocks with lower levels of trust and cooperation. This may have direct costs in reduced growth and trade,⁵⁷ as well as indirect costs in reduced trust in multilateralism, weaker social contracts and inability to address global challenges such as climate change. The Fourth International Conference on Financing for Development will provide a venue to directly address these risks and continue to build policy coherence aimed at delivering on the ambitious and transformative 2030 Agenda for Sustainable Development.

Figure III.F.11

Representation of developing countries in standard-setting bodies, 2010–2022

(Percentage of voting rights or members)



Source: UN DESA.

Notes: The main international SSBs include the Basel Committee on Banking Supervision (BCBS) for standards on banking regulation; the Financial Action Task Force (FATF) for standards on combating money laundering, terrorist financing and other related threats to the integrity of the international financial system; the International Organization of Securities Commissions (IOSCO) for standards on securities regulation; the International Association of Insurance Supervisors (IAIS) for standards on insurance industry regulation and supervision; the International Accounting Standards Board (IASB) for accounting standards; the Basel Committee on Payments and Market Infrastructures (CPMI) for standards on payment, clearing, settlement systems and related arrangements; the International Association for Deposit Insurers (IADI) for deposit insurance standards; and the International Organisation of Pensions Supervisors (IOPS) for pension regulation.

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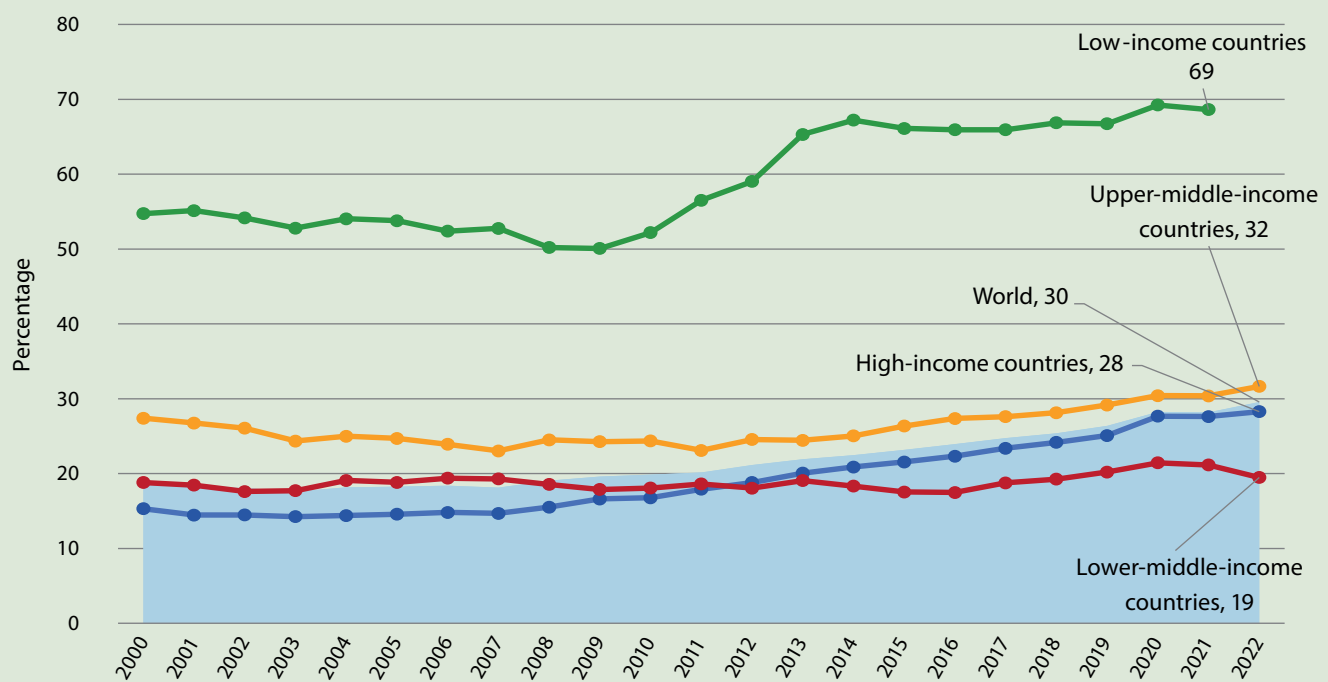
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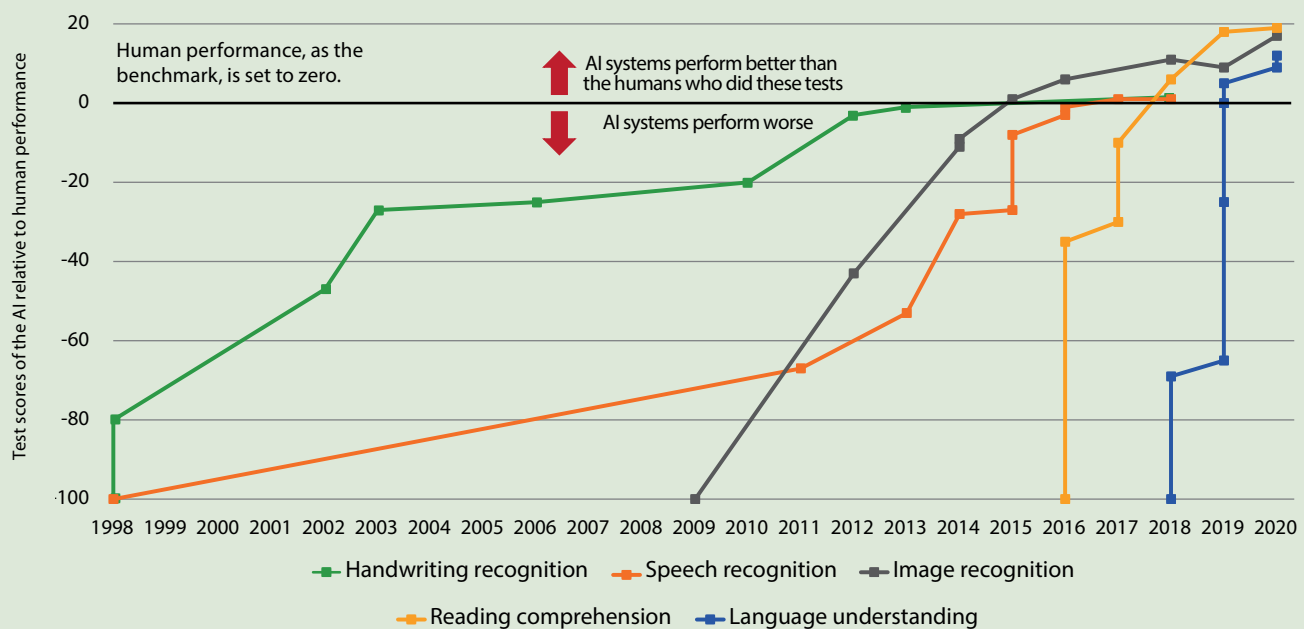
Science, technology, innovation and capacity building *in numbers*

Technological advances have made significant contributions to the SDGs, including increasing renewable energy's share in electricity production.

Share of electricity production from renewable sources

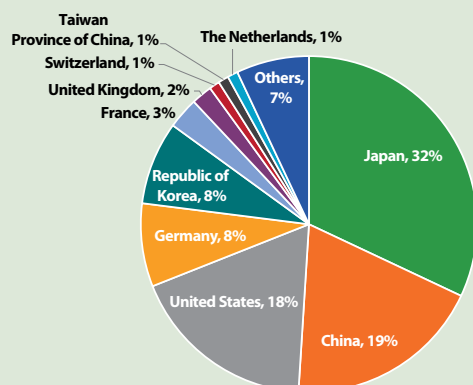


Over the past two decades, there has been a rapid advancement in the global technological frontier, illustrated by the development of artificial intelligence.



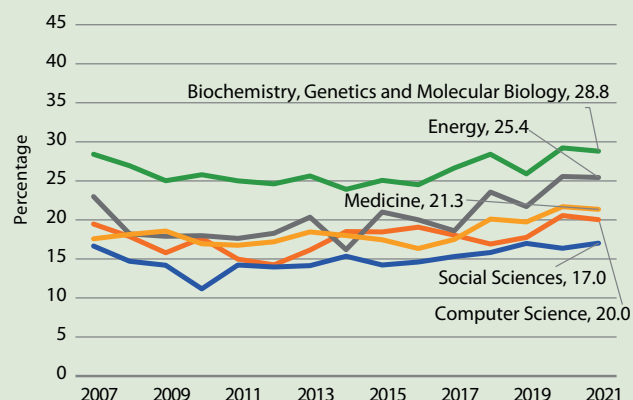
Innovation remains highly concentrated, exemplified by the green technology sector where industrial firms from just seven countries account for 90 per cent of all patenting activities.

Green patenting of industrial firms, 2022



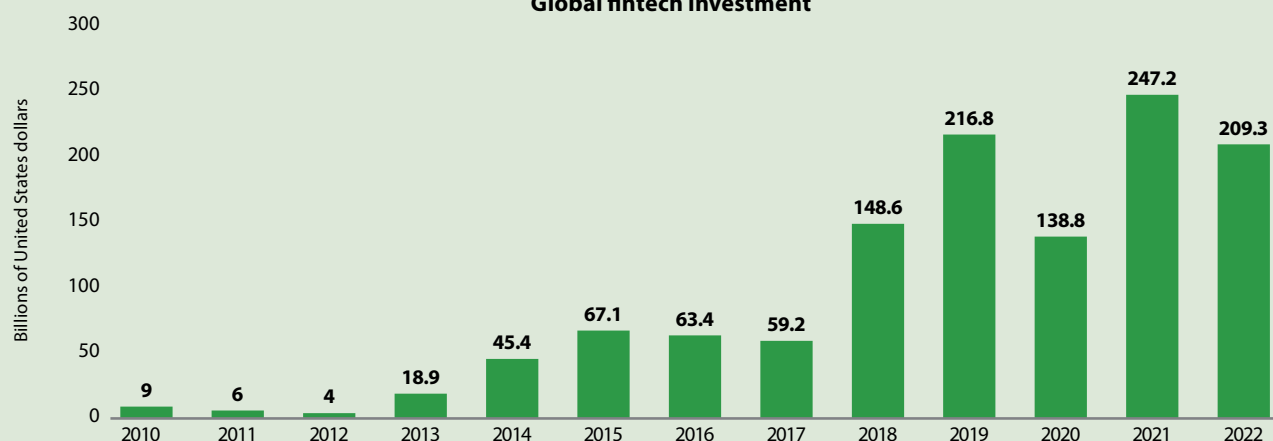
Many developing countries have experienced limited progress in international scientific cooperation, affecting technology diffusion.

Share of scientific publications in middle-income countries involving international collaboration, median

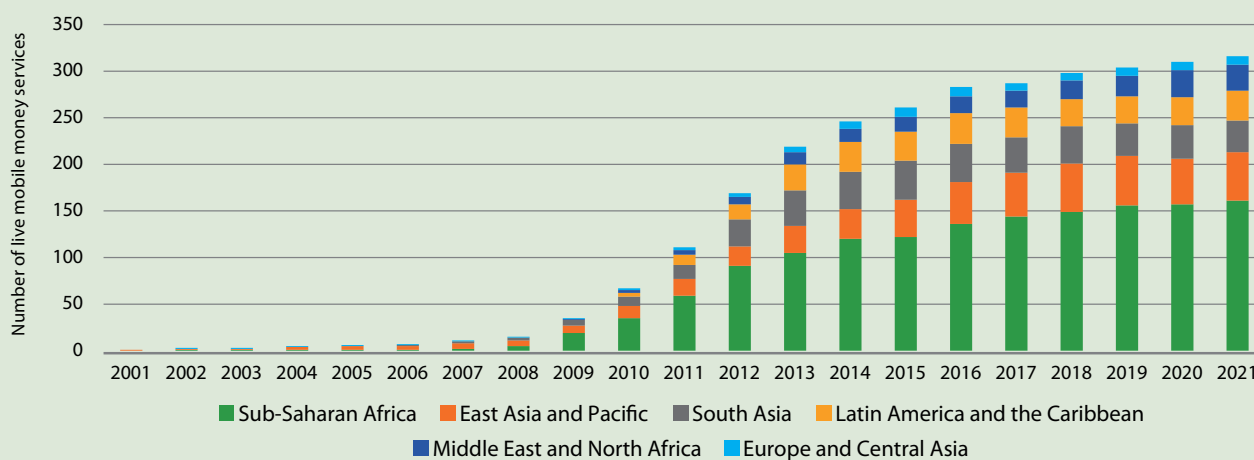


From 2010 to 2022, global fintech investment increased 23-fold, with technological innovations boosting financial inclusion but also presenting new challenges.

Global fintech investment



Globally, the number of mobile money service increased from 1 in 2001 to 316 in 2021, strongly driven by developments in sub-Saharan Africa.





Chapter III.G



Science, technology, innovation and capacity building

1. Key messages and recommendations

Technology holds great promise in advancing sustainable development and improving resilience.

Advances in technological progress have expanded economic opportunities, enhancing productivity, creating new industries and business models and contributing to poverty eradication. Science, technology and innovation (STI) have made significant contributions to safeguarding people's well-being, saving millions of lives during the COVID-19 pandemic. Technologies are also keeping hopes alive that the world can still address some of the most critical environmental threats that the planet is facing, such as climate change and biodiversity loss. The past two decades have seen the transformation of artificial intelligence (AI) from a niche field to a central pillar of technological advancement; generative AI could accelerate and amplify the positive development impacts of technologies.

Although it offers significant opportunities, technological change can, however, have unintended consequences for economic, social and environmental outcomes and human rights. Labour market transformation spurred by technological advances demands careful policy responses to avoid significant job losses and greater economic inequality. Generative AI in particular could cause substantial job loss—with a disproportionate impact on the women's labour force. The misuse of technologies can infringe on human rights, including privacy, as AI-driven business models that rely on access to massive personal data are often inadequate at data protection. AI could also erode public trust in institutions through accelerating the spread of misinformation and disinformation and reinforcing biases. Furthermore, the environmental footprint of some frontier technologies can be significant, increasing energy consumption and water usage and resulting in a surge in electronic waste.

The benefits and costs associated with rapid technological change are unevenly distributed.

Innovation and technology diffusion between and within countries have been uneven, leading to disparate opportunities for countries and communities to harness technological advancements, with rapid technological change sometimes outpacing the ability of societies to adapt. Indeed, the global technological landscape remains characterized by a high geographic concentration of innovation. The top 10 countries for patent applications—as a rough proxy for innovation activities—have consistently accounted for at least 87 per cent of all patents since 1980. Recent data suggests this trend will continue and possibly become even starker with frontier technologies. The concentration of innovation activities does not inherently hinder global development, provided there is an adequate and effective diffusion of technology and knowledge. However, technology diffusion within and across countries has slowed down in the last few decades, partly driven by the increasing complexity of technologies and innovations that raises the level of required complementary investment in physical and human capital, infrastructure and institutions. Another reason is the complex intellectual property rights landscape that countries have to navigate. Geoeconomic fragmentation—as characterized by an increase in trade barriers, strategic interventions by governments, data localization and other measures—could also diminish international technology spillover.

The growing recognition of STI in driving development trajectories and achieving the Sustainable Development Goals (SDGs) necessitates a rethink of the role of STI policy within national and global development frameworks. Mission-oriented, multi-stakeholder STI policies should be placed at the centre of development frameworks. Such policies should aim to ensure effective coordination between technology

and other sectors, between public and private actors and across systemic levels (regional, national and international) to steer technological change towards addressing pressing development challenges.

To ensure innovation and technology diffusion patterns that are consistent with sustainable development, countries need to invest in education and training, infrastructure and institutions and to ensure appropriate levels of market competition and protection of intellectual property rights. It is also important to acknowledge that the provision of technology access does not automatically lead to its widespread adoption due to a lack of financing, inadequate technological awareness and literacy, behaviour inertia, and cultural and social norms. A gender-transformative approach is needed to close the gender-digital divide by addressing gender-related barriers to education and digital tools, and by ensuring online safety, security and privacy.

Financing plays a key role in advancing the development of innovation systems. Different types of financing are needed at different stages of technological progress, depending on the maturity of the technology industry and financial markets and the overall institutional environment of a country. Merit-based grants from government, seed funds, venture capital funds, crowdfunding, traditional banks and stock markets could all play a role as firms move along the innovation cycle.

International cooperation in STI has yielded successes but the formulation of the international STI agenda has historically skewed towards the perspective of developed countries. A shift towards a more inclusive and participatory approach is needed. STI cooperation at the international level is also limited by an overall lack of sizeable and stable funding. The notable fluctuations in official development assistance (ODA) for STI in multilateral organizations pose challenges for international cooperation particularly because STI initiatives typically require stability and long-term planning due to their extended operational timelines.

The rapid expansion of the financial technology (fintech) industry has facilitated greater financial inclusion, but significant gaps remain in access to credit and financial services while new risks have arisen. Policymakers need to create socioeconomic and institutional conditions, not least broader levels of equality, to ensure that all members of society can benefit from advances in fintech. At the same time, they also need to carefully monitor and address the emergence of new, powerful actors in the financial sector. The entry of major tech firms in finance has significant implications for financial market stability, competition, consumer privacy and financial integrity. Given the complex trade-offs among different policy goals, financial sector regulators need to work with industry regulators and competition and data authorities to strike an optimal balance.

The Fourth International Conference on Financing for Development provides an opportunity to address the enduring challenges that countries have faced in generating, accessing and applying technologies that advance sustainable development. The Conference presents an opportunity to identify and address domestic and international hurdles that limit countries' capacity for innovation and technology absorption, and that lead to entrenched asymmetries between countries and firms in the global technology landscape. The Conference could also identify principles to direct the design, execution and evaluation of frontier technologies, including AI-based tools, within the fintech industry.

There are two main sections in this chapter. The first section highlights some of the development opportunities and challenges that technology brings. It will discuss the rapid evolution of the global technology frontier and the uneven innovation and technology diffusion between and within countries. The section will conclude with a discussion of policy areas where concerted efforts are needed to ensure the overall positive and inclusive impacts of technology, as well as the United Nations system's role in supporting capacity-building in countries. The second section will narrow the scope to fintech. It will include an overview of the evolving landscape of fintech, following by a discussion of its impacts and policy implications in the areas of financial inclusion, market stability, competition, consumer privacy and financial integrity.

2. The transformational but uneven impacts of rapid technological change

2.1 STI as a key driver of progress on the SDGs: Opportunities and challenges

Technology has made important contributions to the pursuit of the SDGs, but unintended consequences of technological progress can also impede progress. STI is contributing to improving people's lives, promoting prosperity and protecting the planet. Technology has dramatically improved information flow, supporting people to make economic choices that improve productivity and reduce poverty. It has improved health outcomes and longevity, including saving millions of lives during the COVID-19 pandemic. Moreover, by supporting more real-time evaluation of risks and risk-absorbing capacity, technology also improves the resilience of countries and communities, safeguarding economic, social and environmental advances. At the same time, technological progress can have unintended consequences and its benefits are unevenly distributed, exacerbating inequalities across multiple dimensions.¹ The pursuit of efficiency—enabled by structural changes and technological advances—often comes with significant social and environmental costs. The main challenge for policymakers is thus to mitigate these risks and ensure that technology acts as a catalyst for positive transformation and the realization of the SDGs through a “mission-oriented” STI approach (see section 2.4).

