Financing for Sustainable Development Report 2022

Inter-agency Task Force on Financing for Development

Bridging the Finance Divide

United Nations

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

Financing for Sustainable Development Report 2022

United Nations

This report is a joint product of the members of the Inter-agency Task Force on Financing for Development. The Financing for Sustainable Development Office of the United Nations Department of Economic and Social Affairs serves as the coordinator and substantive editor of the Financing for Sustainable Development Report.

The online annex of the Task Force (http://developmentfinance.un.org) provides additional data and analysis on progress in implementation of the Financing for Development outcomes, including the Addis Ababa Action Agenda and relevant means of implementation targets of the Sustainable Development Goals.

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 (DC2-2170)
New York, N.Y. 10017
United States of America
+1-212-963-7574

developmentfinance@un.org

http://developmentfinance.un.org

Federal Ministry
for Economic Cooperation
and Development

The production of this report and the online annex of the Inter-agency Task Force are generously supported by the Federal Ministry for Economic Cooperation and Development of Germany.

How to cite this report:

United Nations, Inter-agency Task Force on Financing for Development, *Financing for Sustainable Development Report 2022.* (New York: United Nations, 2022), available from: https://developmentfinance.un.org/fsdr2022.

United Nations publication

Sales No. E.22.I.6
ISBN: 978-92-1-101452-5

Overview and key messages



Overview and key messages

A year ago, the Inter-agency Task Force warned of the risk of a diverging world that could lead to a lost decade for sustainable development. Now, at the halfway mark to implementation of the 2030 Agenda, divergence is our reality. While many developed countries saw a rapid economic recovery from the pandemic shock in 2021, developing countries did not regain lost ground. In one in five developing countries, GDP per capita was projected to remain below 2019 levels by the end of 2023. This is even before accounting for the fallout from the war in Ukraine. The result is a severe setback to the Sustainable Development Goals (SDGs), with an additional 77 million people living in extreme poverty in 2021 and a dramatic increase in inequality.

Unless the international community reverses course, this divergence will persist, and may further intensify over the coming months and years. Global geopolitical tensions are rising, fueling uncertainty. The war in Ukraine has led to sharply rising commodity prices, further supply bottlenecks, and increased financial market volatility and downside economic risks, raising the specter of stagflation. The tightening of global financing conditions in the face of rising inflation will put more countries at risk of debt distress, further constraining their fiscal space and hampering economic growth. Today, 60 per cent of least developed and other low-income countries are already at high risk of, or in, debt distress. Vaccine inequity remains high—the number of vaccine doses per 100 people in least developed countries (LDCs) stood at just 23.9, against 147.4 in developed countries. Climate change will continue to exacerbate financing challenges, particularly in vulnerable countries.

The "great finance divide" has been a key driver of divergence. Developed countries borrowed record sums at ultra-low interest rates to support their economies and people through the pandemic, and to invest in recovery. Despite support by the international community, the pandemic response of poor countries has been limited by fiscal constraints. Tax revenues declined, reflecting downward trends in overall economic activity, and many countries were forced to reprioritize expenditure and cut spending in areas critical to the SDGs, such as education and public investment.

In crisis situations, access to long-term financing—international public finance and lending by development banks, as well as commercial financing—enables countries to respond and recover. Yet, for many countries, greater perceived and actual default risks are translating into higher borrowing costs in financial markets. Sovereign spreads and risk premia may seem removed from everyday life; but in the case of sovereign debt, they have a direct impact on people's lives. Sovereign borrowing in foreign currency has historically been expensive—it is associated with comparatively higher risk premia compared to other asset classes, such as corporate bonds or equities. Elevated sovereign borrowing costs also generally raise the cost of domestic private sector borrowing, further limiting investment in many developing countries.

Financing can stimulate growth—but only if it is used well. Governments' ability to borrow affordably is mainly dependent on national actions, including good governance, public financial management and institutional frameworks. Productive investments, including in resilient infrastructure, can improve debt sustainability in the long run: a growing economy helps to raise domestic tax and other revenue. A strengthened domestic financial sector can intermediate a growing savings pool into long-term financing for sustainable development. These are issues at the core of the Addis Ababa Action Agenda, but they also represent a medium- to long-term project.

