

# **WORLD ECONOMIC AND SOCIAL SURVEY 2005:**

# **FINANCING FOR DEVELOPMENT**

*Presentation by:*

José Antonio Ocampo  
Under-Secretary-General for  
Economic and Social Affairs

# **THE MONTERREY CONSENSUS IS THE CURRENT FRAMEWORK FOR INTERNATIONAL COOPERATION FOR DEVELOPMENT**

- ❖ Comprehensive agenda
- ❖ Development cooperation as a partnership between developed and developing countries

## **COMPREHENSIVE AGENDA**

- ❖ Enhance the mobilization of domestic resources.
- ❖ Actively use trade as a instrument of development financing
- ❖ Encourage more stable flows of private external financing
- ❖ Achieve increased and more effective Official Development Financing
- ❖ Achieve debt sustainability
- ❖ Address systemic issues
- ❖ Bring South-South cooperation to new levels

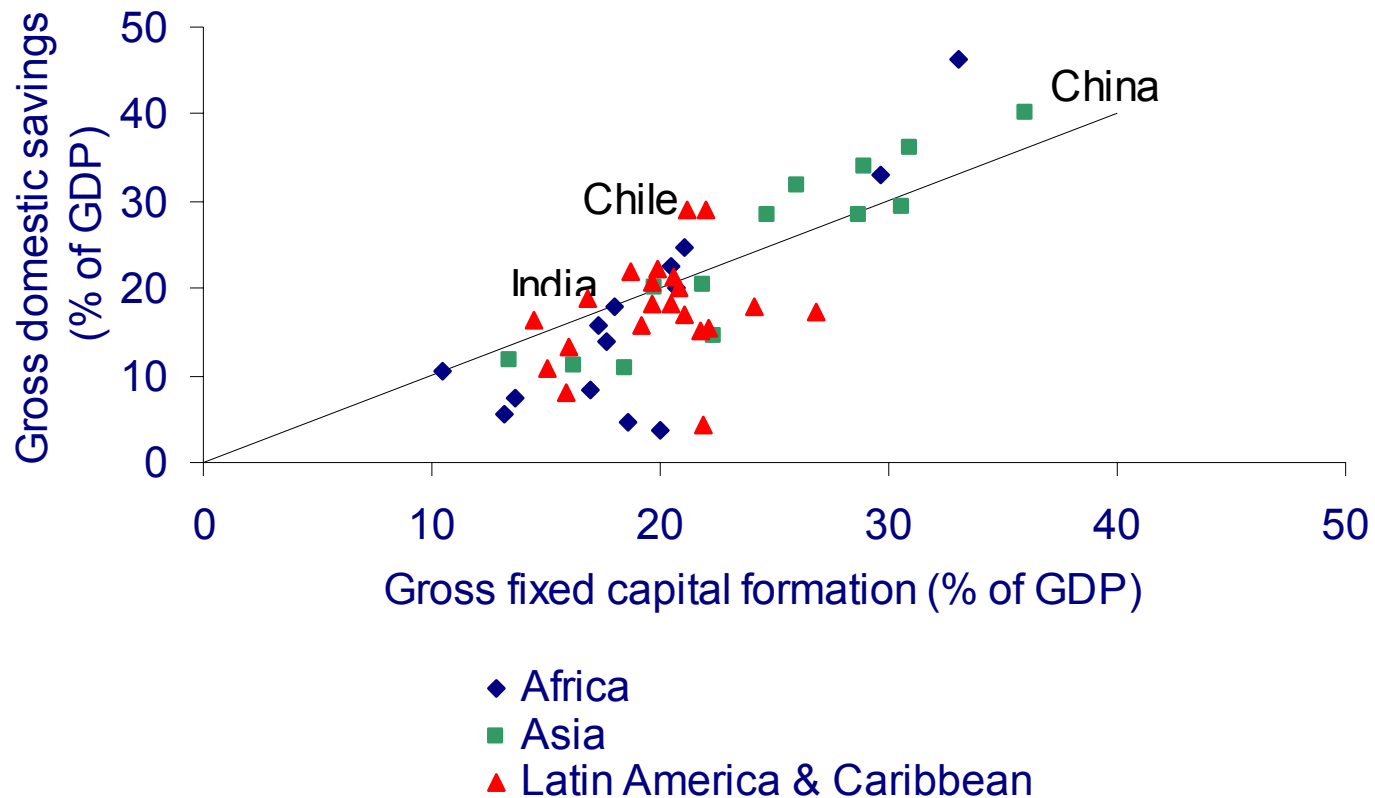
# **PRIORITY 1**

## **ENHANCE THE MOBILIZATION OF DOMESTIC RESOURCES**

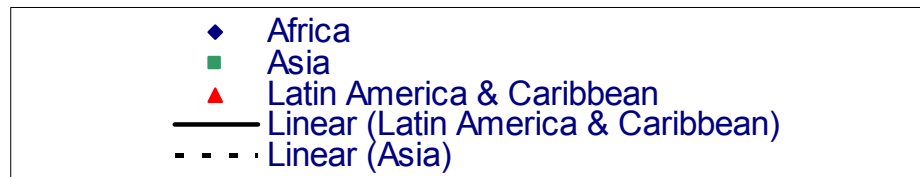