The evolution of the financing for development agenda reflects the growing recognition of the dramatic and potentially transformative impacts of technologies on development progress and on development finance itself. STI has always been considered a key means of implementation for sustainable development; in a major expansion of the financing for development outcomes, STI and capacity-building were added as a separate action area in the Addis Ababa Action Agenda in 2015. The Addis Agenda stresses the importance of public policies and finance to spur innovation and notes with concern the uneven innovative capacity, connectivity and access to technology that exists within and between countries.

Implications for the pursuit of the SDGs: People, planet, prosperity

Technological progress lies at the heart of economic growth, catalysing new industries and business models, expanding economic

opportunities and enhancing productivity. Over the past 25 years, the impacts of novel technologies, foremost digital technologies, on the economy and society have been profound and multifaceted, reshaping fundamental aspects of market transactions and value creation.² Advances in technology have also supported progress across the SDGs. These contributions are too many to note in this report; some prominent examples are listed below.

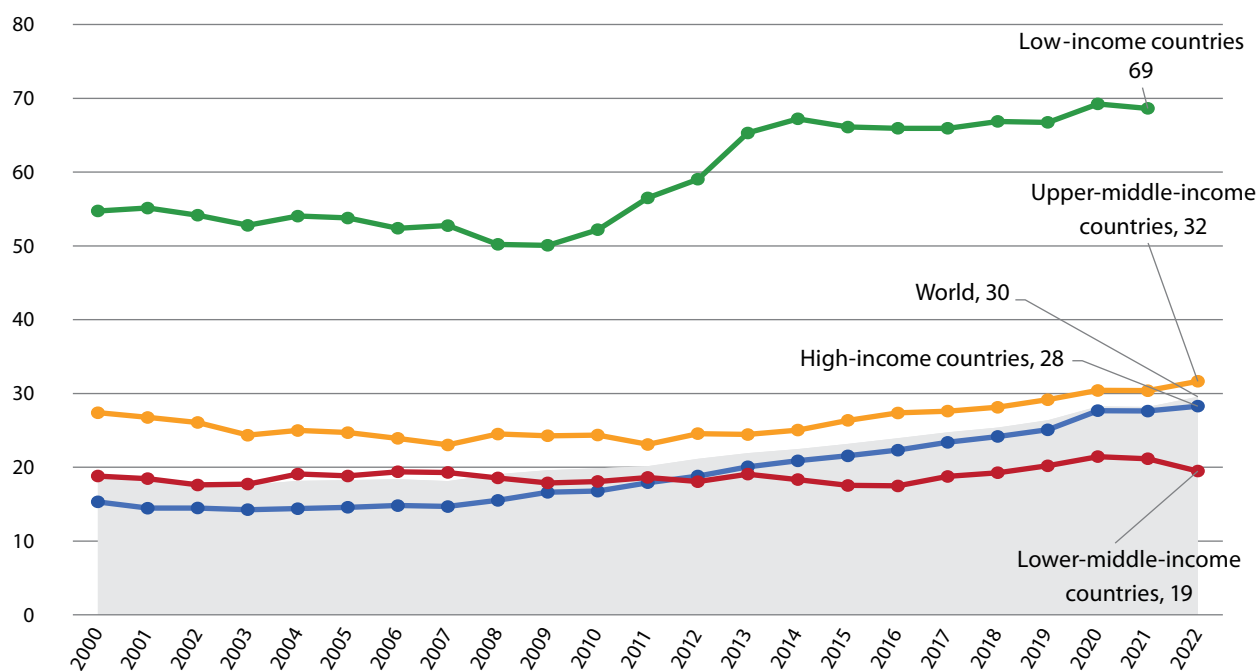
Technological advances have made dramatic contributions to safeguarding people's well-being, with advances in healthcare a prominent example. COVID-19 vaccines saved over 14 million lives globally during the first year of their administration.³ Several of these vaccines deployed mRNA technology, which is now also being used to develop vaccines for dozens of other diseases. Going forwards, integration of AI with other cutting-edge technologies could significantly improve the assessment and management of health risks, leading to the development of more effective healthcare strategies. AI also improves gene-editing tools and expands the ability to modify biological systems, which paves the way to address some of the most difficult medical challenges that humanity faces. Advancements in DNA sequencing technologies, coupled with the steadily declining costs of sequencing procedures, are unlocking new possibilities for genetic therapies targeted at diseases like HIV, beta thalassemia, cancer and more.

New technologies are keeping alive the hope that we can still address some of the most critical threats facing the planet on the environmental front. Climate change and energy scarcity have catalysed

the rapid development of innovative, cleaner energy technologies and significant improvements in energy storage. Renewable energy technologies help to bring power to economically disadvantaged and remote areas, thanks to scalable and cost-effective off-grid solutions.⁴ Although the full potential of renewable energy remains untapped, its usage is growing as the technology improves and becomes more affordable (figure III.G.1).⁵ Two decades ago, renewable energy was often dismissed as too expensive or inefficient. Today, due to technological advancements, the costs of solar and wind energy have plummeted (figure III.G.2), making them competitive with traditional fossil fuels. For example, solar photovoltaic was 710 per cent more expensive than the cheapest fossil fuel-fired solution in 2010, but in 2022 it cost 29 per cent less than the cheapest fossil fuel-fired solution.⁶

A key component that enhances the efficiency of renewable energy sources is advanced energy storage technology, which minimizes energy waste. With the variable nature of renewable energy production from sources like wind, solar and tidal, the capacity to store substantial amounts of electricity and release it upon demand is essential. Concurrently, developments in battery technology, including increased energy density and faster recharging capabilities, are boosting the feasibility of electric vehicles (EVs) as a sustainable alternative to traditional internal combustion engine vehicles. Between 2010 and 2022, the global number of electric cars increased around 1,000-fold, with China a major force behind this dramatic increase (figure III.G.3).⁷ Moreover, the invention of new battery types is broadening the affordability and accessibility of a diverse range of EVs.

Figure III.G.1
Share of electricity production from renewable sources, 2000–2022
(Percentage)



Source: UN DESA elaborations based on Our World in Data (2023).

Note: Renewable energy sources in this chart include biomass, hydropower, solar, wind, geothermal and marine energy. The shaded grey area denotes the percentage of electricity produced through renewable energy globally.

Figure III.G.2

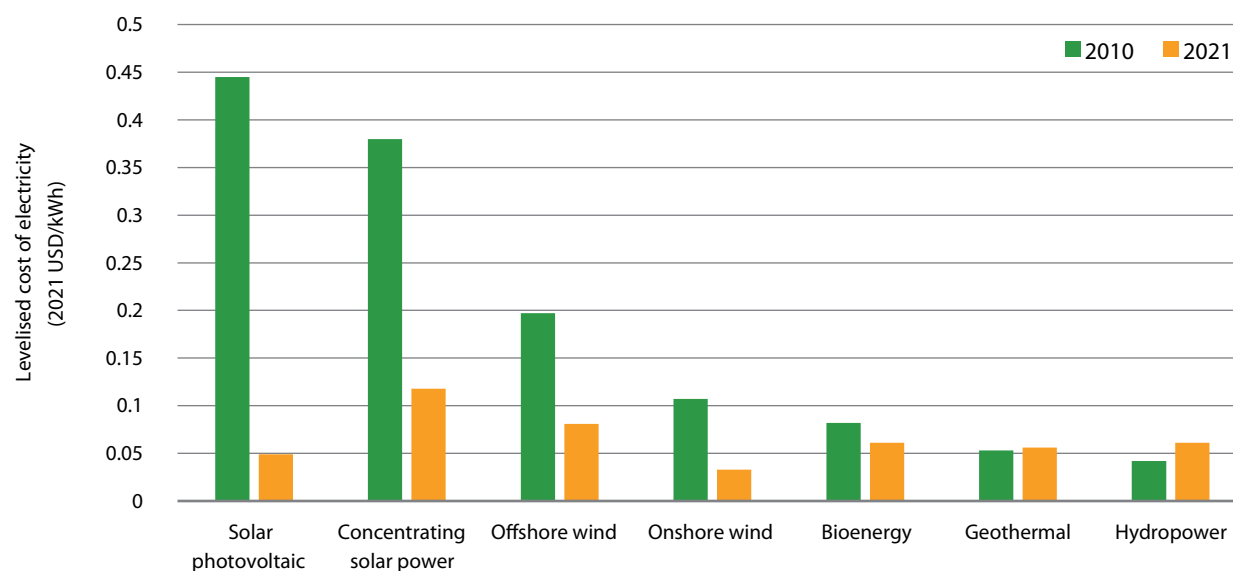
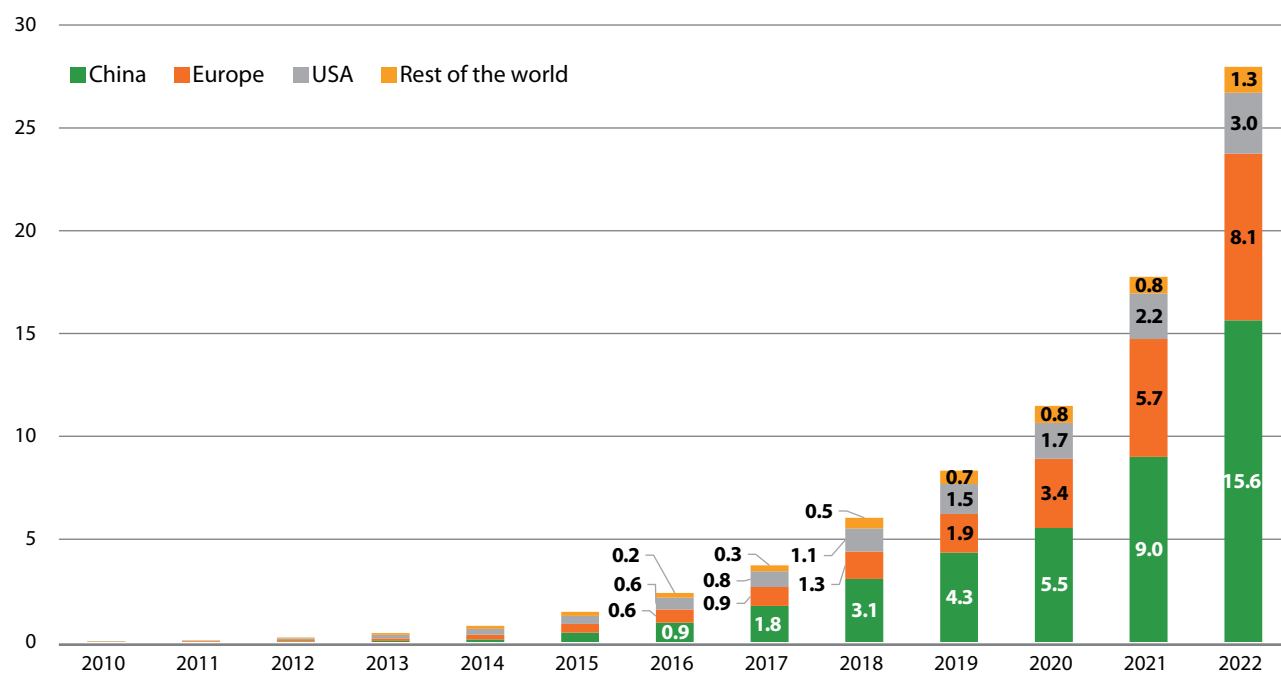
Global weighted average cost of electricity from renewable power technologies, 2010 versus 2021*(2021 United States dollar/kWh)***Source:** IRENA (2023).

Figure III.G.3

Global electric car stock, 2010-2022*(Millions)***Source:** UN DESA elaborations based on IEA's Global EV Outlook 2023 data.

Climate-smart agricultural practices—including those making use of nuclear science and applications—have been used to improve agricultural productivity and food security in the face of climate change.^{8 9} Agroecology and precision farming have helped to enhance resilience and adaption to changing climate conditions.¹⁰ Furthermore, innovative radiation technologies offer solutions to tackle plastic pollution, from isotopic tracing techniques for monitoring in the ocean to recycling plastic using radiation technology.¹¹

Digital technologies have also contributed to economic growth and poverty reduction. Digital technologies can reduce transaction and coordination costs, making market mechanisms more effective and increasing the scale and scope of individual firms.¹² The reduction in search costs in digital environments has greatly improved the scope and quality of searches and information diffusion,¹³ facilitating a more efficient and informed decision-making process as individuals and businesses can access a broader range of information and options with minimal effort.¹⁴ This has contributed to poverty alleviation efforts, for example through access to mobile money, which decreases the consumption poverty of households, with reductions greater among households headed by women.¹⁵ Another example is the use of mobile applications and digital platforms that allow smallholder farmers to access timely information on weather forecasts, market prices and agronomic practices, which empower them to make informed decisions and improve productivity, thus contributing to poverty eradication.¹⁶ Internet penetration is also associated with a reduction in the extreme poverty headcount.¹⁷

However, the benefits of technological progress are unevenly distributed and new technologies also create new risks and challenges across economic, social and environmental dimensions. For example, automation enabled by advanced digital production technologies has contributed to inequality—both by increasing the capital share of national income, with capital income less evenly distributed than labour income across households, and by favouring higher-skilled workers. These workers have skills that are more complementary to new technologies and can increase their relative productivity and wages, while automation increasingly displaces routine and repetitive tasks, thereby worsening wage inequality.^{18 19} The overall effect of automation on the labour market would depend on a range of factors, including labour scarcity and policy measures.²⁰

Automation also reduces the comparative advantage that many developing countries enjoy due to lower labour cost, necessitating new development strategies. More automated production processes that rely less on labour diminish the labour cost-based comparative advantage that many developing countries have exploited to integrate into global production networks and value chains. As labour costs become less relevant, this could lead to reshoring of production to developed countries; recent empirical evidence suggests that the impact of automation on reshoring is indeed positive and significant.²¹ This puts the pursuit of development models based on export-oriented industrialization into question. Many developing countries are now facing the prospect of “premature deindustrialization”, which entails the shift into service-based economies without experiencing an extended period of industrialization that is crucial for improving overall economic productivity.²²

The misuse of technologies can threaten human rights. Technologies like AI that rely on massive amounts of data for training, while

transformative, can infringe on human rights, including but not limited to privacy. Private information revealed to an AI chatbot could be stored and reused for model training without users’ knowledge.²³ In recent years, breaches and leaks have occurred in the databases of corporations that hold the personal data of millions of customers, exposing them to risks of identity or financial fraud. Furthermore, AI-based moderation tools allow social media platforms to quickly censor unfavourable opinions, curtailing freedom of expression.

Without careful management, the environmental footprint of frontier technologies can also be significant.²⁴ Increased data consumption results in higher global electricity and water usage by data centres and distributed ledger technologies. The prevalence of electronic products such as smartphones and small-scale, off-grid solar panels with a short working life also raises growing concerns over the adverse environmental impacts of critical mineral extraction and electronic waste.²⁵ All these pose substantial environmental challenges, especially for developing countries.²⁶

Enhancing resilience

Technologies can enhance resilience and help to preserve hard-earned development gains. The recent period of cascading crises has underlined the importance of improving resilience against shocks. Economic, social and environmental gains made over years can be quickly reversed in crisis times if countries are inadequately prepared to detect, absorb and recover from these adverse shocks.

Technologies can deliver more efficient, rapid and reliable resilience evaluations and enable better decision-making during and after shocks.^{27 28} For example, data can enhance the planning, design and maintenance of resilient infrastructure by supporting more accurate projections of population growth, urbanization and climate change impacts.²⁹ The Internet of Things helps to collect, communicate and process real-time data, generating faster warnings and enabling more rapid emergency and policy responses. Mobile phone-based communication and alert systems help to enhance risk-informed communication, which improves the accuracy and timeliness of disaster risk information and has increased community participation in disaster risk reduction.³⁰ AI allows machines to learn and accumulate experience. This can help to automate the process of improving data collection and processing. For example, drones for remote automated collection of videos and photographs can use AI algorithms to instantaneously interpret the condition of infrastructure, enabling more accurate real-time assessment of hazardous conditions.³¹ Drones can also be used to deliver emergency supplies in the case of collapsed infrastructure or dangerous or remote locations.

2.2 Rapid evolution of the global technology frontier

The global technology frontier has evolved rapidly in recent decades. Rapid technological advancements have occurred along with increasing innovation complexity³² and this pace is set to increase due to frontier technologies that range from AI to biotechnology.

AI has transformed from a decades-old niche field of study to a cornerstone of technological advancement. In 2000, two AI development milestones were the creation of a robot that could recognize and simulate emotions with its face, and a humanoid robot that could

deliver trays to customers in a restaurant setting. At that time, no AI system could provide reliable handwriting, speech or image recognition at a human level, not to mention reading comprehension and language understanding. However, in the intervening years, AI has made significant strides, enabled by the exponential growth of data availability that, in turn, is made possible by the rapid rise in Internet penetration. Algorithms have evolved from basic pattern recognition to complex neural networks capable of deep learning. As figure III.G.4 shows, AI systems have made rapid progress in executing human tasks over the past two decades.³³ They have become steadily more capable in language and image recognition and outperforming humans in all these domains in a standardized test setting, even though they still perform worse than humans in some real-world cases.

Since the AI chatbot ChatGPT was released to the general public for testing in 2022, no AI technology has garnered more attention than generative AI—algorithms that can be used to create new content, including text, code, audio, images and videos.³⁴ The number of generative AI users has since soared and the upward trend is expected to continue going forwards, as the recent evolution of customized AI agents and multimodal and hybrid AI models can further extend the reach of the technology. It is projected that the generative AI market will grow from \$11.3 billion in 2023 to \$76.8 billion by 2030.³⁵

Generative AI has the potential to accelerate and amplify the positive and negative impacts of technology as was discussed in the previous section. For example, it can be used in drug discovery and molecular design, supporting the initial design phases of the material discovery processes that help to quickly produce candidates for experiments.³⁶ It can generate educational content such as quizzes, exercises and interactive simulations, which enhances the learning experience for students.³⁷ Generative AI can also be used to enhance the prediction and modelling of ecological changes and population dynamics, which enables researchers to create accurate, proactive strategies to protect endangered species. While the evidence remains tentative, generative AI could also

serve as a general-purpose technology that enhances the productivity of many sectors and the provision of public services, thus improving people's living standards. At the same time, its ability to engage in complex activities, such as coding, product design, creation of marketing content and strategies or analysis of legal documents, suggests that it could be highly disruptive in labour markets, affecting a wide set of work activities that have so far been considered “safe” from risks of automation—tasks that require expertise, social interaction and creativity. In this view, AI may be considered more threatening to some higher-skill workers who have skills sets that can be more easily replaced by the technology. On the other hand, in countries where such skills are scarce, AI could serve as a complementary resource to support development while these countries build up their human capital.