In the face of a global crisis, near-time actions and additional international support are also needed. The international community has already taken significant steps to address the socioeconomic fallout from the COVID-19 pandemic. A record new allocation of special drawing rights (SDRs), provision of emergency financing at large scale and the G20 debt service suspension initiative (DSSI) have helped to finance the pandemic response and limit the number of countries in debt distress thus far. But additional efforts will be needed to close the large recovery gap, address the fallout from the war in Ukraine and rising food and energy prices in particular, and avoid scarring.

This *2022 Financing for Sustainable Development Report* of the Inter-agency Task Force lays out recommendations to enhance developing countries' access to financing for their crisis response, and for productive investments in recovery, climate action and the SDGs. Three key messages emerge from the Task Force's analysis and inform recommendations across the Addis Agenda action areas:

- **First, financing gaps and rising debt risks must be urgently addressed.** This includes raising resources from all sources of finance, as well as ensuring that these resources are spent well. Given short-term constraints, an increase in long-term sustainable public finance is needed. The international community also needs to step up efforts to address sovereign debt challenges;
- **Second, all financing flows must be aligned with sustainable development.** Recent crises have once again highlighted the interlinkages between the social, environmental and economic dimensions of development. They have underscored the need to address climate change and inequalities head on to preserve economic prospects. Growth can, in turn, help to finance environmental and social action. This implies, for example, adjusting fiscal policies, addressing greenwashing, increasing climate finance and also rethinking incentives in the international financial system;
- **Third, enhanced transparency and a more complete information ecosystem will strengthen the ability of countries to manage risks and use resources well and in line with sustainable development.** Better quality data is needed not only to enable monitoring and accountability, but also to support public and private sector planning and management, and financial integrity. Sovereign debt markets can also be more efficient with higher quality and more complete information.

Addressing the financing gap and fiscal pressures

Domestic actions are at the core of financing sustainable development. For additional financing to translate into long-term, positive outcomes, resources have to be used well. Integrated national financing frameworks (INFFs) can provide a framework to align financing policies and strategies with investment priorities and sustainable development strategies.

- **Good governance and the effective use of proceeds,** including strengthening institutions and the enabling environment, are preconditions for investments to deliver value for money. Improved public financial management and better procurement systems can prevent corruption, including in emergency spending programmes. Such actions mitigate country investment risks and can thus lower the cost of borrowing for both public and private actors;
- Developing **local financial systems** should remain a priority for developing countries and international partners. Deeper and broader local financial markets improve access to long-term financing for public and private actors, widen the investor base and reduce reliance on hard currency financing;
- Boosting **domestic revenue mobilization** requires medium-term planning and strong political will for implementation, while short- and medium-term actions can focus on tackling major sources of noncompliance, including illicit financial flows and broadening the tax base.

The official sector should increase long-term, sustainable finance and provide additional liquidity for countries in need.

- Official development assistance (ODA) providers must **scale up and meet ODA commitments,** especially to LDCs, with a greater volume of grants; as an immediate priority, the financing gap of the Access to COVID-19 Tools Accelerator **(ACT-Accelerator)** must be closed; additional support for Ukraine and refugees must not come at the expense of cross-border ODA flows to other countries in need;
- **Public development banks** have an important role to play in supporting long-term financing. They and other official providers should consider more systematic use of state-contingent clauses in their lending to provide breathing room to countries hit by shocks. The system of development banks should be strengthened by extending capacity and financial support to national institutions; multilateral and regional development banks can, in turn, benefit from national banks' detailed knowledge of local markets;
- **Blended finance** can reduce borrowing costs but needs to focus on where it can add value, with minimum concessionality to avoid diverting resources from social needs;
- **Official debt swaps**, building on regional initiatives, can create space for investments in recovery, the SDGs and climate action, particularly for countries that are fiscally constrained but do not have unsustainable debt burdens;
- **Rechanneling unused SDRs**: voluntary channeling of SDRs to countries most in need can strengthen the impact of the original allocation.

The international community also needs to address rising debt risks and the high cost of borrowing. The Common Framework for debt treatment beyond DSSI (the Common Framework) represents a meaningful step forward in the international debt architecture. But progress has been slow.