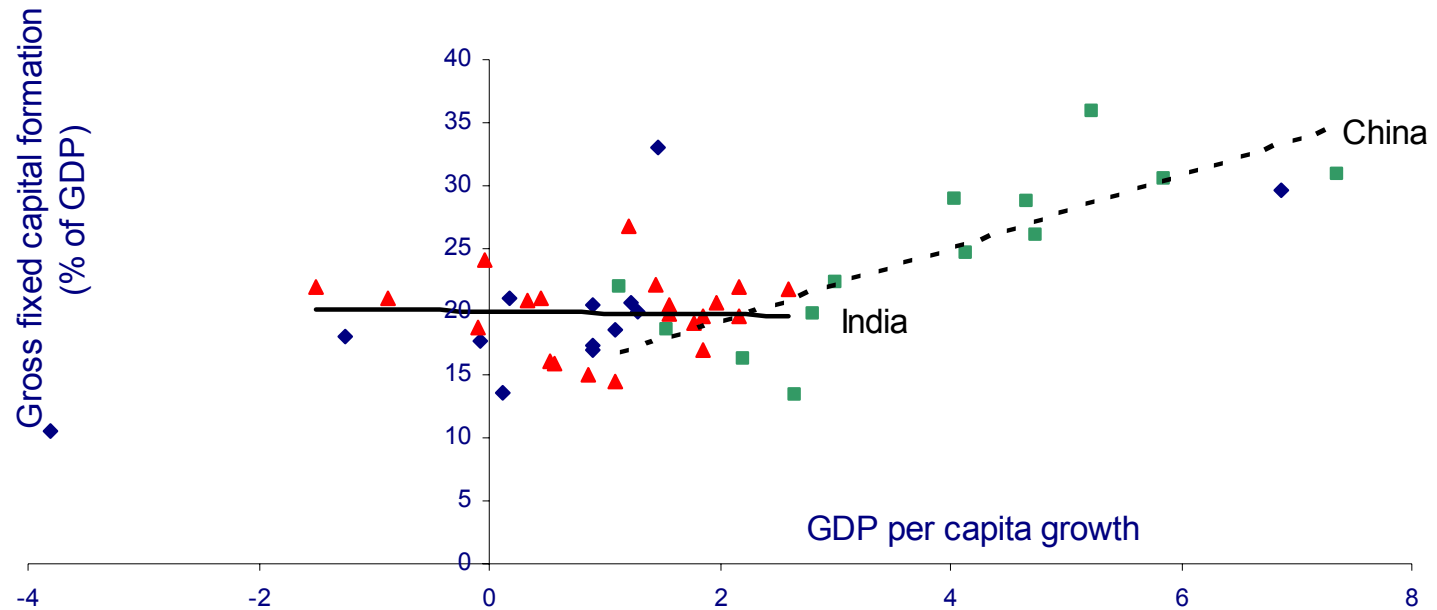
## **DOMESTIC RESOURCE MOBILIZATION**

- ❖ Despite capital mobility, investment and domestic savings are highly correlated.
- ❖ Rapid economic growth is associated with higher investment and domestic savings rates ...
- ❖ ... but this is only evident at high levels of growth ...
- ❖ ... and the causal link tends to go from growth to savings and investment.

# SAVINGS AND INVESTMENT, 1970-2003



# INVESTMENT AND GROWTH, 1970-2003



## **A GOOD INVESTMENT CLIMATE**

- ❖ Inclusive political systems
- ❖ Well-functioning legal systems
- ❖ Credible national development strategies that provide a clear sense of priorities...
- ❖ ... including explicit production sector strategies
- ❖ A broad view of macroeconomic stability
- ❖ Scope in many countries to simplify regulation without compromising broader social goals
- ❖ Balance between flexibility and stability in labor market regulation.