The labour market impacts of generative AI could vary widely across country income groups due to different occupational structures. In low-income countries, an ILO study estimated that only 0.4 per cent of total employment is potentially exposed to the automation effects of generative AI, whereas the estimate for high-income countries is 5.5 per cent.³⁸ The effects are also differentiated across gender. For example, in high-income countries, the share of jobs held by women that could potentially be automated by generative AI is 7.8 per cent, more than double the 2.9 per cent share of jobs held by men, as female-dominant occupation groups such as clerical jobs are most exposed to the technology. Meanwhile, the share of jobs with high augmentation potential—meaning jobs that cannot be completely automated and could be complemented by generative AI—is also greater for jobs held by women than for jobs held by men across all income groups. Similarly, an IMF study found that higher-income countries are more susceptible to the job displacement effects caused by AI adoption but are also better positioned to take advantage of its complementary effect on labour productivity.³⁹ Within countries, it was also concluded that women workers are more exposed to the effects of AI but have more potential for their work to be complemented by the technology.

Box III.G.1 Technology's disruptive impact on institutions

Technological change not only affects production processes but also impacts and—in some cases—transforms institutions, including rules and regulations, cultures and social norms. It can alter the balance of power between different public and private actors, including government, civil society and corporations. For example, the rise of social media has created a powerful channel for the public to voice its opinions in amplified ways that were inconceivable two decades ago. Public complaints communicated on social media platforms have been shown to elicit greater policy responses than complaints made through private channels.⁴⁰ Technologies—if properly employed—can improve public participation in the policymaking process and hold policymakers to account.

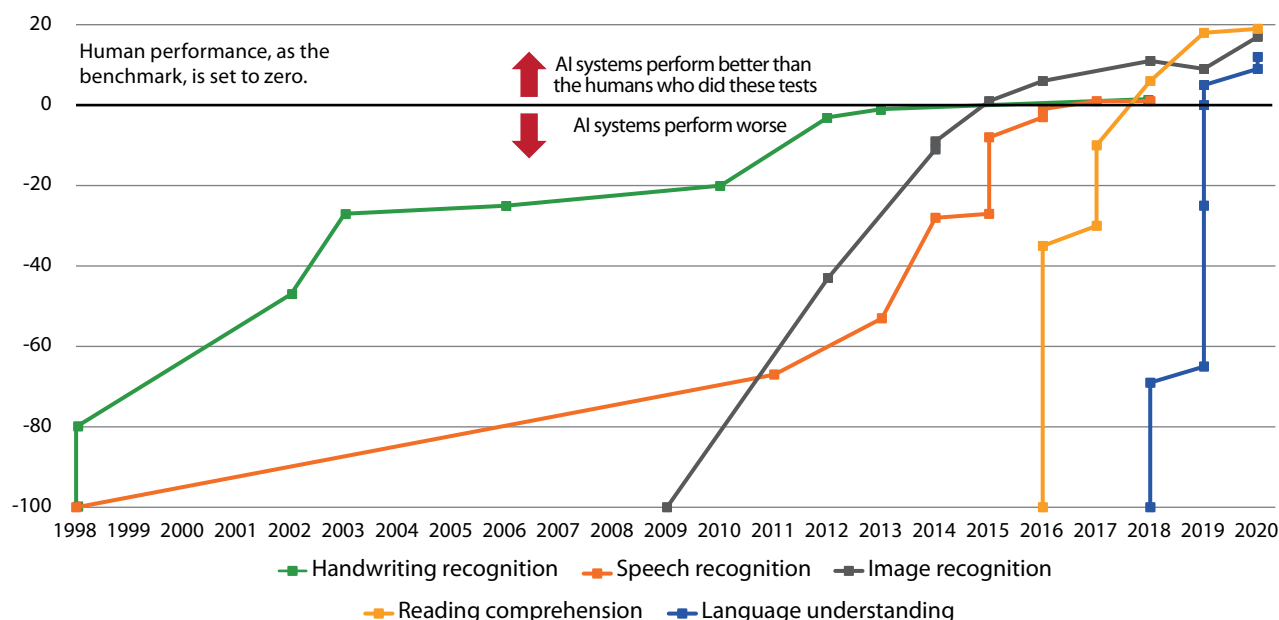
However, if misused, technology can undermine trust in institutions. It can destabilize political systems if it is used to undermine the quality and truthfulness of information that feeds into public debate. AI systems, if trained using data embedded with biases, can perpetuate

societal prejudices, leading to data-driven discrimination. For example, discrimination in lending by fintech lenders occurs through algorithmic scoring, with the lenders charging minority borrowers more for purchase and refinance mortgages.⁴¹ The rapid evolution of technologies also demands a more agile form of governance that can more quickly adapt to changing social, economic and environmental conditions. A lack of commensurate reforms to ensure that the governance model is fit for purpose will erode public trust in institutions.

Moreover, the growing dominance of major actors in technology sectors raises the risk of regulatory capture. Major firms could secure advantages over smaller rivals or new market entrants via political means, negatively affecting consumer welfare in the long run. Major social media firms also hold a central position in playing an intermediary role in public debates, including interactions between the public and governments, with the potential to shape political outcomes. The increased social and political influence of so-called Big Tech—sometimes across national borders—demands a rethink of technology policy and governance to ensure accountability, fairness and inclusiveness.

Figure III.G.4

Evolution of language and image recognition capabilities of artificial intelligence systems since the turn of the century (Test scores of the AI relative to human performance)



Source: UN DESA, adapted from Roser (2022).

Note: The capability of each AI system is normalized to an initial performance of -100.

Historically, technological advancements, although initially disruptive to the labour market, have ultimately contributed to economic expansion and job creation in the long term. Whether generative AI will yield a similar outcome will depend on investment in human capital and adjustment of economic structures and business models that allow workers to take advantage of such technology in their work, rather than being replaced by it. The aforementioned estimates of generative AI's employment effects also suggest that the direction of the gendered impact of the generative AI-induced labour market transition will hinge on how well the transition is being managed and whether the shift would lean more towards automation or augmentation.

Generative AI could also, however, become a powerful vehicle for misinformation and disinformation, further eroding trust in institutions and between people. Its affordability and accessibility lower the barrier of entry for disinformation campaigns.⁴² Generative AI can be used to manipulate the videos and messages of public figures, including government officials, in order to spread false information. Additionally, the easy access to generative AI tools can erode public trust in factual information, even when it is verifiable. As AI-generated content becomes more prevalent online, it could lead to increased scepticism among people, causing them to doubt the authenticity of any information, thus undermining the effectiveness of public debate that is central to good policymaking.

2.3 Persistent technological divide

Rapid technological advancement often coincides with growing inequality as the benefits from innovation are not equitably distributed across different geographies and demographics. This

historical trend has also played out with the rise of digital technologies over the past several decades. Developing countries, particularly the 45 least developed countries (LDCs), face a range of barriers both to creating new technologies and to accessing them: inadequate infrastructure, insufficient physical and human capital investment, lack of financing on the right terms, and missing or incomplete institutions. The development and use of frontier technologies in production is often concentrated in a few large companies, primarily from developed countries. This situation raises concerns about wealth concentration, market competition and potential abuses of market power, perpetuating inequalities over time.⁴³

High geographic concentration of innovation

The persistently high geographic concentration of research and development (R&D) and related assets—observed over the last decades—has first-order implications for the global economy and the technology divide.⁴⁴ The top 10 countries for patent applications have consistently contributed to at least 87 per cent of the worldwide total since 1980.⁴⁵ The dominance of the leading countries continues in frontier technologies.⁴⁶ For instance, 90 per cent of all patenting activity in the field of smart manufacturing is concentrated in 10 countries.⁴⁷ The concentration is even higher in green technology creation, with industrial firms from seven countries accounting for 90 per cent of all patenting activity (figure III.G.5).⁴⁸ With the exception of China, these countries are all high-income economies, which indicates a significant skew towards wealthier nations in terms of innovation and technological development. Moreover, what is notable is the high concentration of innovation activities and slow technological diffusion within these leading countries themselves, which indicates an even higher level of uneven distribution

of innovation and technology access at the more granular firm level (more discussion on this in a later section).

The geographic concentration of innovation and related innovation disparities are due to many factors, including capital (human, physical and financial), institutions, path dependencies, and business and research incentives. One important factor is the presence of localized knowledge spillovers.⁴⁹ Often, it is a dense cluster of successful firms, qualified suppliers and shared resource arrangements within a geographic area, particularly in cities with dense networks and diverse resources, that creates an environment ripe for innovation.⁵⁰ These entities, in close proximity to each other, engage in frequent and often informal exchanges of ideas and knowledge, creating a vibrant, interactive ecosystem that catalyses innovation. Indeed, empirical studies have shown that a greater pool of relevant technological knowledge in close geographic proximity of a firm significantly increases its chances of conducting innovation activities and the persistence of such activities.⁵¹ As these innovation clusters grow, they attract more resources and talent, often at the expense of other less established regions.⁵² This can lead to a self-reinforcing cycle where already successful areas continue to grow, while others lag behind.

Uneven access to and usage of technology between and within countries

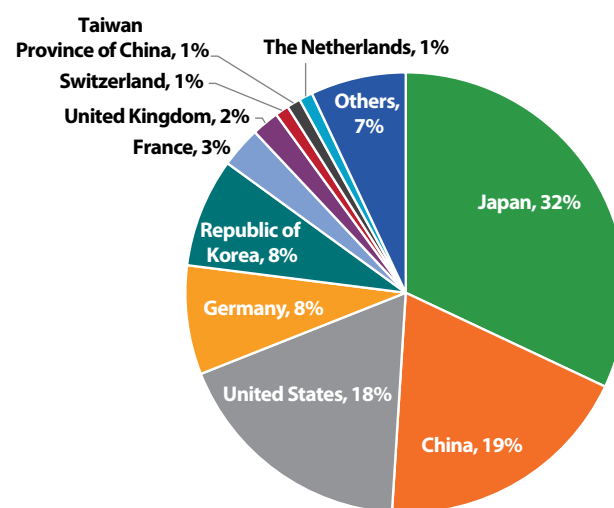
The concentration of innovation activities does not inherently hinder global development, provided there is an adequate and effective diffusion of technology and knowledge. However, technology diffusion has slowed down in the last few decades, both within and across nations, with major implications for productivity growth and broader sustainable development.⁵³

One possible driver of slow technology diffusion is the increasing complexity of technologies and innovations. Such complexity has raised the level of complementary investment in infrastructures, productive capital, skills and capabilities of the workforce that is necessary for technological innovations and successful adoption of new technologies.⁵⁴ It amplifies a longstanding obstacle to technology adoption in developing countries, which is the inadequate investment in the national innovation systems. This can be illustrated by the substantial disparities in internet speed and data use that impede digital gains for low- and middle-income countries.⁵⁵ For instance, in 2023, median broadband speeds in high-income countries were between five and ten times faster than those in low-income countries.⁵⁶ The frontier technology readiness index—a comprehensive measure to evaluate the capability of nations to effectively implement and benefit from cutting-edge technologies—has also shown that there is a persistent capability gap between lower-income countries and those at the capability frontier.⁵⁷ While the capability of many upper-middle-income and some lower-middle-income countries moved closer to the frontier between 2008 and 2021, the gap between the capability of low-income countries and the frontier remains as great as ever (figure III.G.6).

There is also a noticeable slowdown in technology transfer between developed and developing countries.⁵⁸ While the international protection of intellectual property rights provides important flexibilities, it remains tight and complex, making it difficult for developing countries to access technologies that support sustainable development

Figure III.G.5

Green patenting of industrial firms, by country of owners, 2022
(Percentage)



Source: UN DESA elaborations based on Lavopa and Menéndez (2023).

Note: Green patents are broadly defined here as technologies or applications that mitigate or adapt to climate change.

and to manage their own innovation systems.⁵⁹ Even within countries, there is a persistent gap in technology adoption and use between “frontier firms” and the rest of the economy.⁶⁰ Frontier firms lead technological adoption, leveraging cutting-edge technologies to enhance productivity and competitiveness. However, the rest of the economy, particularly small- and medium-sized enterprises (SMEs), often struggle to keep pace with rapid technological changes. A similar pattern can be observed with regard to diffusion of AI technologies. While global firm-level surveys have suggested a broad-based adoption of AI technologies in business operations across regions,⁶¹ national firm-level surveys show that the adoption of AI is predominantly done by large firms.⁶² This suggests AI adoption is highly uneven within countries, including in developed ones.

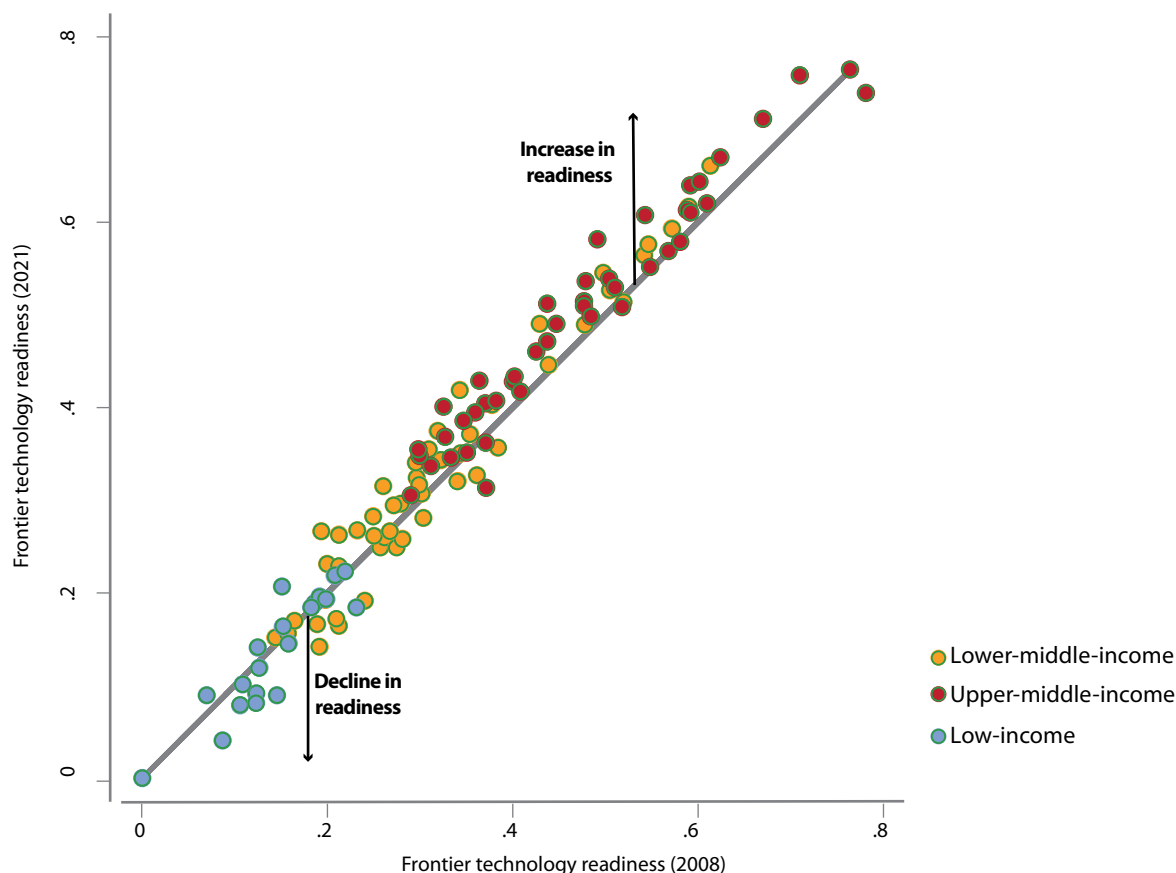
A specific barrier to widespread adoption of AI technology is that the current leading AI models are trained mainly on knowledge produced by and relevant to developed countries. It reflects the reliance of researchers on Internet data for model training, which is predominantly in English and a small group of other languages.⁶³ As such, outputs of these models might be less useful for developing countries, which could further exacerbate the technology divide. This will have to be addressed by training AI models using data that is more relevant to specific regions or countries. Singapore’s Southeast Asian Languages in One Network (SEA-LION) model—a family of large language models that are specifically trained for the Southeast Asia region—is an example of such an initiative.⁶⁴

Innovation and technology diffusion amid geoeconomic fragmentation of the global technological landscape

Geoeconomic fragmentation puts global integration, STI cooperation and technology diffusion at risk (see chapter II and chapter III.D

Figure III.G.6

Frontier technology readiness, 2008 versus 2021



Source: UN DESA calculations based on UNCTAD's Frontier Technology Readiness Index data.

Note: Each dot represents a country. A country that stays below the 45-degree line means that its frontier technology readiness declined in 2021, compared to 2008. Conversely, a country that stays above the 45-degree line means readiness improved in 2021.

for discussions on other impacts of such fragmentation).⁶⁵ Data on trade barriers, for example, shows signs of such fragmentation: After declining for most of the twentieth century, trade restrictions have significantly increased in the past few years.⁶⁶ Technology and innovation, which have long been central to geopolitical competition, are particularly vulnerable to geoeconomic fragmentation. The quest for technological leadership has historically been a strategic imperative for nations, often involving efforts to prevent critical technologies from being acquired by strategic competitors.⁶⁷

Trade barriers to high-tech inputs and services, strategic intervention by governments, limited market access, data localization and other measures could diminish international technology spillover and discourage R&D investment. This disruption could lead to a widening technology gap between nations, undermining the global technological progress that has been made over decades. Even for countries at the technological frontier, protecting critical technologies from foreign competitors is becoming increasingly complicated, as technological innovation is now characterized by a high degree of interdependence and multinational collaboration. In attempting to prevent others from accessing sensitive technological applications, these countries may inadvertently risk undermining their own technological capabilities.

2.4 STI policy, international cooperation and capacity-building

Evolution of STI policy approaches

There is a wide diversity of STI policies across different countries.

This diversity reflects the unique political, economic and cultural contexts of each country that shape their distinct strategies in advancing STI. Yet two broad overall approaches can be distinguished: narrower STI policy approaches that focus on addressing market failures, such as information asymmetries and non-rivalry in the use of technology knowledge; and a broader innovation system approach that aims to address system failures that impede learning and innovation.⁶⁸ These systemic failures include infrastructural (such as physical and science and technology infrastructure), institutional (which includes “hard” institutions such as regulation and the legal system and “soft” institutions such as social norms and values, entrepreneurial culture, and so forth), network (which concerns the interaction between actors in the innovation system), and capabilities (which include competencies and resources).

Beyond addressing market and systemic failures, there is a growing call for STI policy to put greater emphasis on directing

technological change to address development challenges. This also reflects the better understanding of technologies' potential and the importance of STI policy directed at addressing major social challenges in driving development progress. The SDGs can serve as a natural benchmark for this "mission-oriented" STI policy approach; and detailed proposals have been put forth for how countries can develop related STI policy roadmaps for achieving the SDGs.⁶⁹ The evolution towards the mission-oriented approach also means that STI policy needs to be placed at the centre of national and global development frameworks to enable policymakers to better address policy coordination problems, including between technological and sectoral systems, between government agencies and private institutions and across systemic levels (regional, national, international).

Supporting innovation and technology diffusion

Concentrated innovation activities and weak technology underline the need for policies that facilitate access to new technologies and support the capacity of economies, households and businesses to adopt and harness these technologies effectively. There needs to be a concerted push for investments in education, training and reskilling programmes as well as in infrastructure and institutions that strengthen innovative and absorptive capacity, which include context-appropriate competition policy and protection of intellectual property that respects the international legal norms.

