United Nations Secretary-General's SDG Stimulus to Deliver Agenda 2030

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Introduction

The global economy is facing multiple shocks that are threatening to further reverse progress on the Sustainable Development Goals (SDGs). The COVID-19 pandemic, impacts from the war in Ukraine, high inflation and weak economic growth, tightening monetary and financial conditions, and unsustainable debt burdens – along with the escalating climate emergency – are wreaking havoc on economies across the globe. The impact of these compounding shocks on developing countries is aggravated by an unfair global financial system that is short-term oriented and crisis-prone, and that further exacerbates inequalities.

The burden of debt overhang is battering the economies of many developing countries. As of November 2022, 37 out of 69 of the world's poorest countries were either at high risk or already in debt distress, while one in four middle-income countries, which host the majority of the extreme poor, were at high risk of fiscal crisis. The number of additional people falling into extreme poverty in countries in or at high risk of entering debt distress is estimated to be 175 million by 2030, including 89 million women and girls.[1]

A "great finance divide" has sharply curtailed the ability of many developing countries to invest in recovery, climate action, and sustainable development. Even prior to the recent rise in interest rates, least developed countries that borrowed from international capital markets often paid rates of 5 to 8 per cent, compared to 1 per cent for many developed countries. More recently, rising investor risk aversion has pushed the cost of borrowing above what would be warranted by macroeconomic fundamentals in many countries, with some middle-income countries with investment grade ratings paying between 6 and 7 percentage points above US treasury yields in 2022. Sovereign bond yields are now over 10 percentage points above US treasury yields for more than 14 countries,[2] and over 6 percentage points in 21 countries.[3]

The high cost of borrowing not only inhibits investment in the SDGs; it also raises the risk of debt crises. Recent analysis has found that most countries that have had costly debt crises in the past would have been solvent if they had continuous access to financing at low rates (akin to the borrowing costs of rich countries).[4]

High borrowing costs for developing countries are but one symptom of an inequitable international financial and monetary system. Leading economies are able to issue and borrow in their own currencies

1 Abidoye, et al 2022. *Understanding Impacts and Accelerating the SDGs in a moment of multiple overlapping crises*, UNDP Working Paper.

2 As of 13 January 2023. The 14 low- and middle-income developing countries with Emerging Market Bond Index (EMBI) spreads currently higher than 10 percentage points are Argentina, Ecuador, El Salvador, Ethiopia, Ghana, Lebanon, Pakistan, Sri Lanka, Suriname, Tajikistan, Tunisia, Ukraine, Venezuela and Zambia.

3 In addition to the 14 countries listed above, this includes Angola, Bolivia, Egypt, Kenya, Mozambique, Nigeria, and Papua New Guinea.

4 Ugo Panizza, 2022. *Long-Term Debt Sustainability in Emerging Market Economies: A Counterfactual Analysis*, Background for the 2022 Financing for Sustainable Development Report, UN-DESA Working Paper.

– facilitating, for example, quantitative easing at massive scale. In contrast, most developing countries are unable to borrow in local currencies, limiting their macroeconomic policy space and exposing them to foreign exchange risks.

The SDG Stimulus aims to offset challenging market conditions faced by developing countries and accelerate progress towards the SDGs, including through investments in renewable energy, universal social protection, decent job creation, healthcare, quality education, sustainable food systems, urban infrastructure, and the digital transformation. **The SDG Stimulus** addresses both short-term urgencies and the need for long-term sustainable development finance. It calls for a significant increase in financing for sustainable development, to the tune of at least $500 billion per year, to be delivered through a combination of concessional and non-concessional finance in a mutually reinforcing way.

Reforms to the international financial architecture are integral to the **SDG Stimulus**. As highlighted in the Addis Ababa Action Agenda,[5] financing sustainable development is about more than the availability of financial resources. National and global policy frameworks influence risks, shape incentives, impact financing needs, and help determine the cost of financing.

The **SDG Stimulus** puts forward **three** areas for immediate action:

1. ***Tackle the high cost of debt and rising risks of debt distress***, including by converting short-term high interest borrowing into long-term (more than 30 year) debt at lower interest rates.
2. ***Massively scale up affordable long-term financing for development***, especially through public development banks (PDBs), including multilateral development banks (MDBs), and by aligning all financing flows with the SDGs.
3. ***Expand contingency financing to countries in need.***

The international community must collectively implement these needed changes, while countries should put in place national policies to better align all financing flows with the SDGs, such as through Integrated National Financing Frameworks (INFFs).

The SDG Stimulus, while ambitious, is achievable. Investing in the SDGs is both sensible and feasible: it is a win-win for the world, as the social and economic rates of return on sustainable development in developing countries is very high. All the items in the **SDG Stimulus** are already under discussion at the United Nations, other multilateral forums including the Group of Twenty (G-20), at the governing bodies of international financial institutions, and in calls to action such as the Bridgetown Agenda[6]. To make this ambition a reality, urgent political will to take concerted and coordinated steps to implement this package of interconnected proposals in a timely manner is needed.

5 https://www.un.org/development/desa/financing/sites/www.un.org.development.desa.financing/files/2021-09/AAAA_Outcome.pdf

6 The 2022 Bridgetown Initiative - Foreign Affairs and Foreign Trade.

The SDG Stimulus

Action area 1: Tackle the rising risks of debt distress and the high cost of debt

Public debt burdens have worsened since the publication of UN proposals on liquidity and debt in 2021.[7] Sovereign debt has now reached critical levels, with more than a dozen countries either in technical default or at the brink of default, and policy makers in many other countries facing stark choices between paying creditors and fulfilling obligations to their citizens.

The international system does not have the tools to effectively facilitate debt restructurings that sufficiently reduce countries' debt burdens or to address a systemic debt crisis. The Common Framework for Debt Treatment (CF) failed to conclude a single restructuring in the first one and a half years of its existence, underlining that in itself it has not been sufficient to close long-standing gaps in the current debt architecture, and foremost the issue of creditor coordination amongst and between official and commercial creditors. This bodes ill for the system's capacity to address a large number of defaults effectively should a systemic debt crisis unfold. Additional steps are needed to speed up the resolution of unsustainable debt situations and prevent "too little too late" responses. While the G20 has been discussing the design and implementation shortcomings, it has not yet found consensus on a way forward.