# DEEP AND INCLUSIVE FINANCIAL DEVELOPMENT

- ❖ Sound banking systems
- ❖ Domestic capital markets, in domestic currencies of developing countries.
- ❖ Three crucial issues
  - Long-term financing
  - Inclusive financing: equitable access to financial services
  - Prudential regulation and supervision, including counter-cyclical provisions
- ❖ Reformed public sector institutions can play a role.

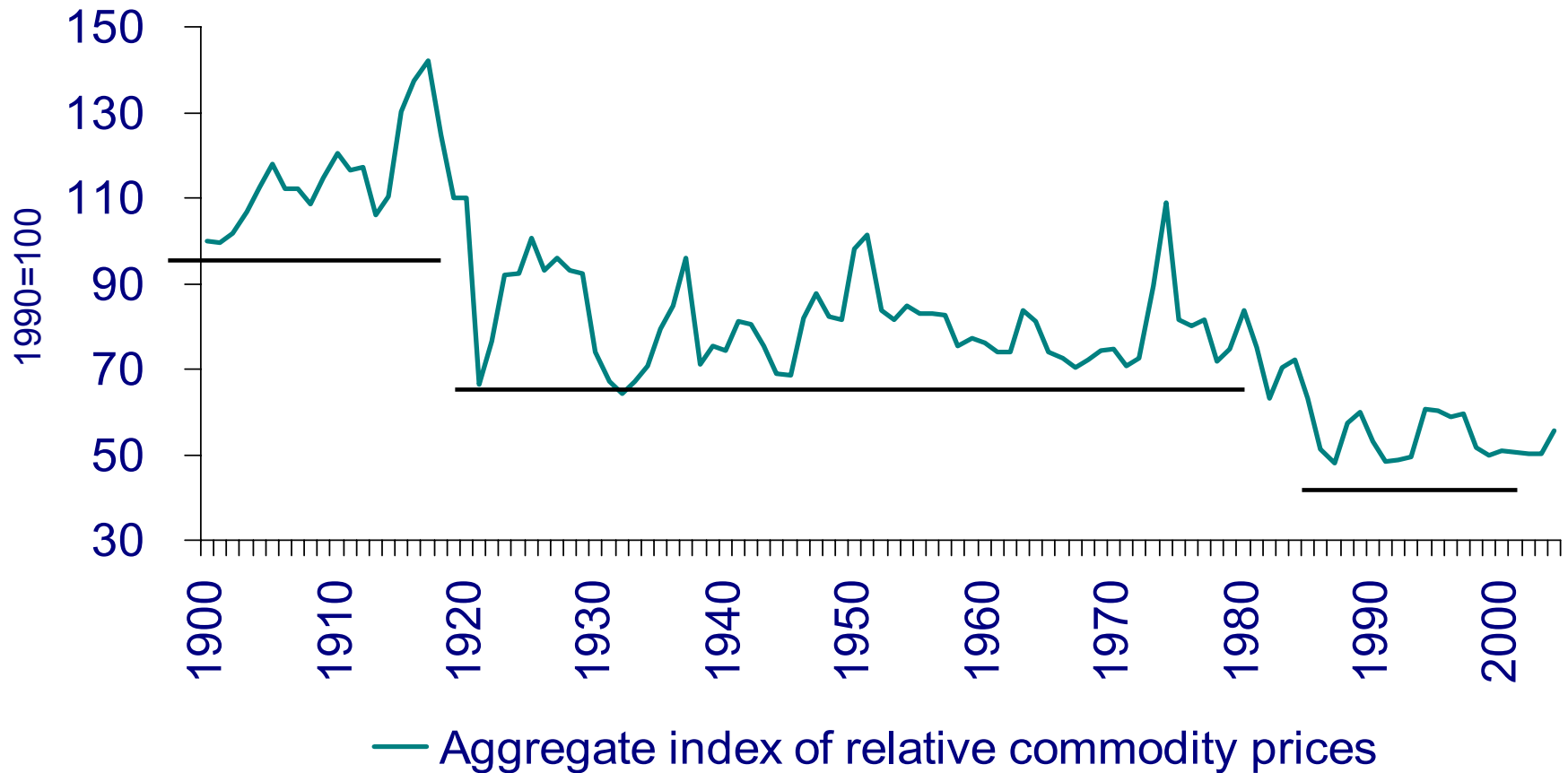
## **PRIORITY 2**

# **ACTIVELY USE TRADE AS AN INSTRUMENT OF DEVELOPMENT FINANCING**

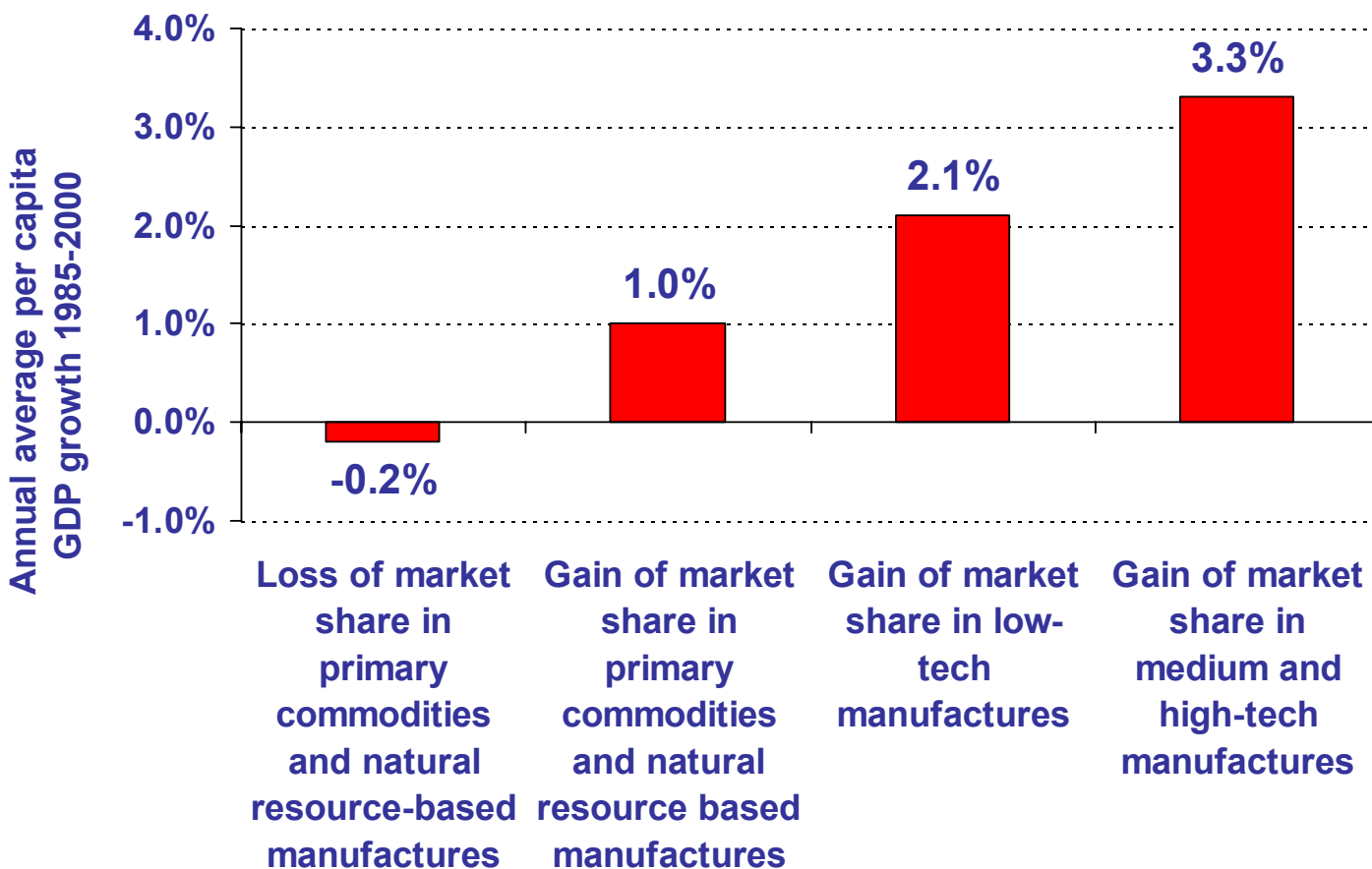
# TRADE AS AN ENGINE OF DEVELOPMENT

- ❖ Need for a universal, rule-based, open, non-discriminatory and equitable multilateral trading system
- ❖ Need to complete the Doha “development agenda” by 2006
- ❖ The pattern of specialization affects the ability to reap the rewards of an open trading system.
- ❖ Particular problem faced by commodity-dependent economies:
  - Non-dynamic segments of world trade
  - Long-term decline in real prices
  - Instruments to manage volatility: from traditional to market instruments
- ❖ Preferential agreements (“open regionalism”) may be a useful addition to multilateralism, but they are not a substitute for it.