To ensure that technological advances are geared towards addressing pressing development challenges, the innovation process should involve a diverse group of researchers, end users and intermediaries who can translate needs and values between producers and users. Gender parity in research, and science, technology, engineering and mathematics (STEM) fields needs to be improved, given the significant underrepresentation of women in these fields (with only one in three researchers globally women; and just over one fifth of all science, engineering, and information and communication technology (ICT) jobs held by women). A notable example of international cooperation on this front is the Equity 2030 Alliance launched by the United Nations Population Fund (UNFPA). The Alliance, a global effort to accelerate gender equity in science, technology and financing solutions by 2030, convenes entities and industries across the globe to take action with the aim of closing gender equity gaps by 2030. The joint effort enables entities to share and learn from best practices, ensuring the inclusion of women in all their diversity throughout the innovation lifecycle of solutions.

Minimizing the unequalizing effects of technologies should more generally be a core objective of STI policy. In light of the potentially dramatic labour market impacts, STI policies should guide technological development to be labour-complementary rather than labour-replacing. To this end, countries can consider measures such as improving tax codes to equalize the marginal tax rates for hiring and training labour, investing in equipment and software, increasing the voice of workers and directing funding for more labour-complementary R&D.⁷⁰ Compensatory mechanisms are also important where the adoption of new technologies produces both winners and losers. Social protection plays a key role here, as does education and training that equips workers with the appropriate skills and supports them in transitioning to new jobs.

Financing for innovation

Financing plays a central role in supporting innovation and technological diffusion as well as guiding technological change.

Different types of financing are needed to fund innovations, depending on the maturity of the technology and financial markets and the overall institutional environment of a country.⁷¹ Basic research and science is mostly publicly funded; but even in the initial phases of product development, where failure risk is high, funding often comes from merit-based public grants or from equity investors. The latter usually involves participation from angel investors, seed funds and venture capital funds and permits investors to oversee business operations and exert considerable control to mitigate investment risks. In the past two decades, crowdfunding through digital platforms has also gained traction as a novel funding method for early-stage innovation. Only as innovative projects progress to more advanced stages of development does the role of traditional financial intermediaries like banks and capital markets become more prominent.

To spur innovations that advance sustainable development and ensure public access to such innovations, the public sector can and should play a key role in financing and incentivizing research.

Public financing allows innovators to recover R&D costs without having to rely on selling their innovations in private markets that could limit diffusion. This can be secured through direct financing (for specific research activities), decentralizing direct financing (e.g. tax credit for research) or a prize financing system (i.e. government awards a prize for successful innovation).⁷² Governments can also use these financial tools to promote socially and environmentally desirable technologies and to maximize public benefits.⁷³

Ensuring sufficient innovation and technology diffusion also requires appropriate market competition and protection of intellectual property rights. Competition authorities need to consider both ex ante measures that focus on developing the necessary environment for healthy market competition and ex post measures that target specific incidences of anticompetitive behaviours.⁷⁴ These considerations must account for changes in how firms compete in the new era of the data economy and the implications for consumer welfare.⁷⁵ Intellectual property systems play an important role in creating a conducive and reliable environment for the transfer of technology, and they need to be tailored to a country's stage of development and technological capability, as noted in the *Financing for Sustainable Development Report 2023*. Governments' innovation and intellectual property policies should take advantage of the flexibilities provided in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) to support technology diffusion. Countries can also consider other intellectual property approaches that might serve them better to mitigate the trade-offs between incentivizing R&D investment and facilitating the spread of the innovations. These could include the knowledge commons approach that underpins the "open source" movement and a public finance-driven innovation approach.

Access does not automatically translate into widespread adoption.⁷⁶ Even when new technologies are markedly superior to existing options, they have not always been widely embraced. In this context, there is a growing recognition of the critical role of feedback loops between supply and demand in the innovation process and specifically how user feedback can effectively guide the allocation of resources and innovation capabilities to meet the needs of society or the market.⁷⁷ Other factors

hindering demand for welfare-enhancing technologies also need to be tackled, such as lack of financing, inadequate technological literacy and awareness of new technologies, behaviour inertia, and cultural and social norms.⁷⁸ Gender-transformative approaches must be at the centre of efforts to increase technology adoption and close the technology divide: addressing gender-related barriers to education and digital tools, meeting women and girls where they are and embedding digital skills into existing programmes; equipping educators with inclusive, gender-responsive ICT integration skills; and ensuring safety, security and privacy online.⁷⁹ Such efforts all require narrowing the gender gap in Internet access. In 2022, only 63 per cent of women were using the Internet compared to 69 per cent of men; and the gap was even greater in lower-income countries, with 21 per cent of women online compared to 32 per cent of men.⁸⁰

International cooperation and capacity-building

Growing technological complexity, the fast pace of technological change and its significant impact across countries call for a collaborative approach to STI. A plethora of cross-border initiatives have been established over the past 20 years. At the regional level, some notable initiatives include the ASEAN Plan of Action on Science, Technology and Innovation 2016–2025, the African Union's STI Strategy for Africa 2024, and the Asia-Pacific Economic Cooperation's Policy Partnership for Science, Technology and Innovation. Also of note are successful experiences with international collective research, which equitably incorporates the views and priorities of different partners. For example, the European Organization for Nuclear Research (CERN) and the Consultative Group on International Agricultural Research (CGIAR) offer useful references for the

design and operation of inclusive and equitable collaboration mechanisms based on open science and co-creation. The IAEA Nuclear Harmonization and Standardization Initiative is an example of a platform that facilitates regulatory collaboration among countries.

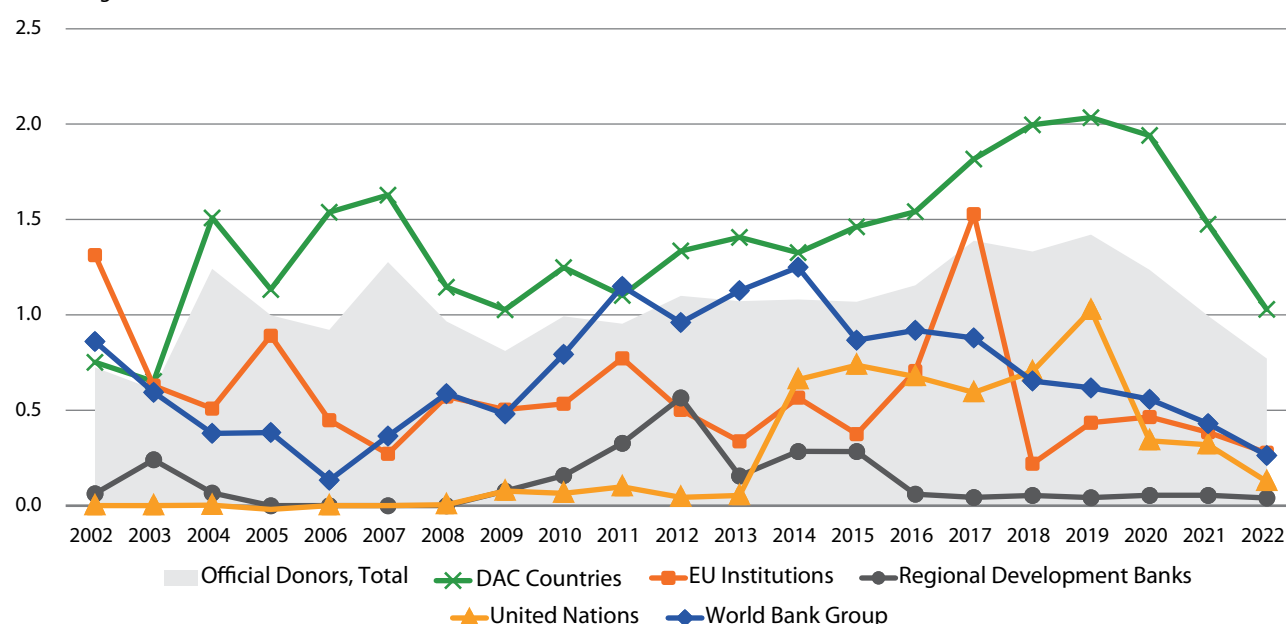
Despite the success of these initiatives, the formulation of the international STI agenda and the evolution of the global innovation system have historically been skewed towards the perspective of developed countries.⁸¹ A shift towards a more inclusive and participatory approach is therefore needed. This requires stakeholder engagement and practical support measures to create a collaborative setting for facilitating exchanges of knowledge among different actors and recognizing the needs of countries with fewer resources.

International cooperation in STI remains limited by a generalized lack of sizeable and stable funding. In terms of concessional financing for STI, the share of ODA in STI did not appreciably increase between 2002 and 2022 (figure III.G.7). Including all official donors, while the share of STI in total ODA increased between 2016 and 2019, it has since declined and in 2022 reached its lowest point since 2003. ODA for STI is also very volatile.

International cooperation on scientific research also diverges between country groups. Whereas high-income countries have seen a broad-based increase in international cooperation across different fields of STI over the past decade or so, many developing countries—with the exception of some larger developing economies—have seen limited progress (figure III.G.8). This partly reflects the limited STI capacity of many developing countries, which hinders their efforts to engage in cross-border collaboration.

Figure III.G.7

Share of official development assistance related to science, technology, and innovation, 2002–2022
(Percentage)

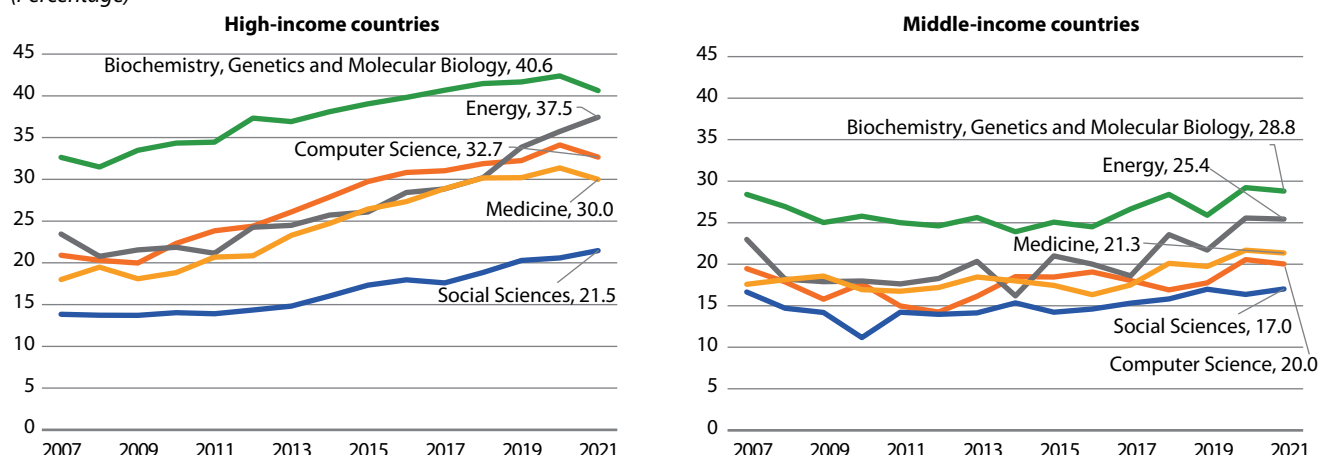


Source: UN DESA calculations based on OECD Creditor Reporting System data retrieved from OECD.Stat.

Note: STI ODA includes the following sectors: Technological research and development, Research/scientific institutions, Medical research, Agricultural research, Forestry research, Fishery research, Environmental research, Energy research, and Educational research. Shares computed using gross ODA disbursement at constant prices.

Figure III.G.8

Share of scientific publications involving international collaboration, by country income group and field, 2007–2021
(Percentage)



Source: UN DESA calculations based on data from OECD Data Explorer.

Note: Data contains 41 high-income countries, and 19 middle-income countries. For each field, the value shown is the median value of the respective country income group.

International efforts to support innovation activities and accelerate technology uptake need to be scaled up. A concerted effort is needed to ensure alignment of the international protection of intellectual property rights with the pursuit of sustainable development. The international intellectual property rights system should allow policy space for countries at different development stages to manage their intellectual property system to support their industrial and STI strategies.⁸² Greater efforts are also needed to support STI cooperation between developing countries through South-South and triangular cooperation, taking advantage of their similar development and technological conditions that could make their experiences more replicable. Countries also need to collaborate on establishing internationally accepted principles for developing technology standards and ensuring consistent interpretation and application of these principles, which is essential for supporting technology diffusion.⁸³ Strong international cooperation on competition policy is needed to narrow the divergence between jurisdictions in terms of antitrust enforcement, which would reduce regulatory arbitrage and allow governments to fully enforce competition laws that provide a level playing field for smaller domestic firms against their bigger international competitors. International support for capacity-building is crucial and must give special attention to marginalized communities and vulnerable groups. Incorporating gender-responsive approaches into capacity-building programmes ensures that women and girls have equal opportunities to participate and benefit from STI advancements.

United Nations efforts to harness STI for sustainable development

As the United Nations focal point for STI for sustainable development, the Commission on Science and Technology for Development (CSTD) discusses policy issues raised by rapid technological change and advances the understanding of science and technology policies. Recent discussions include data for development, global STI cooperation and green technology for sustainable development.⁸⁴ The CSTD also serves as the focal point in the system-wide follow-up to the outcomes of the World Summit on the

Information Society, promoting the sharing of information and knowledge about the major trends, impacts, opportunities and challenges of digital development.⁸⁵

The Technology Facilitation Mechanism (TFM), through the organization of the annual multi-stakeholder forum on STI for the SDGs (the STI Forum), has played a key role in facilitating discussions on STI cooperation in support of the SDGs.⁸⁶ The TFM has also launched the global pilot programme on STI for SDGs roadmaps to support developing countries to envision and plan actions, track progress and foster a learning environment to harness STI to achieve the SDGs. The CSTD and TFM are among the most prominent United Nations platforms to engage with key stakeholders, facilitate exchange and cooperation in STI, and build consensus on a common vision that reflects the needs and aspirations of all countries.

Apart from strategic planning, capacity-building is an important area of international cooperation in STI. Within the United Nations system, the UN Interagency Task Team on STI for the SDGs (IATT) under the TFM serves as a collaboration hub, with 47 United Nations entities and 150 staff members active in 10 workstreams.⁸⁷ This includes a workstream on capacity-building, which designs and delivers training courses and workshops on STI policy for the SDGs, including a global repository of training materials, guidelines and case studies for policy implementation, particularly for developing countries.⁸⁸ The capacity-building workstream has delivered a series of nine training workshops on STI policy and instruments for the SDGs for around 1,200 STI officials from 74 countries, with 51 per cent of the participants women. To build capacity in STI policymaking, the United Nations Conference on Trade and Development (UNCTAD) offers customized training for developing countries,⁸⁹ complementing the national STI policy reviews conducted in 19 countries to identify the key strengths and weaknesses of their innovation systems, establish strategic priorities and integrate STI policies into national development strategies.⁹⁰ In 2023, the United Nations Industrial Development Organization (UNIDO) launched a methodology to assess readiness for industrial innovation in developing

countries, which also serves as a capacity-building tool for policymakers.⁹¹

The United Nations Technology Bank for Least Developed Countries champions technology transfers by aligning the technology demands of LDCs with appropriate solutions through three pillars of work.⁹² The first pillar is the country-specific Technology Needs Assessment (TNA) to map key development challenges facing LDCs and identify the technologies, innovative solutions, skills and knowledge that LDCs need to address them. The second pillar is the design of context-specific technology transfer projects and programmes guided by the TNAs, with the current focus on agriculture and food systems; environment, climate change and resilience; health; and education and digital skills development. The third pillar is the development of STI capacities in LDCs, including to ensure sustainability of the support provided by the Technology Bank. Other major programmes that support technology and knowledge transfer, in particular environmentally sound technologies, include the Global Environment Facility and the Climate Technology Centre and Network. To date, the Technology Bank has completed 12 TNAs covering five countries in 2020, six in 2022 and one in 2023. It is expected that five more TNAs will be completed in 2024. To further enhance the Technology Bank's capacity and effectiveness, Member States have called on international partners to provide voluntary financial and in-kind resources in the Doha Programme of Action for LDCs for this decade from 2021 to 2030.

Given the cross-border implications of AI development and use, global coordination is needed. In October 2023, the United Nations Secretary-General convened a multi-stakeholder AI Advisory Body consisting of experts from government, the private sector and civil society to undertake analysis and advance recommendations for the international governance of AI. The Body will seek to link and coordinate with existing initiatives, including that of the European Union and the Group of Seven (G7) Hiroshima AI Process.⁹³ A core objective of the Body is to identify effective forms of AI governance, informed by an examination of existing models of technology governance that have worked in the past.

Recommendations from the Body—regarding international cooperation on AI governance, scientific consensus on risks and challenges, and key opportunities and enablers to leverage AI for achieving the SDGs—will feed into the Global Digital Compact proposed for adoption by Heads of State at the Summit of the Future in September 2024. In December 2023, the Advisory Board released an interim report on governing AI for humanity.⁹⁴ In its preliminary recommendations, the interim report proposed five guiding principles for AI governance: (1) AI should be governed inclusively, by and for the benefit of all; (2) AI must be governed in the public interest; (3) AI governance should be built in step with data governance and the promotion of the data commons; (4) AI governance must be universal, networked and rooted in adaptive multi-stakeholder collaboration; and (5) AI governance should be anchored in the United Nations Charter, international human rights law and other agreed international commitments such as the SDGs.