The **SDG Stimulus** calls for *immediate actions*, including: a G20 evaluation of the Debt Service Suspension Initiative (DSSI) and Common Framework for Debt Treatment beyond the DSSI (CF); an improved multilateral debt relief initiative to support debt payment suspensions, debt exchanges (for longer maturities and lower coupons) and/or haircuts, including a clear mechanism to include private creditors in official debt relief efforts; debt for SDG or climate swaps; the inclusion of collective action clauses and majority voting provisions in all sovereign bond contracts and syndicated loan agreements, and greater use of risk-sharing debt instruments, such as state contingent debt instruments.

At the same time, the international community must continue to work towards developing *long-term comprehensive and structural solutions to sovereign debt challenges*. This includes an improved understanding of long-term debt sustainability to assess debt risks more accurately and long overdue reforms to the international debt architecture.

Immediate actions

There is an urgent need for the international community to work together to develop an improved multilateral debt relief solution, especially before large debt servicing payments come due in 2023 and 2024. This should go beyond debt service suspension to include a ready-made mechanism to facilitate debt reprofilings, exchanges, or write-downs when necessary.

As a first step, the G20 should commission an independent review and evaluation of the COVID-19 era debt initiatives. An expert panel, agreed by all G20 members, could provide an ex-post evaluation of the DSSI and the CF. It could quantify the benefits, impact, and shortcomings of the mechanisms, and propose improvements to the Common Framework. For example, an improved multilateral debt relief initiative should include debt service suspension during negotiations, and should extend to middle-income countries that might be under stress. As the Common Framework already considers debt treatments on a case-by-case basis, an expansion of eligibility will not mean automatic debt relief, but the ability to assess whether vulnerable middle-income countries need debt relief, and possible paths to access it.

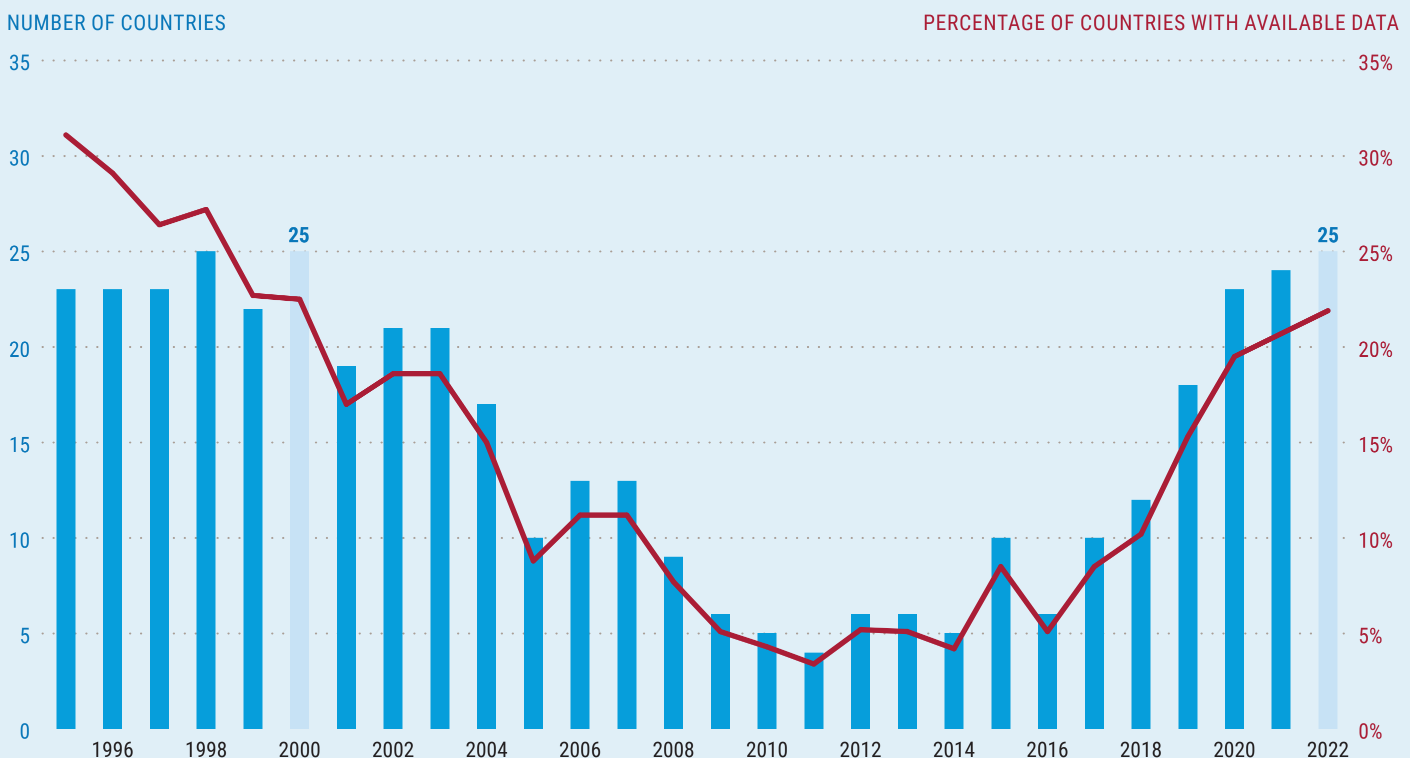
7 United Nations, *Liquidity and Debt Solutions to Invest in the SDGs: The Time to Act is Now*, March 2021, https://www.un.org/sites/un2.un.org/files/2021/03/sg_policy_brief_on_liquidity_and_debt_solutions_march_2021.pdf.