# STEP-WISE HISTORICAL REDUCTION OF COMMODITY PRICES



# PATTERNS OF SPECIALIZATION AND GROWTH



## **PRIORITY 3**

# **ENCOURAGE MORE STABLE SOURCES OF PRIVATE EXTERNAL FINANCING**

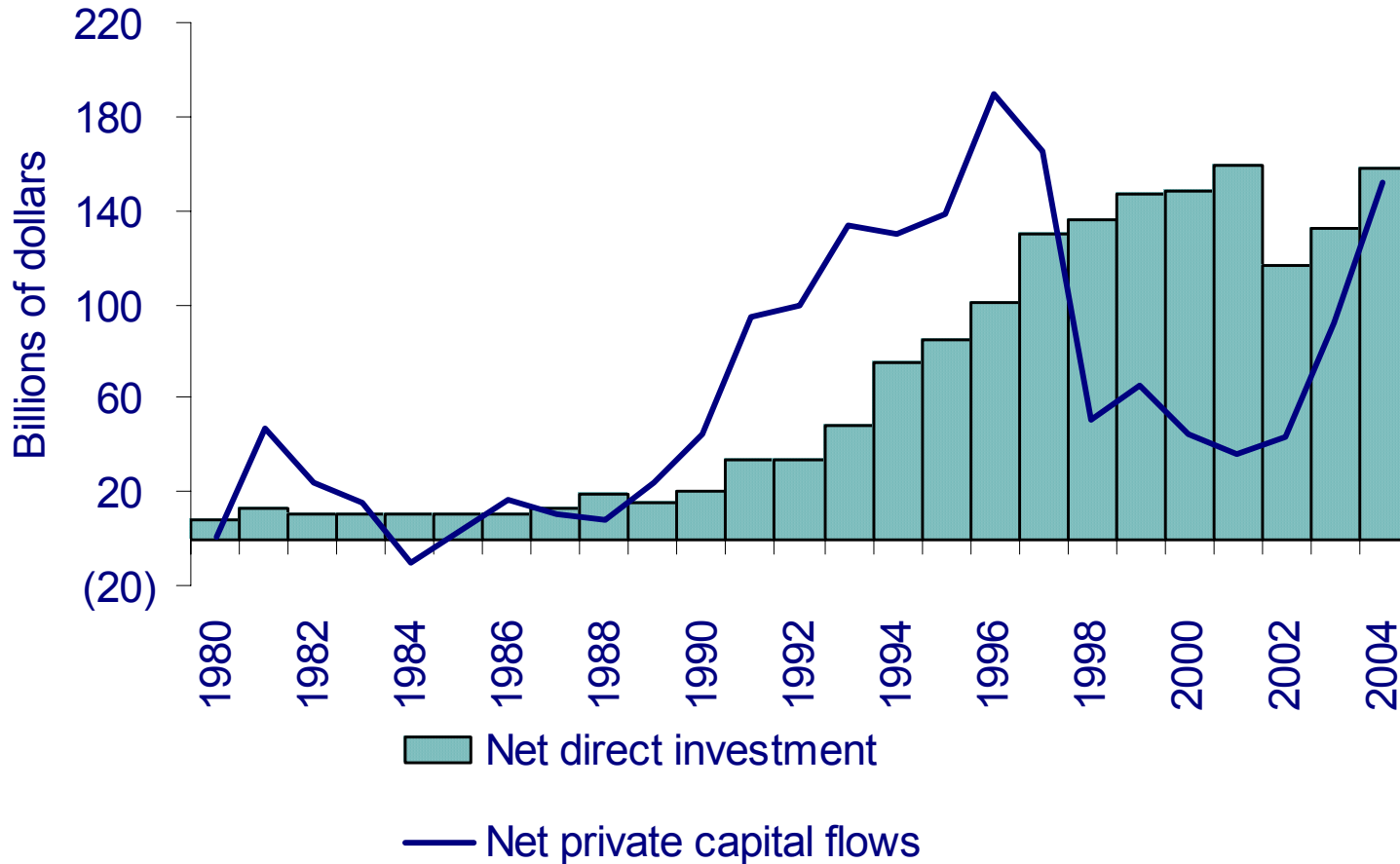
Private capital flows make a major contribution to development if:

- ❖ They flow from capital-abundant to capital-scarce countries
- ❖ Help developing countries smooth external shocks