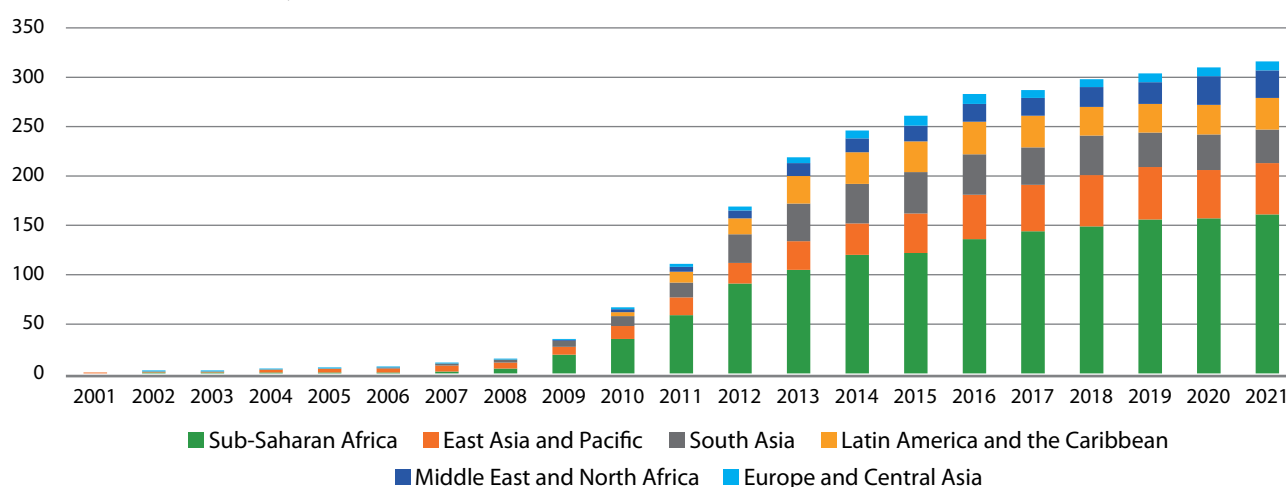
3. Technology and financing for development: Fintech and the implications of STI for action areas of the Addis Agenda

3.1 Fintech

Evolution of fintech over the past 20 years

The global financial landscape is undergoing a transformation, driven in large part over the last two decades by the rapid growth of “fintech”—technology that provides financial solutions based on a combination of modern financial services and emerging technologies. The proliferation of the Internet and the advent of online

Figure III.G.9
Availability of mobile money services, 2001–2021
(Number of live mobile money services)

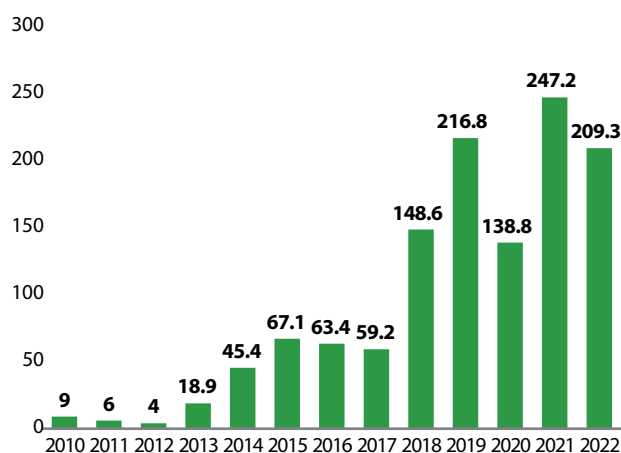


Source: GSMA (2023).

banking in the early 2000s laid the foundation for the iterations of fintech that followed. Digitalization efforts within traditional financial institutions paved the way for more profound technological integration in the financial sector. Mobile money services provided by telecoms and fintech firms and accessed through local agents and text-based phones emerged as a more affordable and convenient way to access digital financial services (figure III.G.9).⁹⁵ For example, over 35 per cent of adults in sub-Saharan Africa use a mobile money account.⁹⁶ The popularization of Internet-enabled smartphones since the mid-2000s provided another impetus for change. Mobile banking applications emerged, leveraging smartphone technology to facilitate on-the-go access to bank and fintech accounts and improved financial management. This period also saw the rise of digital payment platforms that simplify online transactions, followed by a diversification of fintech services, with innovations including automated trading systems, peer-to-peer lending and the early stages of blockchain and cryptocurrency technologies.

The 2008 world financial and economic crisis had a catalytic effect on the expansion of the fintech sector.⁹⁷ Post-crisis regulatory reforms that focus on traditional financing institutions, a period of heightened public distrust of these institutions, pressure to reduce operational costs and a contraction of the interbank markets have allowed the emergence of new entrants to the financial sector,⁹⁸ marking the beginning of the fintech era. This era is defined by the explosion in the number of financial service providers and the application of rapidly developing technology at the retail and wholesale levels, which is reflected by the significant increase in global investment in fintech companies (figure III.G.10), with the primary momentum fed by growth in the United States.⁹⁹ In 2023, an estimated 26,000 fintech companies operated globally, up from around 12,000 in 2019. This growth is expected to continue: Fintech sector revenues are projected to grow sixfold from \$245 billion in 2021 to \$1.5 trillion in 2030, moving from 2 per cent to 7 per cent of the \$12.5 trillion in global financial services revenue.¹⁰⁰

Figure III.G.10
Global fintech investment, 2010–2022
(Billions of United States dollars)



Source: Statista.

Note: The values shown are investment into fintech companies worldwide.

Periods of significant innovation and technological advancement often give rise to economic bubbles; this has also played out in the fintech market.¹⁰¹ The meteoric rise and rapid fall of cryptocurrencies—as shown in figure III.G.11—serves as a poignant illustration of this dynamic.¹⁰² Advocates for cryptocurrencies evoked a new paradigm of monetary exchange that needs no trusted intermediaries. In the end, the crypto financial system failed to deliver full decentralization,¹⁰³ and the rapid and speculative investment in these digital currencies has led to extremely high volatility, with spillover effects to the broader financial market.¹⁰⁴

Fintech and financial inclusion

Advances in fintech have facilitated financial inclusion. Fintech providers have enhanced access to and the use of digital financial services for individuals and micro-, small and medium-sized enterprises (MSMEs). They have improved the affordability and personalization of financial products services that make them more relevant for diverse customer needs. Prominent examples include mobile payment services such as M-PESA in Kenya and online payments and messaging apps in developing countries such as China and India.¹⁰⁵ During the COVID-19 pandemic, fintech companies played a notable role in enabling quick-yet-contactless deployment of government support measures via digital financing to MSMEs and individuals, especially those living in marginalized and poor communities. This included transfers of government emergency funds and digitizing social protection payments and pensions. Fintech can also support MSMEs with sending and receiving funds through peer-to-peer platforms and raising funds through crowdfunding platforms. The extensive data that fintech firms collect offers high-frequency visibility into firm performance and opportunities for embedded financial products that collateralize future sales to clients. This can help to reduce collateral requirements and monitoring costs and can thus provide firms and households with loans they might not otherwise be able to access.

Complementary investments are needed to fully realize the potential of fintech and mitigate risks. The inclusive potential of fintech can only be fully realized with improvements in the public's access to technology, digital literacy skills, complementary digital infrastructure that enables the development and use of fintech, and commensurate regulatory frameworks that allow for innovation while managing risks where they emerge—be that from traditional or new providers. For example, the success of M-PESA in Kenya was predicated on a combination of factors, including high phone ownership, a large physical network of agents that allows easy exchange between cash and mobile money, a nimble regulatory approach, an effective marketing campaign that focused on urban migrant workers, and bank branch closures of significant scale around the time the mobile payment service was launched.¹⁰⁶ These factors are not easy to replicate, which is reflected in the fact that mobile money services have not gained universal traction across developing countries.

Furthermore, the unbanked population using fintech solutions often faces risks similar to those they might face in the formal financial system, such as the lack of financial and digital literacy skills to navigate a technology platform. They are also more susceptible to predatory lending practices and higher interest rates. Fintech, moreover, has not fully delivered on its promise to close the gender gap in access to financial services, as use of the technology by women is

Figure III.G.11

Global cryptocurrency market capitalization, 28 April 2013–7 January 2023*(Trillions of United States dollars)***Source:** CoinMarketCap.

hindered by equipment costs, inadequate literacy skills, and discriminatory social norms and laws that disadvantage women in many countries.¹⁰⁷ Governments need to work with financial institutions—both new and established—to implement targeted policies alongside fintech development, to improve women’s access to financial services and the Internet and to address the differences in attitudes, discrimination and social norms and laws that marginalize women’s access in many countries.

The implications of fintech for financial sector development—market stability, competition, consumer privacy and financial integrity

The entry of new actors, including Big Tech, into the financial services sector presents opportunities for improving financial inclusion, economic efficiency and financial stability, but it also poses intricate policy challenges. Without appropriate regulation, fintech could destabilize financial markets, infringe on consumer privacy and undermine financial integrity. Although traditional regulatory principles are applicable to these new actors for financial activities, their unique data-driven business model—which enjoys economies of scale, network effects and the resultant “winner-takes-most” dynamics—means that their financial activities necessitate not only financial regulation but also competition policy and data privacy laws.¹⁰⁸

Fintech could contribute to financial stability by strengthening decentralization and diversification, deepening financial markets and improving efficiency and transparency in the delivery of financial services. Preliminary evidence suggests that the use of fintech platforms for capital raising in advanced economies has played a role in improving financial stability, possibly through some of these aforementioned channels.¹⁰⁹ Established financial institutions in countries with high regulatory quality and government effectiveness have benefited from

increased competition from fintech firms.¹¹⁰ Well-designed regulations can establish a level playing field—one in which new fintech firms can succeed and incumbent financial institutions are protected from unfair competitive behaviours.

However, fintech can also incentivize riskier activities and exacerbate the cyclicity of financial markets, especially in a suboptimal regulatory environment. Reduced profit margins resulting from increased competition from fintech could create difficulties for established banks in building the capital buffer necessary to absorb losses and maintain solvency.¹¹¹ If regulations are inadequate, reduced profit might incentivize them to engage in riskier lending and investment activities, with implications for market stability. Lending activities facilitated by fintech platforms may also involve greater financial risk due to concentration and overreliance on data-driven algorithms in risk evaluations and credit-related decisions, which could lead to herding behaviours.¹¹² Moreover, fintech can amplify market volatility as it significantly increases the speed and ease of moving money in response to financial market performance. AI can expedite and reinforce the cyclical nature of financial conditions through the automation of risk assessments and credit approvals that tend to fluctuate with economic cycles. To mitigate the risks posed by fintech firms to market stability, it is essential to consistently evaluate and update the licensing framework for financial service providers, taking into consideration emerging entities with innovative business models.¹¹³ Moreover, there is a need to strengthen requirements for capital, liquidity and operational risk management to adequately represent the diverse risks associated with various fintech business models.

One of the primary concerns regarding fintech is the extensive collection and analysis of personal data, which is central to the success of the business model but could infringe on consumer privacy. Fintech firms gather vast amounts of sensitive information, including

on spending habits, financial history and geographic locations, which poses a risk of privacy breaches. Cyberattacks targeting fintech companies have become more sophisticated, raising the risk of personal data being stolen or misused. There is also the issue of consent and transparency. Often, users are not fully aware of how their data is being used or to what extent it is shared with third parties, leading to a lack of control over their own personal information. Moreover, the use of AI in fintech further complicates privacy issues. These technologies can make decisions based on user data that might discriminate against certain groups or invade personal privacy without explicit consent. For example, algorithms might make credit decisions based on factors that are not transparent to users. Concerns regarding data privacy and misuse of personal data could deter consumers from sharing their personal data with fintech firms, which would undermine their business models and competition in the financial sector. Legislative efforts to strengthen consumers' control over their own personal data and increase transparency and accountability in data use have shown some success in mitigating the trade-off between consumer privacy protection and promotion of competition.¹¹⁴ Stronger data protection incentivizes consumers to share their personal data, which allows fintech firms to screen loan applications more effectively and offer lower rates.

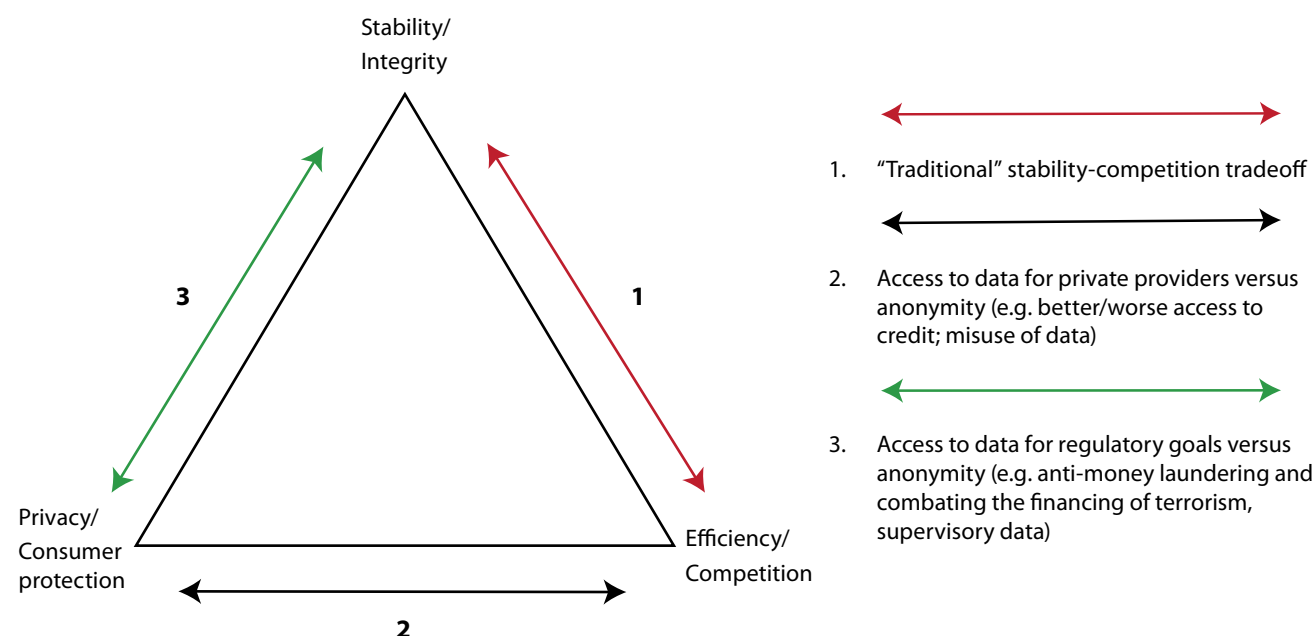
Fintech has heightened the potential for fraud in financial markets. Advanced algorithms and machine learning capabilities, while designed for efficiency and better financial decision-making, can also be used to engineer sophisticated fraudulent schemes. High-frequency trading algorithms, for instance, can be manipulated to create false market trends, misleading investors and disrupting market stability. The rapid pace of transactions in fintech also means that fraudulent activities can proliferate quickly and cause significant harm to consumers and investors before they are detected.

Furthermore, the digitalization and automation provided by fintech platforms have created conditions that could be conducive to illicit financial flows. The anonymity and speed offered by certain fintech services, especially those involving cryptocurrencies and blockchain technology, can be exploited for money laundering and the financing of illegal activities. These platforms can obscure the origins of illicit funds, making it challenging for regulatory bodies to trace and prevent these flows. The decentralized nature of some fintech applications further complicates regulatory oversight, allowing cross-border transactions to bypass traditional monitoring systems. To address fintech's impact on financial integrity, regulators need to prioritize transparency in fintech firms' operations, transactions and business models as well as anti-money laundering (AML) compliance, and adopt stringent measures to detect and prevent financial crimes. Fintech firms need to utilize technology-compatible AML solutions to comply with AML regulations and conduct robust due diligence and compliance checks through reliable sources, given conventional AML solutions utilized in the traditional financial sector are not sufficient in the current technology context.

Overall, policy measures should aim at the broader goals of consumer welfare rather than a narrow focus on market competition or financial stability. In the case of fintech, understanding how common policy tools affect welfare outcomes is complex. For instance, standard financial regulations might conflict with the goals of competition policy and data privacy laws, and vice versa.¹¹⁵ The complex public policy trade-offs among financial stability and market integrity, efficiency and competition, and data privacy and consumer protection—summarized in figure III.G.12—call for cooperation between financial sector regulators, industry regulators and authorities overseeing competition and consumer privacy protection.¹¹⁶

Figure III.G.12

Policy trade-offs between stability, efficiency, and privacy protection in the context of digital transformation in finance



Source: Feyen, and others (2021).

Box III.G.2**Implications of STI for action areas of the Addis Ababa Action Agenda**

In addition to the profound implications for the financial sector and financial sector stability (action areas B and F), technological advances have also contributed to progress and created new opportunities in other actions areas of the Addis Agenda, mainly by improving efficiency and transparency.

Public finance: Digitalization improves tax collection and public service delivery. The increased use of digital payments enables better verification of taxpayers' economic conditions and helps to formalize and tax undocumented economic activities. "Smart contracts" can automate transactions such as licensing, revenue collection and social transfers.¹¹⁷ An example is the blockchain-based digital identity card of Estonia, which allows its citizens to access public, financial and social services and pay taxes.

Digitalization also increases fiscal transparency and accountability. Online platforms for public financial data allow the public to track government spending and revenues. Distributed ledger technologies can be used to create immutable records of transactions, reducing the potential for corruption and mismanagement. Overall, the combination of higher-quality data, enhanced data management systems and increased computer processing power contributes to the better design of fiscal policies.

International development cooperation: Digitalization can improve international development cooperation through timely and better-targeted responses, reduced risk of fraud and a better understanding of impacts, thereby contributing to better programme and project design and implementation. For example, big data and AI

technologies can help to identify, predict and target poverty interventions when information from traditional sources, such as administrative data, is lacking. Also, by increasing transparency and accountability in development cooperation, technologies could help to increase general public willingness to provide support.

Trade: Technology impacts trade by enhancing efficiency and expanding market access. Advances in ICT streamline supply chain management and improve logistics. E-commerce platforms break geographical barriers, allowing SMEs to access global markets. Additionally, digital payment systems and fintech solutions facilitate smoother and faster cross-border transactions, which supports international trade. Digitally delivered services, an increasingly important component of trade, leverage ICT for cost efficiency, broader reach and enhanced tradability (see chapter III.D).

Debt: Advanced data analytics tools enable more accurate and timely analysis of economic and financial data, which helps to predict market trends, assess credit risks and evaluate the impact of various macro-economic scenarios on debt sustainability. Such tools could help to make informed decisions regarding debt issuance, restructuring and repayment.

Also, digitalization can help developing countries to overcome some bond issuance bottlenecks regarding market infrastructures, including central clearing systems, securities custodians, calculation agents and rating agencies.¹¹⁸ With the use of distributed ledger technologies, digital platforms for bond issuance can simplify the process and reduce the time and costs involved by reducing the number of actors involved in the bond issuance process, automating issuance and distribution, reducing the need for human oversight and improving efficiency in settlement.^{119 120}

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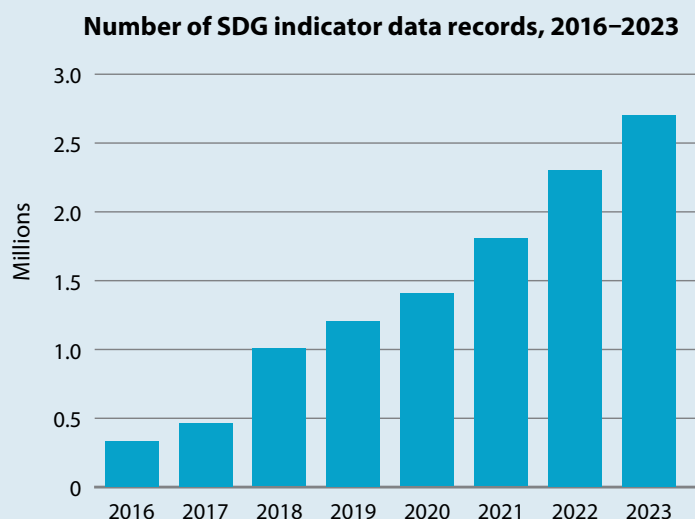
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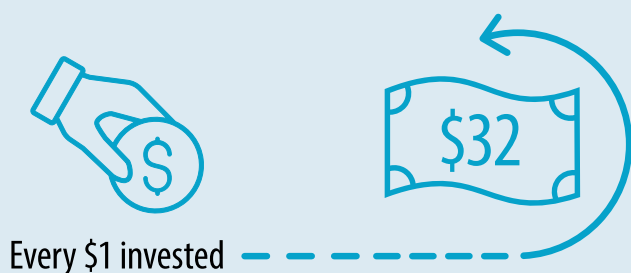


Data, monitoring and follow-up *in numbers*

The SDG indicator framework contains rich information on sustainable development progress beyond the information provided by GDP figures; it is populated with 2.7 million data records.