BOX 1: DEBT VULNERABILITIES HAVE INTENSIFIED, BACK TO HIPC-ERA LEVELS OF DEBT SERVICE

Debt vulnerabilities further increased in 2022 across many developing countries. For many countries debt-burden indicators are back at levels last seen during past periods of debt crises. It is estimated that in 2022, 25 developing countries paid more than 20 percent of total government revenue in external debt service – a number of countries not seen since the year 2000 at the beginning of the Highly-Indebted Poor Countries (HIPC) initiative (Figure A).[i]

Measured based on a combination of credit-ratings, debt-sustainability ratings, and bond spreads, more than 50 developing countries, including many middle-income countries, are suffering from severe debt problems; 26 of 91 developing countries with credit-ratings are currently rated at either 'substantial risk, extremely speculative or default', up from ten countries at the beginning of 2020.[ii]

Figure A: Number of countries paying more than 20 percent of government revenue in external PPG debt service



Source: UNDP based on external PPG debt service data from World Bank IDS database and government revenue data from IMF WEO October 2022 database. Note: Debt service includes interest and principal payments on public and publicly guaranteed (PPG) debt.

i The median country paying more than 20 percent paid 28.6 percent in 2000 and 27 percent in 2022.
ii See *Avoiding 'Too Little Too Late' on International Debt Relief*, UNDP, October 2022. https://www.undp.org/publications/dfs-avoiding-too-little-too-late-international-debt-relief

Second, the international system needs to develop concrete tools to incentivize or enforce private creditors to participate in official debt restructurings, such as in debt exchanges for longer maturities and lower interest rates. Without such a mechanism, private creditors generally have an incentive to *not* participate. For example, debt buybacks, financial guarantees, and/or collateralization were part of the Heavily Indebted Poor Countries (HIPC) initiative in the 1990s and the resolution of the Latin American debt crisis of the 1980s. Several countries also passed laws to limit the ability of non-cooperative creditors to undermine debt relief achieved under HIPC. Additionally, the international community

could explore debt issuance that incorporates most-favoured-creditor clauses.

Third, debt for climate and SDG swaps, which have attracted growing interest,[8] can be helpful for countries that do not yet have unsustainable debt burdens but do have limited fiscal space for SDG investment. While such swaps do not generally restore debt sustainability, they allow countries to redirect debt service payments toward investments in sustainable development and climate action. Debt-for-climate swaps could be structured to allow creditor countries to apply the value of the debt relief towards their climate commitments. Such swaps can either be done bilaterally between an official creditor and a debtor (such as those done by L'Agence française de développement), or by using official or philanthropic funds to buy bonds at a discount in secondary markets (most debt for nature swaps). These can be structured so that the new creditors pass on part or all of the discount to sovereign debtors. Thus far, although there have been examples of successful debt for investment swaps, uptake has been limited, in part due to high transaction costs. A reference framework (which could include template term sheets and performance indicators) could help standardize contracts to the extent possible. This could be complemented by official financial support, such as partial guarantees or collateralization such as those used in Brady bonds.

Fourth, official creditors should also systematically include state-contingent elements into lending. Some official lenders (both bilateral and multilateral, e.g., IADB) already have experience with this approach, which should now become standard practice. This would provide automatic debt suspension in the event of pre-defined shocks (such as natural disasters, declines in GDP, or commodity price changes, akin to parametric insurance triggers), and can be structured to be NPV-neutral. State-contingent debt would obviate the need to negotiate a debt service suspension initiative during a crisis. If used at sufficient scale, such clauses can also help prevent a liquidity crisis from turning into a solvency crisis.

Longer-term reforms to the sovereign debt architecture

IMF debt sustainability assessments (DSAs) provide a basis for estimating a country's debt sustainability.[9] Such analyses are based on average expected interest rates; they thus take into account market interest rates for the many developing countries that have borrowed on commercial markets. Measuring debt sustainability using market interest rates would tend to indicate an increased risk of default during a liquidity crisis when borrowing costs (and developing country credit spreads) rise sharply, with default expectations at risk of becoming 'self-fulfilling'. In the context of the **SDG stimulus**, a "solvency-focused" analysis could complement existing DSAs: using refinancing scenarios based on MDB borrowing terms, which are below market interest rates, could help distinguish between liquidity challenges (when long-term affordable financing can be the solution) and solvency crises (when debt write-downs may be needed).

Comparing the "solvency-focused" outcome to traditional DSAs would highlight when a country would be fundamentally solvent if it had access to improved financing terms. Further review of debt sustainability assessments could also aim to better reflect a country's SDG needs as well as progress on sustainable development by recognizing the long-term value of productive investment in sustainability and resilience. Complementary reforms for longer term modelling could also be promoted for credit assessments of sovereigns by private credit rating agencies.

At the same time, concrete steps must be taken toward a permanent mechanism to address sovereign debt distress including the perennial challenge of creditor coordination, with a view to create a fully operational, timely, and effective sovereign

8 Chamon, Klok, Thakoor, and Zettelmeyer (2022) *Debt-for-Climate Swaps: Analysis, Design, and Implementation*, IMF Working Paper WP/22/162.

9 In 2021 the IMF enhanced its framework for market access countries by: i) broadening debt coverage and including a longer projection horizon; ii) including new tools with different time horizons; iii) enhancing transparency; and iv) providing probabilistic debt sustainability assessments.

debt restructuring mechanism, as called for in the Addis Ababa Action Agenda.[10]

Action area 2: Massively scale up affordable and long-term financing for development

The **SDG Stimulus** calls for a massive boost in investment in crisis response and the SDGs in developing countries, including financing climate action as an indispensable entry point with impact across the SDGs. Public development banks (PDBs), including multilateral development banks (MDBs), are uniquely positioned to play a more important role in accelerating this investment. PDBs can scale up long-term financing that is "non-concessional" but still significantly below the market rates currently paid by developing countries, including to meet investment needs in middle-income countries.

The increase in lending for investment in the SDGs needs to be done in conjunction with improved debt management. When financing supports productive investments in the SDGs, it will also stimulate growth, generate employment, reduce risks, and ultimately improve debt sustainability – even while raising debt-to-GDP in the near term. A high cost of debt servicing (e.g., greater than economic growth), however, increases the risk of debt burdens becoming unsustainable. PDB loans are indispensable because they can lend long-term at interest rates close to the rates paid by developed countries. For example, as of October 2022, World Bank IBRD loans are less than 150 basis points over US Treasuries for most bank's clients.[11]