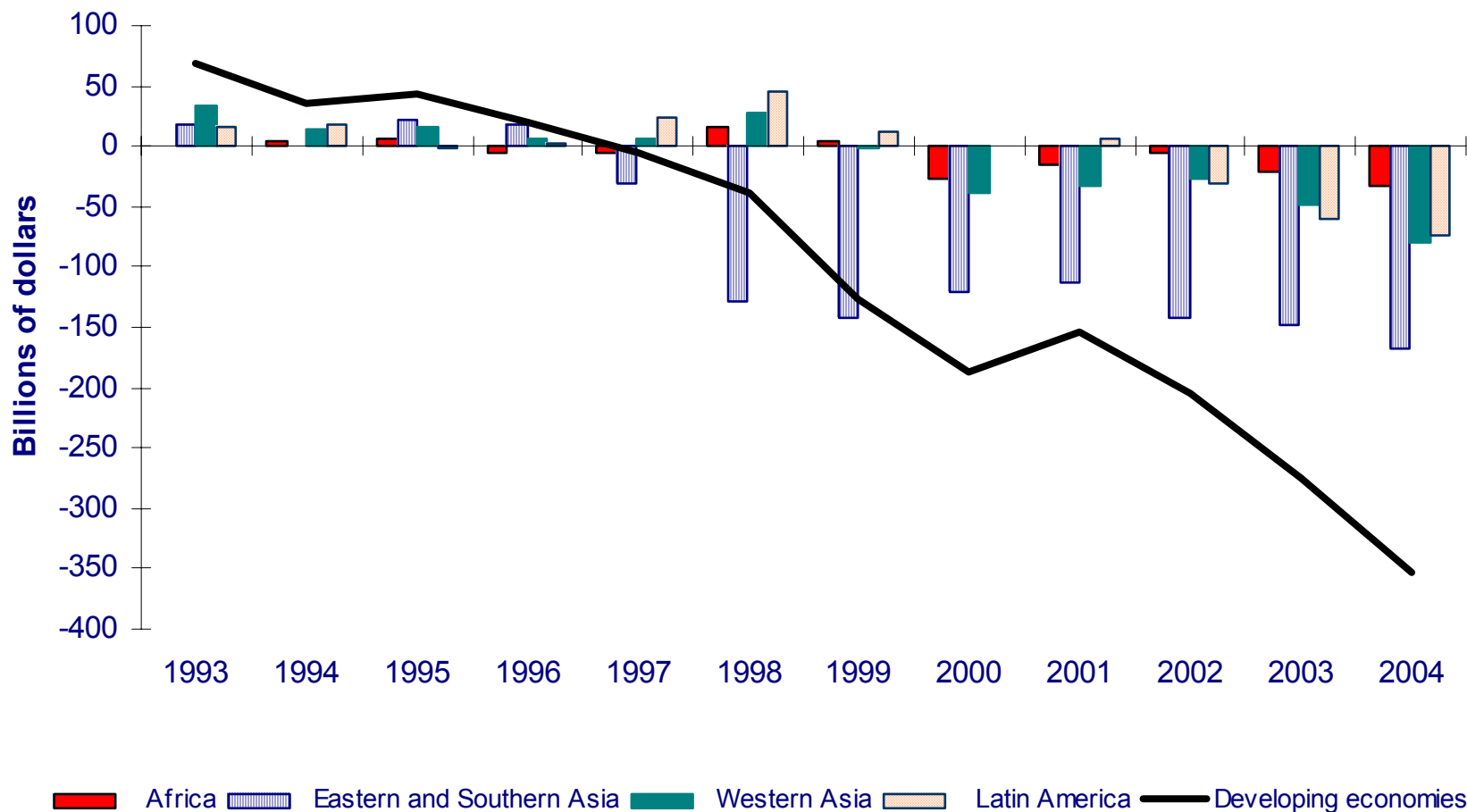
However,

- ❖ Many developing countries have no access to private external financing
- ❖ FDI has been a relatively stable source of external financing...
- ❖ ... but private financial flows have been volatile and reversible (with different flows subject to different patterns).
- ❖ Derivatives are efficient in pricing and distributing risks, but may increase volatility of private flows.
- ❖ Reversibility of private flows can lead to developmentally costly crises.
- ❖ There has been a major outflow of resources from developing to developed countries since the Asian crisis.

# AFTER THE COLLAPSE DURING THE ASIAN CRISIS, PRIVATE CAPITAL FLOWS TO DEVELOPING COUNTRIES HAVE RECOVERED...



# ...BUT DEVELOPING COUNTRIES CONTINUE TO TRANSFER RESOURCES TO INDUSTRIAL COUNTRIES.



## **REDUCE PRO-CYCLICAL FLOWS AND ENCOURAGE COUNTER-CYCLICAL FLOWS:**

- ❖ Commodity-linked and GDP-linked bonds
- ❖ Local currency financing, plus diversified portfolios of such bonds by private investment funds
- ❖ Supportive policies by official financial institutions:
  - Counter-cyclical risk evaluations by MDBs and export credit agencies
  - MDBs as “market makers” for the new instruments.
- ❖ Supportive domestic policies in developing countries:
  - Counter-cyclical banking regulation
  - Counter-cyclical macroeconomic policies
  - Possible role of capital account regulations
- ❖ Need for Basle II to be modified to reduce pro-cyclicality and/or compensated by counter-cyclical measures.