Investment in data pays off: there is an average return of \$32 for every \$1 invested in strengthening data systems in developing countries.

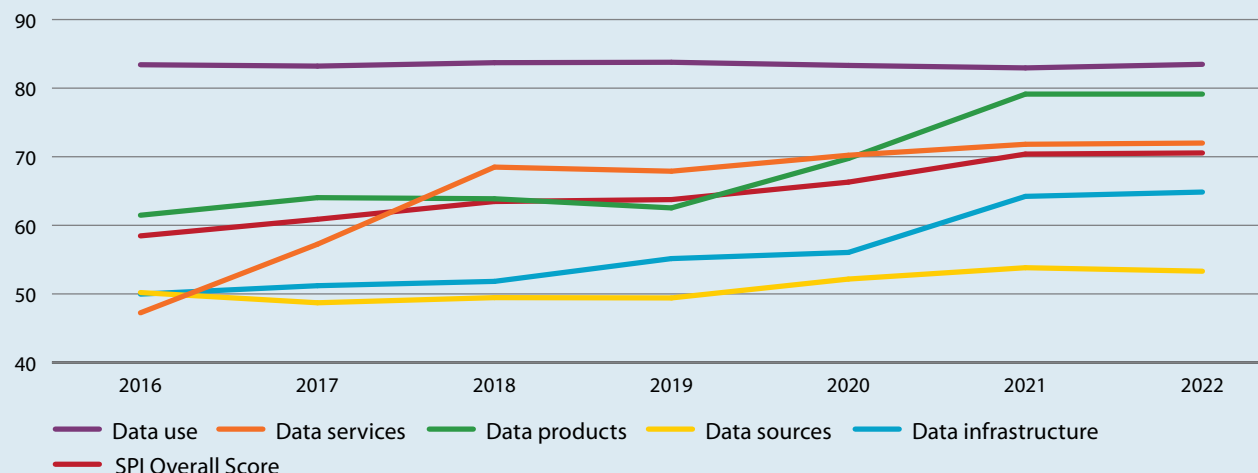


Overall gender data is lagging behind, but it has improved. 51 per cent of country data on gender-specific SDG indicators is now available.



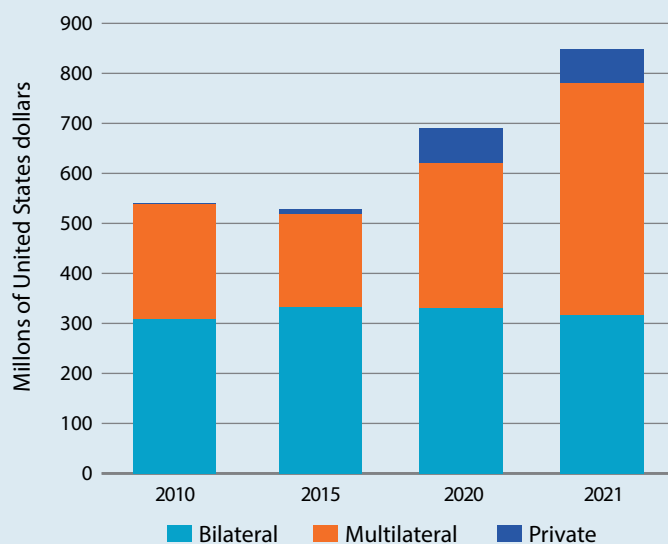
Countries have made significant strides in improving their national statistical systems: global average statistical performance score has crossed 70 out of 100.

Global average scores for statistical performance, 2016–2022



There have been increased investments in data, and total external funding disbursed for data and statistics in 2021 reached nearly \$850 million.

External funding for data and statistics, by donor type





Chapter IV



Data, monitoring and follow-up

1. Key messages and recommendations

Investments in data pay a dividend. Underinvestment in public data systems and statistical activities continues to undermine the pursuit of sustainable development. Despite the potential for substantial economic returns, Member States have not been able to capitalize on the power of data due to a lack of political prioritization, fragmentation, inadequate and siloed investment, and shortfalls in capacity. Fully using data and unlocking the data dividend for the Sustainable Development Goals (SDGs) will require both political leadership and financial commitments.

The excessive focus on income per capita and gross domestic product (GDP) levels obscures progress on all three dimensions of sustainable development.

Efforts to move beyond GDP have gathered steam. The development of the SDG indicator framework, and many well-being and environmental indicator frameworks at national and international levels, show that there is a growing richness of data covering human progress and environmental sustainability. Member States can take the opportunity of summits in 2024 and 2025 to agree to advance a consolidated set of a limited number of indicators that go beyond GDP and can be used as measures of progress. Member States can also decide how they would like to incorporate vulnerability and other factors into allocation criteria for concessional finance.

Financial data is essential in risk mitigation and policymaking but lacks a single overarching framework that unites different parts of the international system. The SDG indicator framework has concentrated efforts and brought greater coordination to the work of international statistical communities, with international and regional organizations and national statistical offices working together to elaborate a complex but useful set of indicators. While the SDG indicators still have some data gaps and challenges, there is much more heterogeneity and inconsistency with regard to the data on financing and

financial systems. The financing for development outcomes never mandated work on an indicator framework, and different international institutions continue on different tracks in data development. The Fourth International Conference on Financing for Development is an opportunity for Member States to mandate the development of a financing indicator framework if they think that will assist efforts to finance sustainable development.

Innovative sources of data can complement traditional data sources but access to data remains a challenge. Technological progress and the use of electronic devices have led to the creation of an ever-increasing amount of digital data, including from social media, mobile phone records, point-of-sale terminals, global positioning system devices and satellite imagery. There is an increasing use of administrative data sources and a growing trend in the collection and use of citizen-generated data for developing policy-relevant information. These and other innovative data sources, if harnessed and utilized effectively, represent an opportunity to generate information in real time, complementing official statistics that bring depth of detail and representation through validated surveys and censuses. While these innovative sources can provide rich evidence for economic and financial policymaking, they also have potential applications in humanitarian work, peacekeeping and human rights. At the Fourth International Conference on Financing for Development, Member States may want to consider strengthening data governance mechanisms which enable Member States to systematically engage with partners, such as the private sector, academia and civil society, to access relevant frontier sources of data while maintaining relevant privacy protections.

Funding for data and statistical systems needs to focus on producing actionable insights that can help to advance progress on the SDGs. A coordinated global financing architecture is emerging to help unlock

the potential of data for development and risk analysis at scale. Member States can agree on priorities and pooling resources through coordinated financing structures at the Fourth International Conference on Financing for Development.

This chapter provides a brief overview of the development of data frameworks related to sustainable development over the past two decades, including a focus on financial data and gender data. It then discusses national statistical systems, their performance and their funding.

2. Data frameworks for sustainable development

Data, including data on financing, is critical for assessing progress and correcting course to achieve agreed goals, but shortcomings in data remain, including regarding coverage and quality. The Addis Ababa Action Agenda underlines the importance of data as well as investment in data and statistical systems. Digital technologies have ensured that the world is awash with data, but this data can only be useful if it is structured as information with a clear context and applicability for decision-makers and other users. Some types of data can be structured into official statistics which are consistent and comparable over time and also across countries. Despite the significant progress made in improving data, information and statistical systems, information gaps remain in many areas. Throughout this report, the Inter-agency Task Force has presented many areas where data is lacking, and boxes IV.2 to IV.6 in this chapter crystalize a few of the most pertinent areas in the financing for development agenda where there are data and informational challenges.

2.1 Beyond GDP

While the measurement of GDP is useful for economic analysis, it is not a comprehensive measurement of progress that fully aligns with the 2030 Agenda for Sustainable Development. GDP is the most widely used benchmark to measure a country's economic progress and the value of its domestic production of goods and services. However, GDP has also been used in unintended ways. Importantly, it is not a good measure of sustainable development or welfare. An overreliance on GDP can result in the pursuit of development with little concern for equality, resilience and sustainability in all its dimensions. Discussion of the need for broader measures of progress beyond GDP goes back to the 1987 Report of the World Commission on Environment and Development, known as the Brundtland report.¹ The topic received fresh attention in a 2009 report on the measurement of economic performance prepared by a commission led by Joseph Stiglitz, Amartya Sen and Jean-Paul Fitoussi.² It was further bolstered by the publication of a multidimensional poverty index in 2010.³ Some countries have already moved ahead to explore frameworks that look beyond GDP (see box IV.1). Subsequently, in the outcome of the Rio+20 United Nations Conference on Sustainable Development in 2012 and in the Addis Agenda, countries recognized the need for broader measures of progress to complement GDP in order to better inform policy decisions. The SDGs and their targets and indicators, universally adopted by Member States, are one response to this need.

Despite its narrow focus, GDP continues to serve as a benchmark in important national and international policy decisions, in

particular for development finance. GDP per capita impacts eligibility for official development assistance, decisions on debt relief and concessional financing, and the status of least developed country (LDC). As a result, key dimensions of sustainable development are not sufficiently considered in the functioning of the international financial architecture, with serious consequences for the sustainable development of all countries, in particular middle-income countries and small island developing States (SIDS). As the disconnect has grown between economic growth and perceptions of a peaceful society, well-being and living conditions, people have lost trust in governments and institutions. The need for a framework to measure progress beyond GDP has become a political and policy imperative.

There is now political momentum to develop metrics beyond GDP.

In the 2021 Our Common Agenda report and as part of his vision for the future of global cooperation, the United Nations Secretary-General emphasized the need “to correct a glaring blind spot in how we measure economic prosperity and progress”.⁴ In May 2023, the Secretary-General published a call to action in the form of a policy brief on the topic and suggested that Member States move to measure what they truly value.⁵ It proposed the elaboration of a robust technical and scientific process informed by sound and disaggregated data, which resulted in a United Nations value dashboard of a limited number of key indicators that go beyond GDP, and a major capacity-building and resourcing initiative to enable Member States to use the new framework effectively. In September 2023, Member States responded with the SDG Summit political declaration confirming the political commitment “to explore measures of progress on sustainable development that complement or go beyond GDP to have a more inclusive approach to international cooperation”, including the consideration of information on access to development finance and technical cooperation. Measures of progress that go beyond GDP is one of the global governance topics being discussed in the context of the Summit of the Future, to be held in September 2024.

Measurement and consideration of vulnerability is important for countries that face complex development pathways. Countries facing a high risk of external shocks and stressors often lack economic and social resilience. Yet, there exists no universally accepted standard for quantifying structural vulnerability at the national level and across the multiple dimensions of sustainable development. Addressing this gap, a high-level panel of experts developed the Multidimensional Vulnerability Index (MVI) and submitted its final report to the President of the General Assembly in September 2023.⁶ According to the MVI, SIDS, LDCs and land-locked developing countries (LLDCs) emerge as the most vulnerable groups, on average, highlighting their structural vulnerability and lack of resilience. Furthermore, MVI scores were not correlated with income, implying that the MVI can be a useful complement to GDP.

The MVI should be a living tool, with robust governance arrangements and a common approach to its use across the international system. The MVI uses high-quality indicators, predominantly sourced from United Nations data. Nevertheless, the MVI was conceived as a living instrument, subject to regular updates to incorporate advancements in data quality and availability, vulnerability measurement methodologies and understanding of the causes and consequences of vulnerability. In particular, external debt service data could be incorporated if missing data and data quality issues can be resolved (see box IV.6 and chapter III.E). An intergovernmental process is now deliberating on the high-level panel's

Box IV.1**The use of measures that go beyond GDP in Bhutan**

Bhutan is globally recognized as a leader in moving beyond GDP through its gross national happiness (GNH) approach, which was introduced in 1979 and takes a holistic view of social development.^a The measures underpinning GNH were developed over a three-year period in a participatory and inclusive way, involving a wide range of groups from government to local communities.

The current GNH index is made up of nine domains which are intended to reflect normative values embedded in the culture and traditions of Bhutan (figure IV.1). Under these nine domains, there are 33 indicators which aim to provide a complete picture of well-being, taking into account economic, environmental and social factors. The latest GNH report was published in 2023.^b

The GNH index forms the quantitative bedrock of national policy development, implementation and monitoring. It is linked to the Government's 12th Five Year Plan^c through the incorporation of GNH indicators into its results-based approach framework. Each new policy proposal is assessed using a GNH Policy Screening Tool, which provides a framework for the systematic assessment of the potential consequences of the policy against the GNH index. Efforts are also under way to use the GNH index as a criterion for resource allocation.

Bhutan's development initiatives emphasize advancing renewable energy options and safeguarding biodiversity because of the application of the GNH index. The preservation of culture and the environment also serves as a significant motivation for Bhutan's strategy of "high value, low volume" tourism. Since 2015, the SDGs have also been integrated in the index and the accompanying policy development and monitoring process.

Figure IV.1

The nine domains of the Bhutan GNH index



Source: GNH 2022.

^a Economic and Social Commission for Asia and the Pacific, Committee on Statistics. 2022. "From gross domestic product to well-being and sustainability: Note by the secretariat". ESCAP/CST/2022/5.

^b Karma Ura and others. 2023. *Gross National Happiness (GNH) 2022*. Thimphu: Centre for Bhutan and GNH Studies.

^c Gross National Happiness Commission. 2019. *Twelfth Five Year Plan 2018–2023*. Thimphu: Royal Government of Bhutan. At the time of publication, the Thirteenth Five Year Plan is pending Government endorsement.

report and the MVI, including its applicability, scope, custodianship, governance and ways to further improve it. The panel itself called for donors and international financial institutions to incorporate MVI into existing policies and practices, pursuing a common approach to the extent possible, for example on concessional finance allocation criteria (see chapter III.C).

2.2 Development indicator frameworks

The Millennium Development Goals (MDGs) marked the first time that the United Nations system built quantitative targets into a political agreement on global norms. Building on the United Nations global conferences of the 1990s, the Millennium Declaration of 2000 featured eight MDGs, including 18 time-bound targets. Those targets formed the basis for the development of 48 quantitative indicators by an inter-governmental process agreed at the General Assembly in 2001. The MDGs established measurable objectives for priorities for developing

countries. For 15 years, measurement against the MDG indicators gave the world information on development progress.

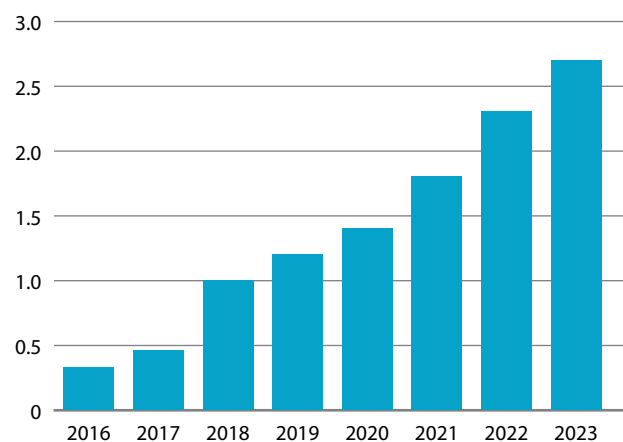
The 2030 Agenda marked a step change in ambition, including on efforts to quantify the progress towards sustainable development. The SDGs set forth in the 2030 Agenda are a set of universal goals that respond to the urgent environmental, political and economic challenges facing the world. In August 2015, Member States adopted the 2030 Agenda, including the 169 specific targets set out under the SDGs. While each country has the freedom to establish a national framework in achieving the SDGs, the Inter-Agency and Expert Group on Sustainable Development Goal Indicators (IAEG-SDGs) developed a universal global indicator framework—a voluntary and country-led instrument that included an initial set of indicators to be refined annually. Approved by the Statistical Commission in March 2017, and adopted by the General Assembly in July 2017, the indicator framework is subject to comprehensive

reviews every five years, the first of which was concluded in 2020 with 36 major changes to the framework.⁷

The adoption of the global SDG indicator framework has spearheaded major efforts by the statistical community to develop internationally established methodologies or standards for all indicators and to produce data. The SDG indicator database contained over 2.7 million records by the time of the SDG Summit in September 2023 (figure IV.2).⁸ The percentage of Tier 1 indicators that have an established methodology and for which data is regularly produced increased from 36 per cent to over 70 per cent between 2016 and 2023 (figure IV.3).⁹ Since 2020, all indicators have an internationally established methodology, meaning there are no longer any Tier 3 indicators. For example, important improvements to the indicator tracking financial resources mobilized for developing countries from multiple sources, including an initial conceptual framework on South-South cooperation measurement, were adopted in 2022 (see chapter III.C). Figure IV.4 shows the overall progress made but also the gaps in availability of the country level data. Major gaps and a lack of progress are notable in key priority areas of gender (Goal 5, see below), climate change (Goal 13) and governance (Goal 16). The timeliness of data is often a challenge as well. Not all indicators have or require new data every year, but for 35 per cent of indicators there is no data for the three years preceding the current year, making data less useful to policymakers.

The SDG indicator framework is complemented by additional data frameworks to delve deeper into specific topics. Member States have recognized the power of data to drive progress and since 2015, have adopted additional indicator frameworks. Strong accountability is one of the cornerstones of the Sendai Framework for Disaster Risk Reduction, and a set of 38 indicators, recommended by an Open-ended Intergovernmental Expert Working Group, is used to track progress in implementing the seven targets of the Sendai Framework. The Kunming-Montreal Global Biodiversity Framework is accompanied by a detailed monitoring framework, adopted in December 2022, consisting of a set of agreed indicators for tracking progress towards the goals and targets of the Framework.¹⁰

Figure IV.2
Number of SDG indicator data records, 2016–2023
(Millions)



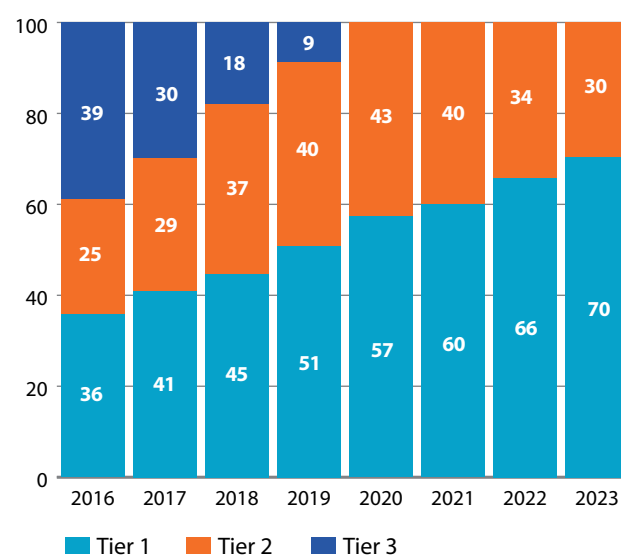
Source: UN DESA.