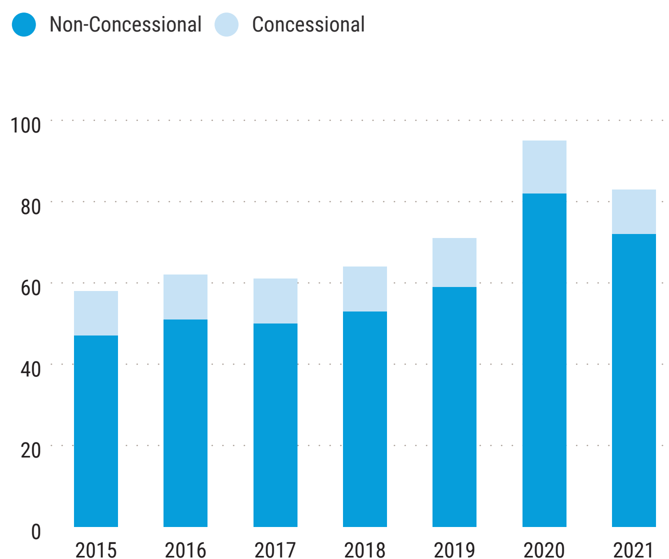
PDBs already have a large footprint — 522 development banks and development finance institutions have total assets of US$23 trillion.[12] PDBs are estimated to finance around 10-12 per cent of investment globally. MDBs are much smaller in size with annual disbursements totalling almost $100 billion per year collectively (see figure 1). Nonetheless, MDBs provided exceptional support to offset global crises, such as in 2009, and again in 2020, though they were constrained in their COVID-19 pandemic response due to limited financial capacity. With greater financial capacity, MDBs and PDBs have the potential to play a much larger role in development finance.

Strengthening MDBs

With stronger capital bases and better use of existing capital, MDBs can increase lending from $100 billion per year to **at least** $500 billion per year.

Shareholders have not increased the size of MDBs paid-in capital bases in line with the increase in size of the global economy or the needs for sustainable development investment (see figure 2). While the World Bank received a sizeable capital increase in 2018, it was not on the scale needed to finance a massive investment push to achieve the SDGs by 2030. Of the regional banks, only the African

Figure 1: Loan disbursements by multilateral development banks, 2015–2021
(Billions of United States dollars)



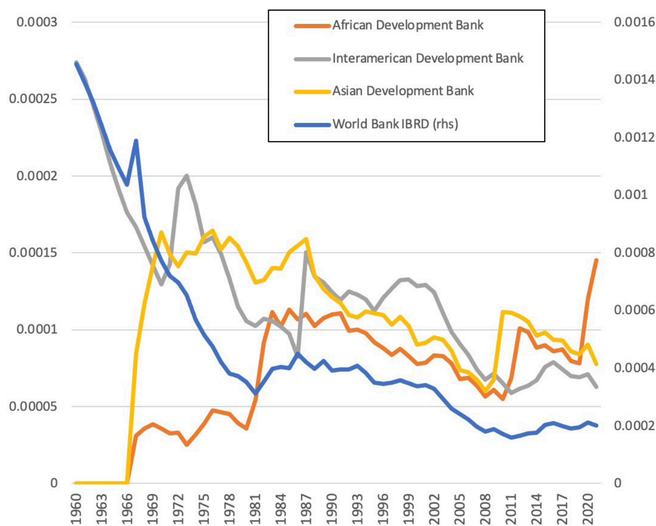
Source: World Bank, International Debt Statistics

10 See United Nations, *Liquidity and Debt Solutions to Invest in the SDGs: The Time to Act is Now,* March 2021.; and UN policy brief on the international financial architecture, forthcoming.

11 8 to 10-year IBRD dollar loans are priced at 1.09 per cent over a variable SOFR for most clients. C. Landers and R. Aboneaaj, *Is World Bank Lending a Hot Ticket in a Global Credit Crunch?,* CGD Blog Post, November 2nd, 2022.

12 Finance in Common, *FICS Progress Report 2022*, October 2022.

Figure 2: Paid-in capital as a share of world gross product, select MDBs, 1960-2021
(Ratio)



Source: United Nations calculations

Development Bank has received a sizeable capital increase recently.

To further increase MDB lending capabilities, shareholders need to increase the size of the banks' capital bases. At the same time, the banks need to leverage their capital bases more efficiently. Countries have been calling for MDBs to maximise the use of their balance sheets since the adoption of the Addis Ababa Action Agenda, and recapitalization discussions have been ongoing for years. India, as the 2023 president of the G20, has suggested a strong focus on MDB reforms, and the World Bank itself has drawn up an "Evolution Roadmap".

Table 2 presents two scenarios for capital increases, noting that these numbers are indicative and meant to give a range of possible outcomes. In the first scenario, the size of the current capital base of each bank is doubled. In the second scenario, MDB capital is set so that paid-in capital as a share of world gross product is equivalent to its highest level since 1960 (implying a particularly large increase for the World Bank). Such capital increases could be contributed over time, for example over 5 years. If the resulting lending capacities shown in Table 2 were disbursed over a 6-year time horizon, it would equate to between $80 and $310 billion of additional lending per year.

More efficient use of existing capital, such as by adopting more flexible criteria could further expand the lending capacity of MDBs. For example, MDB shareholders typically pay-in only a small portion of the banks' capitalization, with the rest considered as callable capital (see table 1). Some MDBs conservatively only use paid-in capital in their internal capital adequacy calculations, even though credit rating agency methodologies count a portion of callable capital when assessing credit worthiness. The G20 Capital Adequacy Framework (CAF) Review provides solid first steps for using the MDBs' capital more efficiently. Studies by S&P, the Bank of Italy and other researchers have estimated that revising MDB capital adequacy policies could boost MDB lending by $500 billion while preserving credit ratings, or over $1 trillion with a one notch fall in ratings.[13] The CAF Review indicates that its proposed reforms would result in several hundred billion dollars in available lending over the medium term.

Combining an increase in paid-in capital with more efficient use of their balance sheets, could increase MDB investments substantially. While each bank would need to carefully model the scenarios based on its existing financing structure, applying CAF review estimates to the capital increase scenarios shown in Table 2 implies that a boost to lending could be between $1 trillion and $3 trillion. While the numbers shown are just indicative, they reveal significant scope to deliver much of the needed public resources for investment in the SDGs.

Rechannelling special drawing rights (SDRs) through MDBs, which are already prescribed SDR holders, can contribute to increased MDB lending. The MDBs should develop a concrete instrument to operationalize the use of rechannelled SDRs in

13 Standard & Poor's, *Key Considerations for Supranationals' Lending Capacity and Their Current Capital Endowment*, 18 May 2017; Riccardo Settimo, *Higher multilateral development bank lending, unchanged capital resources and triple-a rating: A possible trinity after all?*, Occasional Papers n. 488, Bank of Italy, April 2019; Waqas Munir and Kevin Gallagher, *Scaling Up for sustainable development: Benefits and costs of expanding and optimizing balance sheet in the multilateral development banks*, Journal of International Development, January 2020, 32(2), 222–243.