## **ATTRACTING PRIVATE FLOWS TO LOW-INCOME COUNTRIES**

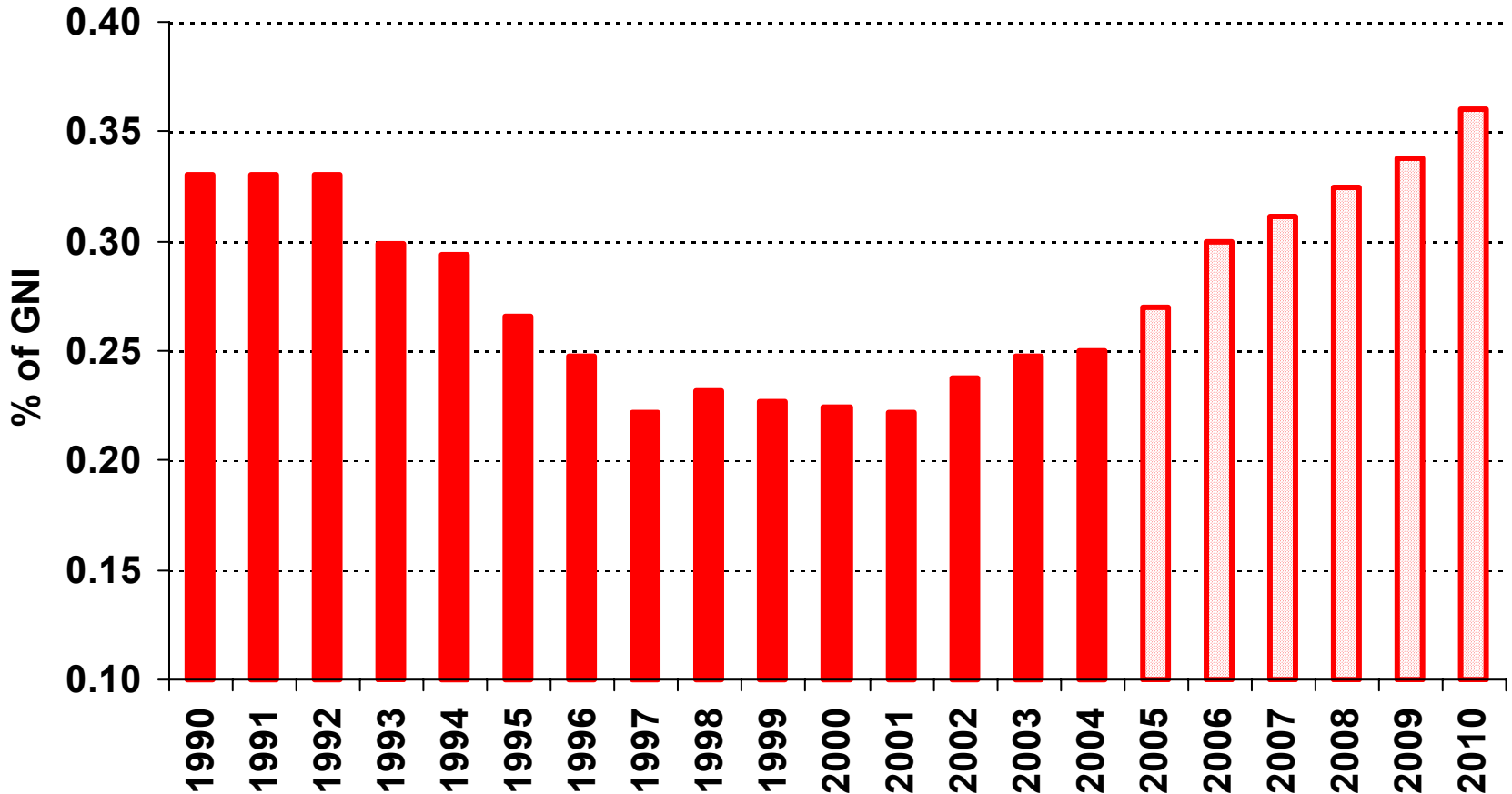
- ❖ Improved information flows for potential investors
- ❖ Market instruments to mitigate risks, plus broader use of multilateral instruments (insurance and guarantee schemes)
- ❖ Some “subsidy” scheme to such instruments based on donor funding to agencies offer such guarantees