2.3 Financial data frameworks

Global standards in regard to financial data were first created in the 1990s and have been updated to address developments and gaps in coverage. The financial crisis in Mexico in 1994 underscored the role that information deficiencies could play in contributing to market turmoil and prompted an effort by the IMF to codify existing good practices in dissemination of economic and financial data.¹¹ In December 1997, the IMF Executive Board approved the general data dissemination standards (GDDS) as a general framework to guide countries in developing sound systems to support eventual dissemination of data to the public. In the wake of the Asian Financial Crisis, the special data dissemination standard (SDDS) launched coverage of foreign currency liquidity and external debt.¹²

The 2008 world financial and economic crisis highlighted gaps in key financial sector data, leading to the launch of a Data Gaps Initiative (DGI) in 2009. While some signs of economic and financial instability could be seen in the official data in the run-up to 2008, there were significant gaps in the data relevant for financial stability analysis. At the time, the economic and financial data did not fully capture risks in domestic financial sectors, the cross-border financial linkages, and the vulnerabilities and exposure of certain sectors of the economy to shocks. The Group of Twenty (G20) finance ministers and central bank governors endorsed 20 recommendations to address data gaps related to tail risks within the financial sector, leverage and maturity mismatches, linkages

Figure IV.3
SDG indicators by tier, 2016–2023
(Percentage)



Source: UN DESA.

Note: Tier 1: Indicator is conceptually clear, has an internationally established methodology and standards are available, and data are regularly produced by countries for at least 50 per cent of countries and of the population in every region where the indicator is relevant. Tier 2: Indicator is conceptually clear, has an internationally established methodology and standards are available, but data are not regularly produced by countries. Tier 3: No internationally established methodology or standards are yet available for the indicator, but methodology/standards are being (or will be) developed or tested.

Box IV.2

Revenue statistics

The availability—and quality—of cross-country data on government revenues (tax, non-tax, social contributions and grants) has improved vastly over the past decade. Historically, the go-to source for such information was the IMF's Government Finance Statistics (GFS), but many low- and middle-income countries did not provide the IMF with comprehensive data.

Today, the situation is much improved; not only is coverage of the IMF better, but efforts by other organizations complement its work. The IMF's World Revenue Longitudinal Dataset (WoRLD), launched in 2015, brings together data from the GFS with estimates from other databases. The Revenue Statistics of the OECD now incorporates vastly improved data for Africa and the Asia-Pacific regions. The UNU-WIDER Government Revenue Dataset (GRD)^a synthesizes data from across the IMF and OECD datasets as well as harnessing the rich revenue data contained in IMF Article IV assessments. These global databases have enabled analyses and research regarding the role of tax in development. There are also regional efforts, with data hosted by the United Nations Economic Commission for Latin America and the Caribbean, the African Tax Administration Forum and the Asian Development Bank providing insights into revenue collection in Latin America, Africa and Asia, respectively. Finally, data that accounts for revenue accruing from the activity of extractive industries has greatly improved, with disaggregated data reported by the Extractive Industries Transparency Initiative as well as the OECD Revenue Statistics and the GRD. However, despite these improvements, challenges remain in closing data gaps and improving the comparability of data.

There are still many low- and middle-income countries where comprehensive data on revenue collection on an annual basis is lacking. While for most countries available data will provide (at least) an annual estimate of total government or tax revenue, a fuller picture of revenue collection—for example disaggregated across different types of income—is sometimes missing. Furthermore, many countries only report revenue data collected by the central government, missing data on potentially significant amounts of revenue that are collected by local governments. Local government revenue data is available in the World Observatory on Subnational Government Finance and Investment^b but its comparability with data on central government revenues is unexplored and coverage for many low-income countries is lacking.

On the comparability of available data, most often data reported to the GFS or OECD Revenue Statistics is broadly comparable, save for a few different classification choices. However, this is not always the case, and where data differs in magnitude across sources, users are left with a challenge to understand exactly which figure is “correct” for a given country. A difference of half a percentage point of GDP is significant in low-income countries, where tax-to-GDP ratios remain perilously low. A better understanding—and documentation—of why these differences emerge would be invaluable.

^a The GRD was initially established by the International Centre for Tax and Development.

^b Data from the OECD/UCLG World Observatory on Subnational Government Finance and Investment (SNG-WOFI) initiative is available at: <https://www.sng-wofi.org>.

between individual financial institutions and cross-border capital flows, and distribution of income, consumption and wealth. The first phase of the DGI successfully concluded in September 2015; however, gaps remained in some areas.

The G20 launched a second phase of the DGI in 2015, amid remaining data gaps coupled with growing concerns that the digital revolution was introducing new risks to the financial system and sustainable equitable growth. The key objective of DGI-2 was to implement the regular collection and dissemination of comparable, timely and high-quality statistics for policy use. Similar to DGI-1, DGI-2 encompassed 20 new or revised recommendations focusing on statistics that supported: (i) monitoring of risk in the financial sector; and (ii) analysis of vulnerabilities, interconnections and spillovers, both domestic and cross-border, and other emerging policy needs.

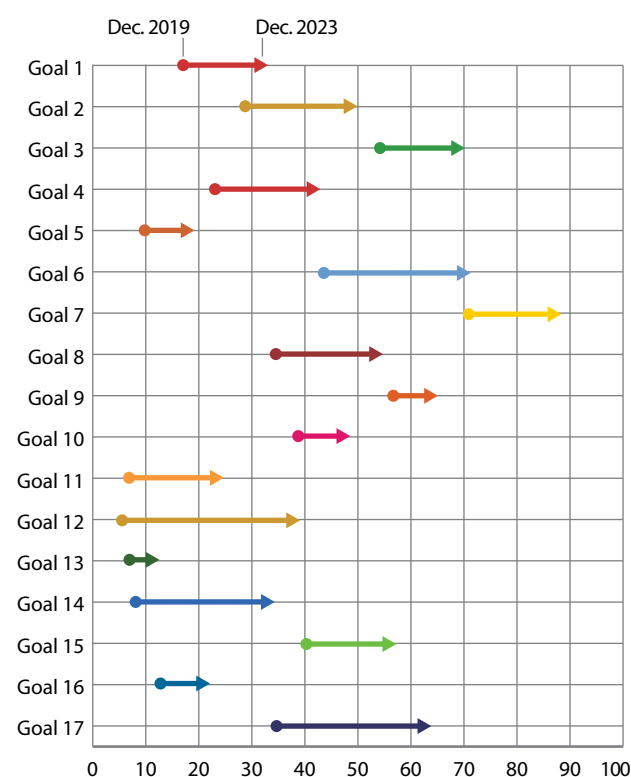
DGI-2 concluded in December 2021. Despite the progress made, however, some participating economies did not fully close the data gaps related to some DGI-2 recommendations. Challenges remained with regard to securities financing transaction statistics, securities statistics, sectoral accounts, international investment positions, international banking statistics, cross-border exposures of non-bank financial corporations, public sector debt statistics and commercial property price indices. Participating economies and international organizations continue to work towards closing these remaining DGI-2 data gaps.

In 2022, amid the accelerating climate crisis, increasing economic polarization and large-scale digital transformation, policymakers faced a new wave of complex and multidimensional policy challenges that required new data on sustainable development challenges. A third phase of DGI was therefore launched to address the data gaps in these areas, with the G20 endorsing 14 recommendations that cover four main priority policy areas: (1) climate change mitigation and adaptation; (2) creating more equitable distributions of income and wealth; (3) addressing the risks and leveraging the opportunities of financial innovation to ensure financial stability and improve financial inclusion; and (4) improved data access and data sharing. The initiative, launched by the G20 finance ministers, aims to create timely official statistics that allow them to address current policy issues. The IMF, in close cooperation with the Financial Stability Board and the Inter-Agency Group on Economic and Financial Statistics and in consultation with countries, will coordinate the implementation of the 14 recommendations. Similar to DGI-1 and DGI-2, the goal of DGI-3 is for the participating economies to catalyse the development of these statistics and equip all other countries with the tools and methodologies they need to navigate these challenges. Compared with previous DGI phases, DGI-3 includes a range of new stakeholders, including environmental-economic statisticians as well as the private sector holders of data. For most of the DGI-3 recommendations, there are existing agreed methodologies but greater attention needs to be given to data development and production.

Figure IV.4

Member States that have data for SDG indicators, by goal, 2019–2023

(Percentage of countries)



Source: UN DESA.

Note: Data for at least two years since 2015, weighted average across indicators. Circle shows December 2019, arrowhead shows December 2023.

2.4 Gender data

Data and statistics are indispensable tools for devising evidence-based policies and programmes on gender equality and women's empowerment, assessing their impact and promoting accountability. A dearth of sex-disaggregated data and insufficient multidimensional gender statistics pose major constraints for policymakers and gender equality advocates. Among countries with recent official statistics on monetary poverty, only 42 per cent have poverty data disaggregated by sex.¹³ Where data is disaggregated, large gender gaps are evident. Among countries producing multidimensional poverty indicators, only 20 per cent disaggregated these indicators by sex or sex of the head of household.¹⁴ While full disaggregation would not be possible given the nature of some SDG indicators, only 27 of all the SDG indicators have sex disaggregated data for more than 95 per cent of countries (figure IV.5).

Greater efforts need to be made specifically on producing data and tracking progress on SDG 5—achieving gender equality and empowering all women and girls. As of 2022, Member States crossed the symbolic 50 per cent mark in terms of gender data availability on 82 gender-specific SDG indicators and sub-indicators,¹⁵ with 51 per cent of SDG gender data now available (up from 26 per cent in 2016).¹⁶ A similar analysis on a subset of 50 gender-related indicators found that countries

reported on average on 31 per cent of these indicators in at least one year from 2016 to 2020.¹⁷ Still, only 3 of the 18 indicators and sub-indicators on SDG 5¹⁸ have sufficient data to assess progress over time across all regions and in 5 out of the 18 indicators and sub-indicators, global data remains insufficient to assess current levels.¹⁹ Gender data gaps arise for diverse reasons and cannot be tackled by isolated, disjointed efforts. However, external funding for gender statistics has been stagnant since 2015.²⁰

2.5 Innovative sources of data

The integration of innovative data sources has transformed official statistics over the past decade. The use of innovative data, such as big data (usually sourced from the private sector²¹), geospatial data, citizen-generated data and data science, promises more timely, disaggregated and relevant information, filling gaps in existing official statistics when new information needs arise or existing statistics fall short of providing the required information. The use and integration of new data sources can be more cost-efficient than traditional data sources such as surveys. According to a comprehensive review and survey by the Committee of Experts on Big Data and Data Science for Official Statistics, approximately 80 per cent of national statistical offices have incorporated references to modernization, innovation, data science and alternative data sources into their strategic visions. The survey highlights the shift towards collecting data from diverse sources, including from the private sector, emphasizing collaboration between national statistical offices and public/private sector institutes to navigate challenges related to privacy, access and integration.²² The drive towards the use of innovative data sources has led to the creation of new institutions, including the establishment of regional and global hubs for big data and data science.

The vision for innovative data use is confronting real-world challenges related to data access and privacy. For example, the use of privately held data must have a proper legal basis as a prerequisite for statistical agencies to obtain such data. The privacy rights of individuals must be protected and issues of data quality and appropriate use addressed. The survey results indicate that statistical agencies are addressing these challenges in a strategic way. Access to private sector data, coupled with data privacy protection, emerged as a major focus in innovation strategies, leading to updates in statistical legislation by more than 80 per cent of offices. How official statistics are produced is changing, but not universally, as not all methods are applicable across countries (e.g. the use of scanner data for producing price statistics). A Collaborative on Citizen Data was established in April 2023 at the Fourth United Nations World Data Forum. This Collaborative developed the draft Copenhagen Framework on Citizen Data that defines the possible types of citizen data and offers a common understanding of how to leverage its responsible production and curation.²³ Geospatial information, for one, has been very widely adopted, driven by demands for the global monitoring of the SDGs. Geospatial data is the data source for multiple global SDG indicators on land cover and land use such as the average share of the built-up area of cities that is open space for public use for all (SDG indicator 11.7.1).

Innovative data sources can also generate information for policymakers and stakeholders outside the statistical system.

Not all data for use by policymakers will be held in the statistical system, with notable real-time data and information efforts conducted by central banks and financial regulators (see above). Administrative data sources

Figure IV.5

Availability of sex-disaggregated data, by SDG indicator, 2015–2023*(Percentage of countries)*

Goal 1	Goal 2	Goal 3	Goal 4	Goal 5	Goal 6	Goal 7	Goal 8	Goal 9
1.1.1	2.1.1	3.1.1	4.1.1	5.1.1	6.1.1	7.1.1	8.1.1	9.1.1
1.2.1	2.1.2	3.1.2	4.1.2	5.2.1	6.2.1	7.1.2	8.2.1	9.1.2
1.2.2	2.2.1	3.2.1	4.2.1	5.2.2	6.3.1	7.2.1	8.3.1	9.2.1
1.3.1	2.2.2	3.2.2	4.2.2	5.3.1	6.3.2	7.3.1	8.4.1	9.2.2
1.4.1	2.2.3	3.3.1	4.3.1	5.3.2	6.4.1	7.a.1	8.4.2	9.3.1
1.4.2	2.3.1	3.3.2	4.4.1	5.4.1	6.4.2	7.b.1	8.5.1	9.3.2
1.5.1	2.3.2	3.3.3	4.5.1	5.5.1	6.5.1		8.5.2	9.4.1
1.5.2	2.4.1	3.3.4	4.6.1	5.5.2	6.5.2		8.6.1	9.5.1
1.5.3	2.5.1	3.3.5	4.7.1	5.6.1	6.6.1		8.7.1	9.5.2
1.5.4	2.5.2	3.4.1	4.a.1	5.6.2	6.a.1		8.8.1	9.a.1
1.a.1	2.a.1	3.4.2	4.b.1	5.a.1	6.b.1		8.8.2	9.b.1
1.a.2	2.a.2	3.5.1	4.c.1	5.a.2			8.9.1	9.c.1
1.b.1	2.b.1	3.5.2		5.b.1			8.10.1	
	2.c.1	3.6.1		5.c.1			8.10.2	
		3.7.1					8.a.1	
		3.7.2					8.b.1	
		3.8.1						
		3.8.2						
		3.9.1						
		3.9.2						
		3.9.3						
		3.a.1						
		3.b.1						
		3.b.2						
		3.b.3						
		3.c.1						
		3.d.1						
		3.d.2						

	>95% coverage
	>50% coverage
	>5% coverage
	No disaggregation

Source: UN DESA.**Note:** Data for at least one year since 2015, coverage by the percentage of countries. Some indicators are not possible or relevant for disaggregation by sex.

Figure IV.5 (continued)

Availability of sex-disaggregated data, by SDG indicator, 2015–2023

(Percentage of countries)

Goal 10	Goal 11	Goal 12	Goal 13	Goal 14	Goal 15	Goal 16	Goal 17
10.1.1	11.1.1	12.1.1	13.1.1	14.1.1	15.1.1	16.1.1	17.1.1
10.2.1	11.2.1	12.2.1	13.1.2	14.2.1	15.1.2	16.1.2	17.1.2
10.3.1	11.3.1	12.2.2	13.1.3	14.3.1	15.2.1	16.1.3	17.2.1
10.4.1	11.3.2	12.3.1	13.2.1	14.4.1	15.3.1	16.1.4	17.3.1
10.4.2	11.4.1	12.4.1	13.2.2	14.5.1	15.4.1	16.2.1	17.3.2
10.5.1	11.5.1	12.4.2	13.3.1	14.6.1	15.4.2	16.2.2	17.4.1
10.6.1	11.5.2	12.5.1	13.a.1	14.7.1	15.5.1	16.2.3	17.5.1
10.7.1	11.5.3	12.6.1	13.b.1	14.a.1	15.6.1	16.3.1	17.6.1
10.7.2	11.6.1	12.7.1		14.b.1	15.7.1	16.3.2	17.7.1
10.7.3	11.6.2	12.8.1		14.c.1	15.8.1	16.3.3	17.8.1
10.7.4	11.7.1	12.a.1			15.9.1	16.4.1	17.9.1
10.a.1	11.7.2	12.b.1			15.a.1	16.4.2	17.10.1
10.b.1	11.a.1	12.c.1			15.b.1	16.5.1	17.11.1
10.c.1	11.b.1				15.c.1	16.5.2	17.12.1
	11.b.2					16.6.1	17.13.1
						16.6.2	17.14.1
						16.7.1	17.15.1
						16.7.2	17.16.1
						16.8.1	17.17.1
						16.9.1	17.18.1
						16.10.1	17.18.2
						16.10.2	17.18.3
						16.a.1	17.19.1
						16.b.1	17.19.2

	>95% coverage
	>50% coverage
	>5% coverage
	No disaggregation

Source: UN DESA.**Note:** Data for at least one year since 2015, coverage by the percentage of countries. Some indicators are not possible or relevant for disaggregation by sex.

Box IV.3

Measuring government spending on essential services

Tracking and reporting domestic pro-poor social spending is central to achieving the SDGs. Research suggests that spending on health, education and social protection in low- and middle-income countries remains below the recommended minimum levels required to meet the SDGs.^a SDG indicator 1.a.2 aims to track the proportion of total government spending on essential services (education, health and social protection). However, progress on improving consolidated, comparable, publicly available and up-to-date sector-specific data is limited.

The main sources of data for education, health and social protection expenditure differ. The United Nations Educational, Scientific and Cultural Organization (UNESCO) compiles education expenditure data, with government spending as a percentage of GDP reported for 166 countries within the past five years, although only 90 countries have data for 2022. UNESCO also has spending data in United States dollars for 90 countries between 2019 and 2021; however, only 19 out of these 90 countries have data for 2022 or later. The World Health Organization compiles health expenditure data for 217 countries, with details on health expenditure as a percentage of GDP and government expenditure, as well as in United States dollars. Within the past five years, 186 countries have reported health expenditure data, but none have data for 2022 or later. For social protection, the World Bank ASPIRE database has social assistance expenditure as a percentage of GDP for 51 countries up to 2019, but no more recent data.^b The latest International Labour Organization (ILO) World Social Protection Report has collected social

protection expenditure data for 185 countries between 2020 and 2022.

Recent SDG reporting is based on a sample of approximately 100 countries who report to the IMF's government finance statistics (GFS) database.^c The manuals for compiling the government finance statistics take an institutional approach to expenditure categorization, while classification for different public purposes was described in a United Nations Statistical Commission-agreed standard in 2000 called the Classification of the Functions of Government (COFOG).^d The GFS includes COFOG breakdowns for only selected functions and a limited number of mostly advanced countries. Work remains to be done to integrate the data collected by UNESCO, WHO, the World Bank, ILO and regional bodies and ensure consistency with the data provided to the IMF. There are also considerable time lags in the data production process, as agencies collect data only after allowing a considerable period for finalization of budgets and closing of accounts at the national level.

- a UNICEF Office of Research—Innocenti. 2022. "COVID-19 and shrinking finance for social spending", Innocenti Policy Brief series, Brief 2022-01, Florence, Italy.
- b The World Bank is planning to update the household survey data on which this is based. See <https://thedocs.worldbank.org/en/doc/61eb4e9e13155f9589e728b395ea53fc-0380082021/original/RSR-ASPIRE2-0-and-smoother-2021-attachment1-ASPIRE-Work-Program-FY20-FY22-ALL.pdf>
- c United Nations. *The Sustainable Development Goals Extended Report 2023: Goal 1*.
- d United Nations Statistical Commission, "Classifications of Expenditure According to Purpose: Classification of the Functions of Government (COFOG), Classification of Individual Consumption According to Purpose (COICOP), Classification of the Purposes of Non-Profit Institutions Serving Households (COPNI), Classification of the Outlays of Producers According to Purpose (COPP)".