TABLE 1: CAPITALIZATION OF SELECT MULTILATERAL DEVELOPMENT BANKS, 2021

INSTITUTION	EXISTING PAID-IN CAPITAL	CALLABLE CAPITAL	SUBSCRIBED CAPITAL	EXISTING ASSETS & LOANS
IBRD	$20 billion	$279 billion	$298 billion	$227 billion
African Development Bank	$14 billion	$194 billion	$208 billion	$32 billion
Asian Development Bank	$7.5 billion	$141 billion	$149 billion	$140 billion
Inter-American Development Bank	$6 billion	$171 billion	$177 billion	$110 billion
TOTAL	**$47 billion**	**$785 billion**	**$831 billion**	**$509 billion**

Source: S&P Global, MDB annual reports

a timely manner. While not all countries are legally able to accomplish such a rechannelling, MDBs can design these instruments to preserve the SDR role as a reserve asset, building on experiences at the IMF.[14] This could be complemented with the exploration of changes to allow more countries to re-channel SDRs through MDBs and other prescribed holders. For instance, developed countries could lend their SDRs through a hybrid debt instrument which would allow MDBs to count them as quasi-capital, thus further enhancing MDBs' capacity for long-term financing.

Improved terms of lending

Additional leverage and capital infusion would provide the head room needed to improve the terms of lending, including: the cost of borrowing, loan maturities, repayment schedules (including state-contingent repayments), and exposure to exchange rate volatility.

First, MDB lending should be long-term (30 to 50 years), with more significant grace periods to allow time for large scale SDG-related investments to yield results in terms of contributing to economic growth, realizing improved wellbeing and productivity from human capital investments, and generating savings from resilience to shocks.

Second, the MDBs should offer low interest rates, akin to borrowing costs of developed countries, especially for vulnerable countries that might not have sufficient access to affordable finance. As global financial conditions tighten, it is especially important that the MDBs have the capacity to act counter-cyclically. The banks could mix concessional and non-concessional[15] resources, with the criteria for the allocation of international public resources based on all the dimensions of vulnerability that affect developing countries, and not solely on a country's national income. This should include using measurements that go beyond GDP or the

14 Such as with the Poverty Reduction and Growth Trust (PRGT) and Resilience and Sustainability Trust (RST).

15 Non-concessional in this case refers to lending without subsidies provide by aid. However, MDB loans are all concessional in the sense that they offer better terms than market borrowing.

TABLE 2: ILLUSTRATIVE IMPACT OF RECAPITALIZING SELECT MULTILATERAL DEVELOPMENT BANKS

INSTITUTION	EXISTING PAID-IN CAPITAL	EXISTING ASSETS AND LOANS	RANGE OF POTENTIAL PAID-IN CAPITAL INCREASES	POTENTIAL INCREASE IN LOANS FROM PAID-IN CAPITAL
IBRD	$20 billion	$227 billion	$20 billion	$225 billion
			$120 billion	$1.39 trillion
African Development Bank[i]	$14 billion	$32 billion	-	$30 billion
			$14 billion	$59 billion
Asian Development Bank	$7.5 billion	$140 billion	$7.5 billion	$110 billion
			$8 billion	$123 billion
Inter-American Development Bank	$6 billion	$110 billion	$6 billion	$94 billion
			$20 billion	$314 billion
TOTAL	**$47 billion**	**$509 billion**	**$47-148 billion**	**$487 billion - 1.86 trillion**

i The African Development recently received a doubling of paid-in capital, raising the size of the bank to its highest level ever. For AfDB additional lending represents the mobilisation of resources from the recently paid-in capital on the low end, and another doubling of paid-in capital on the high end.

Source: UN calculations, S&P Global, MDB annual reports.
Note: Range of paid-in capital increases are derived from: on the low-end doubling paid-in capital, and on the high end returning the MDB to its historic greatest size compared to the global economy since 1960. The increase in loans assumes the banks leverage new capital in line with the average leverage they achieved in the 3 years pre-COVID. Figures reflect 2021 and are rounded.

multidimensional vulnerability index (MVI) currently being developed at the United Nations.

Third, greater use of state-contingent clauses in MDB lending can provide breathing room to countries hit by shocks by automatically suspending payments in the case of a disaster, economic or financial crisis, or other exogenous shocks, as is already done by some bilateral and multilateral lenders (see below). These could be structured to be net-present-value (NPV) neutral debt service suspensions to have minimal impact on MDB credit quality.

Fourth, providing a greater share of lending to governments in local currencies would contribute to lowering borrowers' debt risk profiles, particularly when lending for projects that are unlikely to generate foreign currency earnings. International financial institutions (IFIs) are better placed than sovereigns to manage currency risk since IFIs can diversify across currencies while sovereigns face a concentrated foreign exchange risk. Several MDBs have increased their local currency offerings; the World Bank, for example, offers currency conversions for 25 local currencies. The MDBs typically do not take the currency risk on their balance sheet and the extra costs of executing mirroring transactions with private market participants are passed on to the sovereign borrower. Instead, MDBs could manage the currency risks on their large balance sheets, which could serve as a diversified portfolio, as called for in the Addis Ababa Action Agenda.

Strengthening the system of public development banks

Just as there is scope to increase the capitalization of MDBs, in many countries there is scope to increase the capital base of national and subnational development banks, as well as ensure that the PDBs are putting their balance sheets to optimal use. This should be combined with effective risk management and strengthened governance. Regulatory frameworks applied to NDBs can be tailored to protect their financial sustainability while incentivizing the sustainable development effectiveness of their investment. PDBs operations should be fully aligned with the SDGs in a holistic way and could be considered in Integrated National Financing Frameworks (as discussed below).

Closer cooperation across MDBs and PDBs to strengthen the entire development bank system would enable greater impact and potentially higher lending. This can be achieved, for example, through greater use of co-financing and other risk-sharing mechanisms, which can allocate risk across the PDB system and reduce risks on individual MDB balance sheets. MDBs should also strengthen their financial cooperation and technical assistance provided to national development banks. In turn, regional and global institutions can benefit from the local knowledge of national institutions. In addition, reinforcing collaboration and strengthening practices through platforms such as the *Finance in Common Initiative*, which gathers many PDBs, can ensure a strong alignment of investments for the SDGs, particularly climate action, thus multiplying their impact.