- **Strengthen the Common Framework**, including by taking timelier action; clarifying how comparability of treatment for commercial creditors will be implemented; expanding eligibility to highly indebted middle-income countries; and providing debt service suspension for the duration of negotiations;
- The international community should work towards a more **comprehensive solution to address sovereign debt challenges.**

Aligning all financing policies with SDG and climate priorities

Governments need to ensure that inequalities are reduced through use of the fiscal system.

- **Progressive tax systems** could directly reduce inequalities; expenditures should aim at reducing inequality, for example, through strengthened **social protection**;

- Gender equality can be advanced with both **gender-responsive budgeting** and **gender-responsive tax policies.**

The pandemic has emphasized the importance of financial, economic and trade systems in supporting health outcomes.

- Trade and investment policy actions are needed to address vaccine inequality and **improve access to medical products** and other technologies vital for combating the pandemic.

To address the climate crisis, there needs to be a just transition to a low-carbon world with greening of both public and private finance.

- **Pricing of carbon emissions** is a powerful tool alongside ending inefficient fossil fuel subsidies and using regulatory instruments to promote a sustainable economy;
- Countries should accelerate **investments in a sustainable energy transition**, especially given current high fossil fuel prices; development partners should align and target their support accordingly and can also use targeted blended finance instruments;
- To improve the positive impact of sustainable private investment, policymakers can promote **credible norms for sustainable investment products**, with greater disclosure and more rights for individual investors to express their sustainability preferences;
- Regulators need to adopt **globally consistent corporate sustainability reporting standards** for both privately owned and listed companies to allow policymakers, consumers and investors to integrate sustainability issues into their decisions.

Improving information ecosystems, data and transparency

Both public policy actors and private markets rely on data and access to information in their financing decision-making. However, gaps remain in data coverage and quality, particularly in regards to sustainability issues and related corporate reporting (see above), and stark divides persist between developed and developing countries. New technologies and digitalization present opportunities to close these gaps across the Addis Agenda. While enormous efforts and progress have been made, as catalogued in this report, some sectors of public and private finance have not yet effectively taken advantage of advances in technology.

- **Broadening the scope and improving the inclusivity of international sharing of tax information,** so that more countries are able to receive information that is suitable to their capacities and needs, will help to combat tax evasion and eliminate illicit financial flows;
- **Transparency in debt financing** is essential for effective debt management, debt crisis prevention and resolution. It has been a major focus of international support, but challenges remain;
- **Credit rating agencies** could provide valuable information to investors by making a clear distinction between model-based and discretionary components of sovereign ratings. **Long-term sovereign ratings could also be developed** to complement existing assessments, including by integrating climate transition pathways, as a core part of their methodologies;
- Developing measures of sustainable development and **data indicators beyond GDP could help to better inform policymaking** and direct actions towards sustainable development priorities.

About this report

The 2022 *Financing for Sustainable Development Report* of the Inter-agency Task Force begins with an assessment of the global macroeconomic context (chapter I). The thematic chapter (chapter II) explores the "great finance divide", the impacts of high borrowing costs for developing countries as well as recommended remedies. The remainder of the report (chapters III.A to III.G and IV) discusses progress in the seven action areas of the Addis Agenda, and advances in data. Each chapter gives updates on implementation and lays out the challenges and policy options at both the national and international levels—including in response to the current crisis and pandemic and climate risks. The report also responds to two specific requests included in the outcome of the 2021 Economic and Social Council Financing for Development Forum: it discusses the role of credit rating agencies (chapter II) and the potential use of the multidimensional vulnerability index (chapters III.C, III.E and IV).

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 and its online annex draw on their combined expertise, analysis and data. The major institutional stakeholders of the financing for development process—the World Bank Group, the International Monetary Fund, the World Trade Organization, the United Nations Conference on Trade and Development and the United Nations Development Programme— play a central role, jointly with the Financing for Sustainable Development Office of the United Nations Department of Economic and Social Affairs, which also serves as the coordinator of the Inter-agency Task Force and substantive editor of the report.

developmentfinance.un.org

9 789211 014525