Box IV.4

Data on public development banks

Governments have long used public development banks (PDBs) as important financing tools to implement their national economic and social policies to foster economic growth and reduce poverty. While PDBs have been active in many sectors, they have been especially important to efforts to finance large infrastructure. PDBs have a large array of different mandates and governance structures in different contexts, including channelling blended finance and other forms of alternative finance alongside the private sector. Frequent mandates include supporting small- and medium-sized enterprises and exports, financing housing, and providing agricultural sector financial support.^a

There have been limited efforts to produce comparable global data on the spread, size and impact of national and subnational PDBs. The World Bank, in conjunction with the World Federation of Development Financial Institutions, conducted surveys in 2012 and 2017 which covered 90 and 64 development banks, respectively.^b Those surveys covered mandate, business model, governance, funding, size, profitability and regulation, among other topics. While those surveys provided a rich and deep dataset for analysis on many of the largest national development banks, coverage was limited. A global research programme was

launched by the Finance in Common Summit in 2020 to increase the data and knowledge on PDBs. The most recent dataset identified 533 PDBs—distributed across every region and operating at local, national, regional, international or multilateral levels (see chapter III.A).^c The broad dataset provides a comprehensive mapping of PDBs worldwide, including information on their ownership structure, size of assets and official mandate.

Given the importance of PDBs as instruments to deliver on public goals, especially in helping to address market failures related to climate change mitigation and climate change adaptation, more comprehensive and regular cross-country information on the operations of PDBs could help countries to better structure their institutions and ensure they are delivering on their goals.

- a Jiajun Xu and others, "Art in the doing: Public development banks serving public policies".
- b José de Luna-Martínez and Carlos Leonardo Vicente, "Global Survey of Development Banks"; World Bank Group and World Federation of Development Financing Institutions. 2018. *2017 Survey of National Development Banks*.
- c Jiajun Xu and others, "What are public development banks and development financing institutions?—Qualification criteria, stylized facts and development trends" in *China Economic Quarterly International*, vol. 1, No. 4 (2021).

are particularly useful for disaggregation, including by sex and location, but there are challenges, including the need for effective collaboration among different parts of government, managing data quality concerns and respecting confidentiality. Citizen-generated data also provides an alternative that can complement and enhance official data, supporting policies, programmes and projects to achieve the MDGs. It is a low-cost, real- or near-real-time data source and is also typically more disaggregated. The collection and use of citizen-generated data can reveal intersectional inequalities, make data and policy more inclusive and help to empower people, boosting ownership and the social contract.²⁴

3. National statistical systems and funding

3.1 Trends in performance of statistical systems

Cross-country comparison of statistical systems became possible in the early 2000s and has recently improved with the creation of statistical performance indicators. In 2004, the World Bank launched the Statistical Capacity Indicators (SCI), consisting of three dimensions (methodology, sources and periodicity). The SCI drew on publicly available international databases and national statistical organization websites to populate the indicators and contribute to SDG monitoring (figure IV.6).²⁵ In 2021 the World Bank inaugurated the Statistical Performance Indicators (SPI) to build on and replace the SCI.²⁶ The SPI better reflects the changing global data landscape to focus on development outcomes. Incorporating

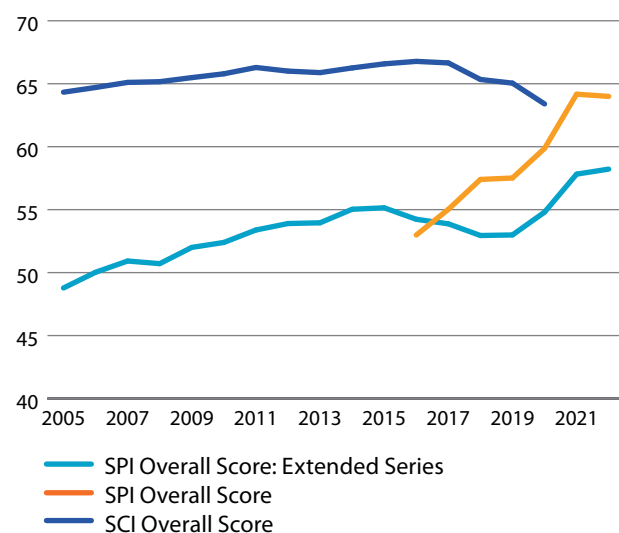
an assessment of the maturity of national statistical systems, the average overall SPI score across countries increased by 12 points between 2016 and 2022 and reached a score of 70 measured on a scale from 0 to 100, marking significant progress over a short period of time (figure IV.7). For countries where data is available under both indices, SPI performance far exceeds the improvements achieved in the period from 2005 to 2015, as measured by the SCI, when much less progress was made.²⁷

Progress in statistical systems has focused on expanding available data, but improvements to data sources remains a weak area.

The SPI has five pillars covering: data use; data services; data products; data sources; and data infrastructure; with 22 specific dimensions. Between 2016 and 2022, the greatest progress was made on data services (pillar 2) and data products (pillar 3) (figure IV.7), while moderate improvements were made on data infrastructure (pillar 5). However, there were only limited advances on improving data sources (pillar 4) and data use (pillar 1), although data use is already at a high level. Several countries made substantial headway and increased their overall SPI score by at least 25 points between 2016 and 2022, driven by improvements in the individual pillars (figure IV.8). While many countries improved their data services, many also saw a deterioration in those services.

Statistical system performance is driven by the capacity of the staff and funding provided. Higher-income countries have systematically better-performing statistical systems, although improvements in the SPI between 2016 and 2022 were very similar across different income groups (figure IV.9). It appears that improvements in the infrastructure for producing official statistics (pillar 5) is driving the overall progress of the SPI—perhaps related to more financing provided to data infrastructure development. As a result of the proliferation of data initiatives and monitoring frameworks, more attention is being paid to developing statistical systems. However, the challenge is to turn the increased attention and funding into more useful data that yields more actionable information to guide policymakers.

Figure IV.6
Statistical performance, 2006–2022
(Index)



Source: World Bank.

Note: Data for 145 countries with both statistical capacity indicator (SCI) and statistical performance indicator (SPI) scores. The SPI extended series was constructed to show changes in statistical performance using data in the SPI that are available historically.

3.2 Trends in funding for data and statistics

Funding is a critical factor for many countries that want to improve their data and statistics, including financial data. There is no systematic tracking of national financing for data and statistics, not least because the efforts are often spread across national statistical offices, line ministries, central banks and financial regulators. Over the last five years the percentage of countries having a fully funded national statistical plan has declined regardless of their income level. The lack of national funding for statistics is especially a challenge for low- and middle-income countries: In 2021, not a single low-income country had a fully funded national statistical plan. National statistical offices consistently report shortages in financial resources as one of their major constraints in producing the statistical outputs needed for SDG monitoring.

External financing can be relevant for many developing countries. In 2021, the most recent year for which data is available, total disbursed external funding—including official development assistance, non-concessional official lending and private sector assistance—for data and statistics rebounded and reached a new peak of \$799 million, a 14 per cent increase over 2020 (figure IV.10). In 2021, multilateral channels emerged as the predominant source of funding for the first time. In 2021,

Box IV.5**Environmental, social and governance data on private enterprise**

Measuring the private sector's contribution to the SDGs and the Paris Agreement on Climate Change is essential to paint an exhaustive picture of progress. To do so, private entities need to produce robust environmental, social and governance (ESG) data (synonymous with non-financial, or sustainability data). Fit-for-purpose ESG data is also necessary for investors to make informed decisions towards transition-aligned investments and to monitor their performance. Regulators and supervisors may also need this data.

In contrast to centuries-old financial accounting, standards for the production of information on non-financial issues have emerged relatively recently and so far are mostly voluntary. The Global Reporting Initiative (GRI) was established in 1997. Although data availability has increased over time due to requests by asset owners—with 98 per cent of S&P 500 companies now publicly disclosing sustainability data^a—coverage remains limited. Data gaps still exist for companies in developing countries, for non-listed entities, and for asset classes beyond listed equities and corporate bonds. Additionally, data quality is constrained

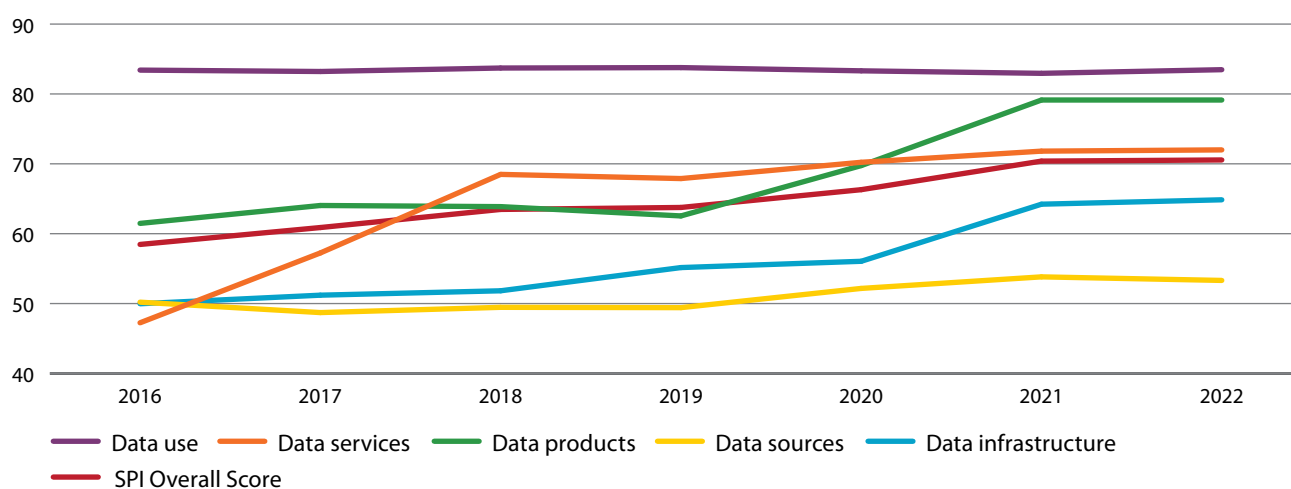
across the board, with ongoing issues related to reliability, consistency and comparability, exacerbating greenwashing concerns (see chapter III.B). Moreover, the disclosure of data alone is insufficient to steer capital towards sustainability; better and more transparent data must also impact economic decision-making.^b

Efforts are under way to standardize voluntary reporting standards, exemplified by the establishment of the IFRS Foundation's International Sustainability Standards Board (ISSB) (see chapter III.B). Legislation is being enacted at regional and national levels to bolster the sustainable finance information ecosystem, addressing definitions (e.g. taxonomies), data availability (e.g. disclosure legislation), reliability (e.g. investment and consumer product labels) and comparability (e.g. regulating ESG ratings). Without global harmonization, private businesses will face fragmentation and higher reporting burdens. Furthermore, some existing standards do not employ a double materiality perspective, looking only at the impact of the environment on a business and not providing insights into the enterprise's impact on the wider environment, including the SDGs and the Paris Agreement.

^a Governance & Accountability Institute, "Sustainability reporting in focus".

^b Mariasunna Giannetti and others, "'Glossy green' banks: The disconnect between environmental disclosures and lending activities". European Central Bank, Working Paper Series No 2882.

Figure IV.7

Global average scores for statistical performance, 2016–2022
(Index)

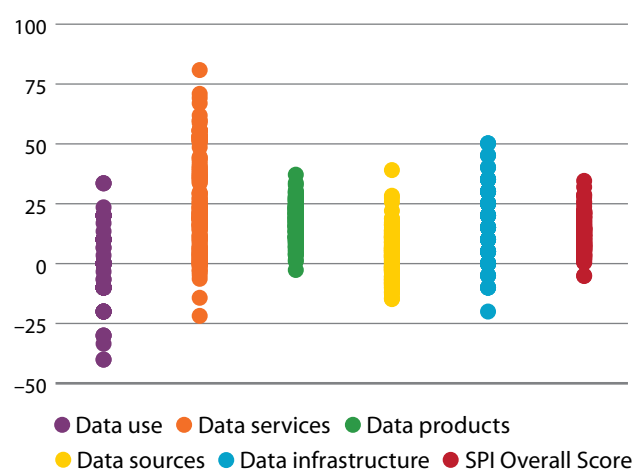
Source: UN Statistics Division calculations based on World Bank data.

Note: Data for all pillars and all years (2016–2022) are available for 167 Member States.

loans for data and statistics also reached their highest level ever, at \$240 million, while the volume of grants declined for the third consecutive year.²⁸ The World Bank has scaled up concessional lending to developing countries to strengthen statistical systems and help close core data gaps in five areas: (i) household surveys; (ii) enterprise surveys; (iii) agricultural data; (iv) price data; and (v) administrative data.

International development and national statistics communities have created new partnerships to promote funding for data and statistics. Significant efforts went into financing the production of data related to the MDG indicators, but as the MDG era came to a close, external funding declined. In 2016, the United Nations, chief statisticians of national statistical agencies and data experts from around the world launched the *Cape Town Global Action Plan for Sustainable Development Data*, which

Figure IV.8
Changes in country scores of statistical performance,
2016–2022
(Index)



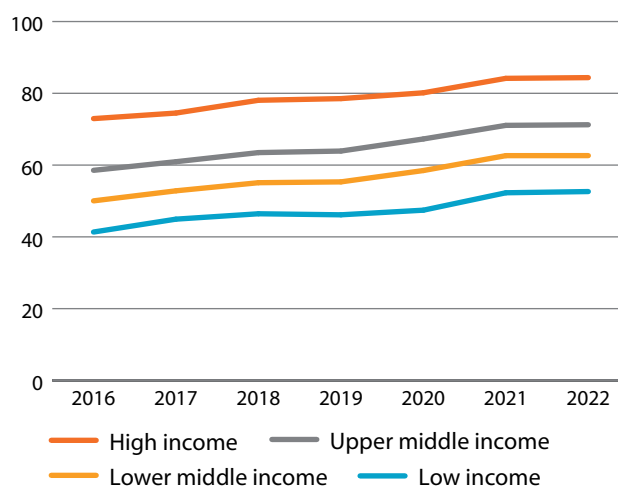
Source: UN Statistics Division calculations based on World Bank data.
Note: Data for all pillars and all years (2016–2022) are available for 167 Member States.

championed both a country-led investment blueprint as well as a call for better global coordination of development financing for data on SDG progress.²⁹ Similar calls to action have emerged from recent United Nations data forums, including the *Bern Data Compact for the Decade of Action on the Sustainable Development Goals*³⁰ and the *Hangzhou Declaration: Accelerating progress in the implementation of the Cape Town Global Action Plan for Sustainable Development Data*,³¹ both of which call for more and better investment in countries' data systems, data capacity and data capital.

Despite increasing international and domestic investments, large gaps remain. A 2022 investment case calculated that for every \$1 invested, data has delivered an average economic return of \$32 in developing countries.³² Historic investment levels for data and statistics are less than half of what is needed to deliver on data for the SDGs. Investments in data from external sources have remained relatively static for several years,³³ suffering from fragmentation and duplication of effort.³⁴

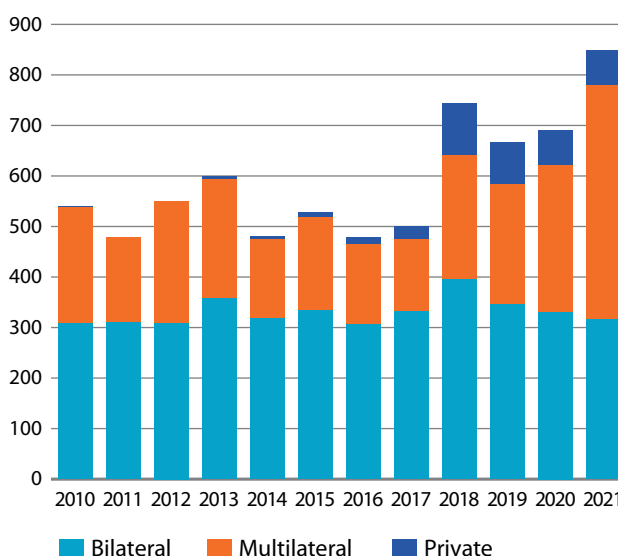
Countries are now moving towards a more coordinated global financing architecture for data and statistics. New commitments featuring stronger international cooperation to support data and statistics are materializing, although additional key actions are needed in the immediate term to maximize opportunities across regions to achieve the SDGs. Donors are pooling resources, which are leveraging significant additional funds from development banks such as the World Bank's International Development Association or International Bank for Reconstruction and Development resources. This includes the launch of new, complementary funds to support countries' data systems, data capital and risk analytics in a more coordinated way: for example the World Bank's Global Data Facility (GDF)³⁵ and the United Nations's Complex Risk Analytics Fund (CRAF'd).³⁶ The two institutions launched a high-level effort designated "Data With Purpose" and hope to jointly mobilize at least \$500 million through the GDF and CRAF'd.³⁷ These types of investments can unlock the sustained investment of domestic resources for data and statistics.

Figure IV.9
Statistical performance, by country income group,
2016–2022
(Index)



Source: UN Statistics Division calculations based on World Bank data.
Note: Country classification based on World Bank country groups by income.

Figure IV.10
External funding for data and statistics, by donor type,
2010–2021
(Millions of United States dollars)



Source: Paris21.
Note: Disbursements in constant 2021 prices.

Box IV.6**Sovereign debt data**

Improving the collection of and access to sovereign debt data is crucial for addressing the debt challenges that many countries face. For borrowers, it helps them to assess fiscal risks and make informed decisions to ensure that debt remains sustainable, which could help to lower borrowing costs. For creditors, it supports risk assessments for their lending decisions and can help to address debt distress when needed, for example by more accurately estimating the scale of debt relief required to restore debt sustainability.

Progress has been made in improving sovereign debt transparency and data in the past two decades. The World Bank's International Debt Statistics—the most comprehensive external debt database—has increased its coverage significantly, which can be partly attributed to the World Bank's new lending policy that promotes the disclosure of public debt data and the reconciliation undertaken with several key creditors. The G20 Operational Guidelines for Sustainable Financing promote information-sharing between creditors and borrowers, and the IMF and World Bank have developed a diagnostic tool to help with their implementation. The OECD Debt Transparency Initiative has set up

a data repository on private sector lending to low-income countries. The United Nations Conference on Trade and Development (UNCTAD) and the Commonwealth Secretariat's debt management and recording systems help to improve countries' ability to record, monitor and report public debt information and to submit loan-level information to the World Bank's Debtor Reporting System. The Institute of International Finance has developed a template for carveouts from confidentiality clauses that allows submission of debt data to the OECD.^a

Despite the progress made in this area, debt data challenges persist and more needs to be done. A review of the domestic legal frameworks in 60 developing countries found that less than half require the preparation of key debt-related publications. Among International Development Association-eligible countries, 23 per cent do not disclose any debt data, although the number has decreased from 40 per cent three years ago. On the creditor reporting side, very few private banks have disclosed loan data under the aforementioned OECD Debt Transparency Initiative. The Group of Seven (G7) countries have started publishing information regarding every official sector loan to other countries on their own websites, but with varied levels of detail.

^a Karla Vasquez and others. 2024. "The legal foundations of public debt transparency: Aligning the law with good practices". IMF Working Papers.

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