Meeting ODA commitments, providing grants where needed

The most vulnerable countries will still need grants to finance their investments in the SDGs, including countries that are facing enormous humanitarian financing gaps. While official development assistance (ODA) increased to its highest level in 2021 and is expected to increase further in 2022, it failed to keep pace with rising needs and demands from the COVID-19 crisis and the impacts of the war in Ukraine. In addition, much of the increase in ODA has financed in-donor refugee costs and humanitarian spending to address the food crisis and other emergencies. Ensuring that ODA remains additional to other sources of international support, and is not diverted from traditional development priorities, remains essential to help support humanitarian aid appeals around the world, including but not limited to addressing the impacts of the War in Ukraine. Moreover, ODA remains at less than half the agreed target of 0.7 per cent of donor country gross national income. Meeting ODA commitments would provide over $150 billion per year in stimulus for the SDGs.

As noted above, the allocation of concessional finance, as well as debt relief, should be based on all dimensions of vulnerability and not solely on a country's national income. The multidimensional vulnerability index can give the international community a new yardstick to guide allocations and help address a longstanding concern of Small Island Developing States as well as many other countries in special situations. Criteria for the allocation of ODA used for debt relief can also be prioritised based on vulnerability and need.

Combining public and private finance towards public aims

The private sector plays an important role in financing sustainable development and filling financing gaps – particularly for projects where there is an expected cash flow to repay the private partner. Public funds can be used to crowd in private finance and unlock investment in the SDGs where the private sector would not have invested on its own, often due to high perceived risks. MDBs, PDBs, and development cooperation agencies can work more closely with private partners to leverage resources, such as through guarantees and first loss tranches. However, blended finance efforts to date have not had a large impact and have in some cases overcompensated private partners.

A *new approach* to blended finance is needed, including a focus on development impact rather than bankability, use of non-concessional loans, and structures where the public sector can share both risks and rewards fairly, as called for in the

Addis Ababa Action Agenda. Blended finance inherently lowers risks. In no case should official guarantees overcompensate the private partner. It is also important to engage the appropriate private partner for a given transaction. For example, private partners with short to medium investment horizons, who require an exit strategy, should only be engaged in deals where this is likely to be feasible (e.g. where countries have liquid domestic capital markets). A strong emphasis on country ownership is also necessary to ensure that blended finance projects are aligned with national strategies.

Action area 3: Expand contingency financing to countries in need

The current international monetary and financial system exposes developing countries to sudden changes in financial market sentiment and high volatility of capital flows. Many developing countries – especially those that are facing intermittent access to markets amid high financial market volatility – will need greater financial assistance in the near term. Urgent efforts are also needed to change the global financial architecture from one that is short-term oriented and crisis-prone, to one that is resilient and better able to absorb shocks. **The SDG Stimulus** includes steps to strengthen the global financial safety net and address immediate liquidity needs to help countries improve their crisis response.

Special drawing rights (SDRs)

The allocation of SDRs in August 2021 provided countries with liquidity without creating additional debt. Amid the multiple external shocks, developing countries have lost an estimated $379 billion of reserves in 2022, almost double the amount of SDRs they received in the allocation. **The SDG Stimulus** calls for a new issuance of SDRs.

The SDG Stimulus calls for countries with unused SDRs to urgently re-channel them to countries in need, including through rapid disbursing instruments at concessional terms and with minimal conditionalities. Promises to do so have already been made through the G-20, but the results need to be achieved more quickly. As noted above, MDBs should also develop a concrete instrument to allow countries to channel unused SDRs through the banks.

Unused or newly allocated SDRs could also back a new trust to finance climate mitigation projects in developing countries. A Green Fund based on SDRs contributed as capital was first proposed in 2009,[16] and this idea has been revived under the Bridgetown Agenda. The IMF has already operationalized a Resilience and Sustainability Trust (RST), but the scale and ambition is not commensurate with the challenges faced by the world and the growing demand for resources.

Other innovative mechanisms to increase global liquidity and leverage resources for sustainable development

The international community should also continue to explore or accelerate the implementation of other mechanisms that can increase liquidity and boost available resources for sustainable development. The recent operationalization of the IMF Resilience and Sustainability Trust (RST) is a welcome development. It is expected to support countries in building resilience to external shocks such as climate change and pandemics, while contributing to sustainable growth and long-term balance of payments stability. Nevertheless, tying the RST to other IMF programmes with strict conditionality is a concern, and while RST arrangements have a 20-year maturity for repayment, the resources are disbursed alongside a short-term IMF programme.

Growing risks from more frequent and interconnected shocks will require new financing instruments. The IMF's new Food Shock Window can help to ease urgent balance of payment pressures in some of the hardest-hit countries. The Loss and Damage Fund agreed to in COP27 is a welcome

16 Hugh Bredenkamp and Catherine Pattillo, *Financing the Response to Climate Change*, IMF Staff Position Note SPN10/06, March 25, 2010.

development. New instruments should be quick disbursing, with low interest rates, and parsimonious conditionality. Access limits to emergency lending windows at the IMF and the World Bank should also be increased.

Countries can explore the creation of regional mechanisms to increase liquidity, including through enhancing regional financing arrangements. The presence of central bank swap lines, typically extended from reserve currency central banks to the central banks of other developed countries, has already proven effective at calming markets during periods of volatility. Extending the availability of swap lines to more developing countries would contribute to reassuring cross-border investors. To increase access to swap lines for all, the IMF could facilitate a multilateral currency swap facility, with the participation of global reserve currency issuing central banks, to provide access to emergency liquidity for a broader set of developing countries.

In the long-term, the international financial architecture could also be made more shock-absorbent and resilient by ensuring that financial resources can automatically be provided to countries during times of shock. This is needed because in times of crises there is a flight to safety among international investors, whereby there is a rush to hold assets denominated in hard currencies. This ultimately leads to currency depreciation in developing countries. This could include integration of state-contingent and disaster clauses, as well as mechanisms to enable countercyclical issuance of SDRs in a more automatic or timely manner in times of crisis, which would avoid protracted political negotiations during crises and provide SDRs for immediate use when most needed.

To ensure that societies are better prepared for future shocks and can benefit from just transitions as digital, demographic, and green transformations accelerate, a whole-scale effort is also needed to re-prioritize where, and how, investments are made. As will be elaborated below, this calls for aligning all forms of finance with the SDGs including by using tools such as Integrated National Financing Frameworks (INFFs) to help determine the finance mix in countries and identify how resources can be mobilized and re-directed.

Implementation and operationalization at the country level

In addition to the implementation of the SDG Stimulus at the global level, the UN, IMF, and MDBs should work closely together in supporting countries in 2023 and beyond to implement the SDG Stimulus on a case-by-case basis.

Several countries are exploring implementing the **SDG Stimulus** at the country level through INFFs, which were first introduced in the 2015 Addis Ababa Action Agenda. In October 2021, G20 Leaders endorsed the G20 Framework of voluntary support to INFFs.[17]

INFFs help governments chart long-term SDG investment plans and fiscal frameworks based on national priorities, consistent with a sustainable debt trajectory. The INFF methodology puts forward discrete steps countries can take to incorporate financing for the SDGs into national planning.[18] INFFs provide tools for Governments to assess financing needs (laying out alternative need assessment methodologies); map out financing flows and link them to needs; evaluate investment policy options, including trade-offs across the SDGs; and prioritize new financing policy actions through a holistic approach (see Box 2).[19]

Well-designed INFFs can contribute to improved clarity about how international resources can best be used. All official creditors — including bilateral donors, the IMF, multilateral development banks, and others — need to coordinate their actions with country-led and country-owned INFFs. The recently launched INFF Facility[20] brings together international efforts to support countries as they develop and operationalise INFFs.

At the country-level, INFFs can also help ensure that all investments are aligned with national priorities and ensure that investments that provide buffers to populations during crises and yield long-term returns — such as universal social protection, decent job creation, and re-skilling and lifelong learning programmes — are prioritized. Several UN-led initiatives, including the Global Accelerator on Jobs and Social Protection for Just Transitions, are aiming to support governments in prioritizing and enhancing investments in these areas.

17 Financing for Sustainable Development Outcome Document, G20 Development Working Group, 2021. https://dwgg20.org/app/uploads/2021/10/DWG-outcome-document-on-Financing-for-Sustainable-Development.pdf

18 See *INFF Guidance Material* laid out by building block at https://inff.org/ Building Blocks.

19 See also the 2019 *Financing for Sustainable Development Report* https://developmentfinance.un.org/fsdr2019.

20 Financing for Sustainable Development Outcome Document, G20 Development Working Group, 2021. https://dwgg20.org/app/uploads/2021/10/DWG-outcome-document-on-Financing-for-Sustainable-Development.pdf

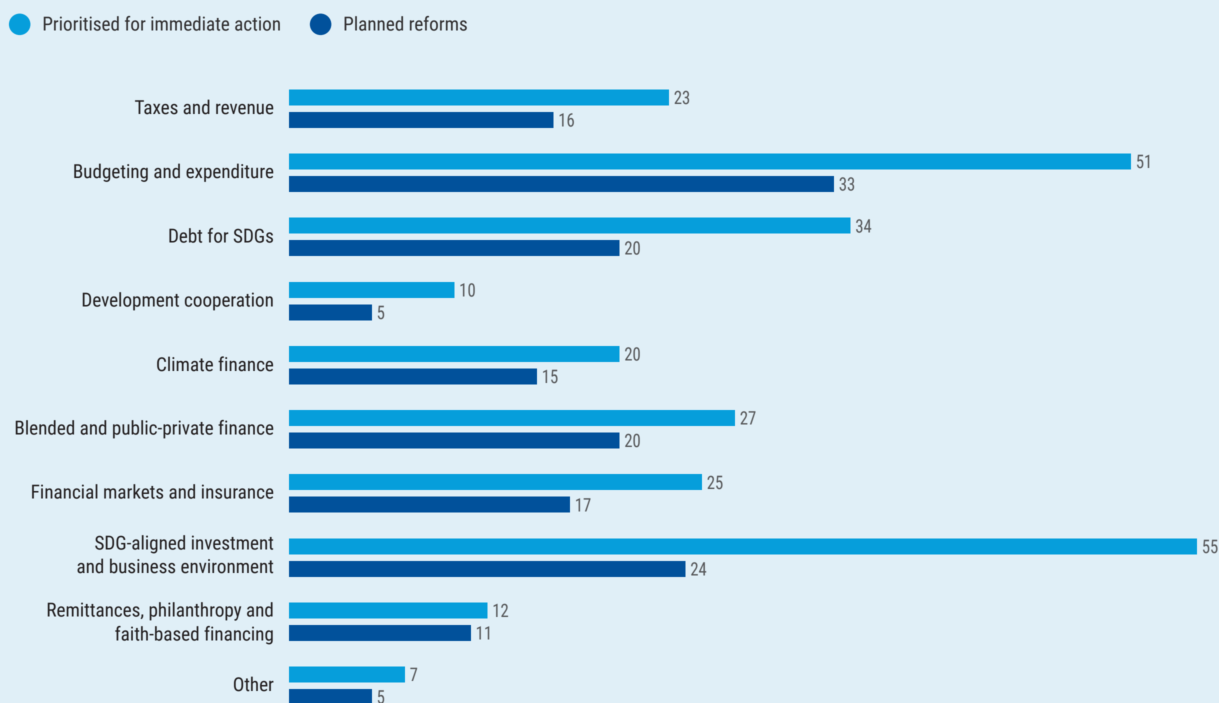
BOX 2: IMPLEMENTATION OF COUNTRY-LED INTEGRATED NATIONAL FINANCING FRAMEWORKS

As of year-end 2022, 85 countries are developing INFFs to finance national SDG priorities.[21] INFFs are country-owned processes, generally led by Ministries of Finance and Planning, built on dialogue with national stakeholders from across the public sector, private sector, and civil society.

A 2019 study found that while most countries were incorporating the SDGs into national developing strategies, the majority of plans were not costed.[22] INFFs help countries fill this gap. They lay out mechanisms for countries to estimate the cost of achieving the SDGs and help countries design financing strategies to mobilise and align public and private capital using the full range of public policies, financing instruments and partnerships. As of year-end 2022, 39 countries are articulating INFF financing strategies for the first time, with another 25 broadening the scope of existing financing strategies to consider private as well as public finance for the SDGs.[23] The first two INFF financing strategies were launched during 2022.[24]

A survey in early 2022 found that countries implementing INFFs identified more than 250 financing policy reforms for immediate action (Figure 3). These reforms include integrating the SDGs into national budget processes; mobilising and aligning tax policy with the SDGs; deploying innovative debt instruments within sustainable debt frameworks; unlocking public-private investments; and steering incentives in financial markets and commercial investments toward the SDGs. Many countries are systematically identifying and promoting SDG-aligned investment opportunity areas through their INFFs, with more than 450 SDG-aligned investment opportunities identified to date.[25]

Financing policy reforms being prioritised through country-led INFFs, 2022
(Number of reforms)



Source: State of INFFs in 2022, INFF Facility

21 Including 16 low-income countries, 37 lower-middle income countries, 29 upper-middle income countries, 33 least developed countries, 18 small island developing states and 32 in fragile settings.

22 A review of 107 national development plans in 2019 found that the majority (79) had no specific costing associated with plan implementation and only a minority (29) explained how they would be financed. Chimhowu, A., Hulme, D., Munro, L., 2019, The *'New' national development planning and global development goals: Processes and partnerships*.

23 The State of INFFs in 2022, INFF Facility. https://inff.org/resource/the-state-of-integrated-national-financing-frameworks-in-2022-or-report

24 The President of Nigeria launched the Nigerian financing strategy in September 2022. The Mongolian National Committee for Sustainable Development, which is chaired by the Prime Minister, endorsed Mongolia's financing strategy in August 2022.

25 *2022 INFF Sustainable Investment Stocktake for the G20 Development Working Group*, 2022, INFF Facility. https://inff.org/resource/2022-inff-sustainable-investment-stocktake.

Call to Action and Recommendations

The SDGs are issuing an SOS. The SDGs include the indispensable transitions needed for sustainability, peace, and prosperity – for example combatting climate change and financing the digital transition. Yet, the cascading crises have pushed the SDGs out of reach. The Human Development Index has fallen globally for two years in a row, for the first time in over three decades. The impact of these compounding shocks on developing countries is further exacerbated by an unfair global financial system that relies on short-term cost-benefit analyses, is crisis-prone, and favours the rich over the poor. An SDG financing boost is sorely needed.

The SDG Stimulus aims to offset deteriorating conditions faced by developing countries and accelerate progress towards the SDGs. It calls for a substantial increase in financing for sustainable development, on the order of at least 500 billion per year - at the bare minimum. Such investments need to be financed by long-term affordable financing – requiring a major expansion of lending by the MDBs and better terms on borrowing.

In his opening address to the UN General Assembly on 20 September 2022, the UN Secretary-General called on the G20 to support the **SDG Stimulus**. He followed up with letters to the G20 Finance Ministers and Central Bank Governors and the G20 summit leaders, urging the G20 to endorse the Stimulus, including:

Tackle the high cost of debt and rising risks of debt distress

- The G20 should commission an **independent review and evaluation** of past, existing and prospective debt initiatives. An expert panel, agreed by all G20 members, could provide an evaluation of the CF and alternative proposals.
- Develop an improved **multilateral debt relief initiative**, to support debt payment suspensions, debt exchanges (for longer maturities and lower coupons) and/or haircuts, with an expansion of eligibility to all vulnerable countries in need.
- In conjunction with the improved debt relief initative, develop a concrete tool to **incentivize, encourage, or enforce private creditors participation** in official debt restructurings.
- Develop a program **for debt for SDG or climate swaps,** which allow countries to use debt service payments for investments in sustainable development and climate action, freeing up fiscal space.
- Systematically include **state-contingent elements** into lending by all official creditors.
- **Develop "solvency focussed" debt sustainability assessments** (DSAs) for market access countries and include the SDGs and non-economic factors.

- Take concrete steps toward a **permanent mechanism to address sovereign debt distress**.

Massively scale up affordable long-term financing for development

- **Strengthen the MDBs** by increasing their capital bases, better leveraging their balance sheets, and re-channelling SDRs through them.
- **Improve the terms of lending by MDBs**, including longer-terms, lower interest rates, use of state-contingent clauses, and more lending in local currencies.
- **Strengthen the system of public development banks (PDBs)**, with increased capacity and more cooperation between national and multilateral banks.
- **Meet ODA commitments** with allocations of grants based on vulnerabilities, not only income.
- **Combine public and private finance towards public aims** with a focus on development impact and country ownership.

Expand contingency financing to countries in need

- **A new issuance of SDRs**; re-channel unused SDRs to those in need more quickly; set up concrete mechanism to re-channel unused SDRs through MDBs.
- Create a work programme to explore how **SDRs can finance climate mitigation and be automatically issued in times of crisis**.
- **Explore other innovative mechanisms to increase global liquidity,** by increasing access limits to existing emergency lending windows at the IMF and World Bank, and through new instruments that are quick disbursing, with low interest rates, and parsimonious conditionality.
- **Create regional mechanisms to increase liquidity**, including through enhancing regional financing arrangements and making central bank swap lines more widely available.

Implementation and operationalization at the country level

In addition to the implementation of the **SDG Stimulus** at the global level, the UN, IMF, and MDBs should work closely together in supporting countries in 2023 and beyond to implement the **SDG Stimulus** on a case-by-case basis. Integrated National Financing Frameworks (INFFs) can help operationalize the **SDG Stimulus** at the national level including by re-prioritizing investments in sectors vital to boosting resilience and providing buffers during shocks such as universal social protection, decent job creation, re-skilling, and life-long learning programmes. They are an ideal tool for countries to set out their priorities and key financing policies.

Most of the elements in the **SDG Stimulus** – strengthening the system of MDBs and PDBs, addressing debt risks, ensuring contingency finance when needed, and national actions – are already on the international agenda. They need a political push to make the ambition a reality.

The United Nations, with its ability to convene governments and relevant stakeholders across multiple domains, is uniquely placed to move reforms forward. 2023 will be a critical year as we mark the half-way point to the 2030 Agenda and host the High-Level Dialogue on Financing for Development, a Climate Ambition Summit, and an SDG Summit in September. Agreement on this **SDG Stimulus** by Heads of State and Government will lock in a chance to rescue the SDGs and deliver on our collective promises to citizens of the world.