## **PRIORITY 4**

# **ACHIEVE INCREASED AND MORE EFFECTIVE OFFICIAL DEVELOPMENT FINANCING**

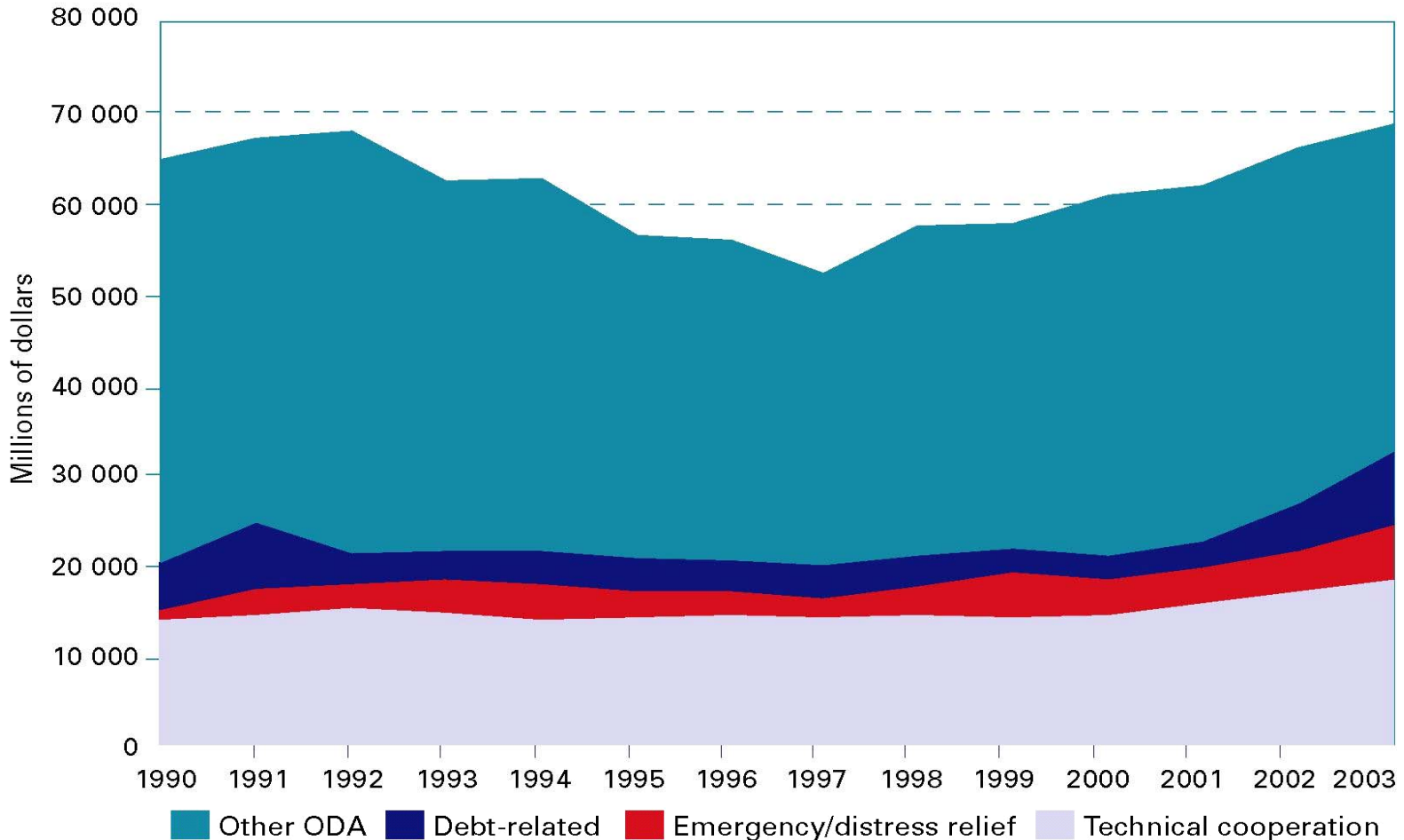
- ❖ There has been a partial recovery of ODA since Monterrey, particularly for LDCs
  
- ❖ But:
  - Most of the increase has been for debt relief, emergency aid and technical assistance...
  - ...plus the effects of exchange-rate and price changes
  - Concentration of aid in a few countries

# THERE HAS BEEN A RECOVERY OF ODA THAT IS EXPECTED TO CONTINUE...



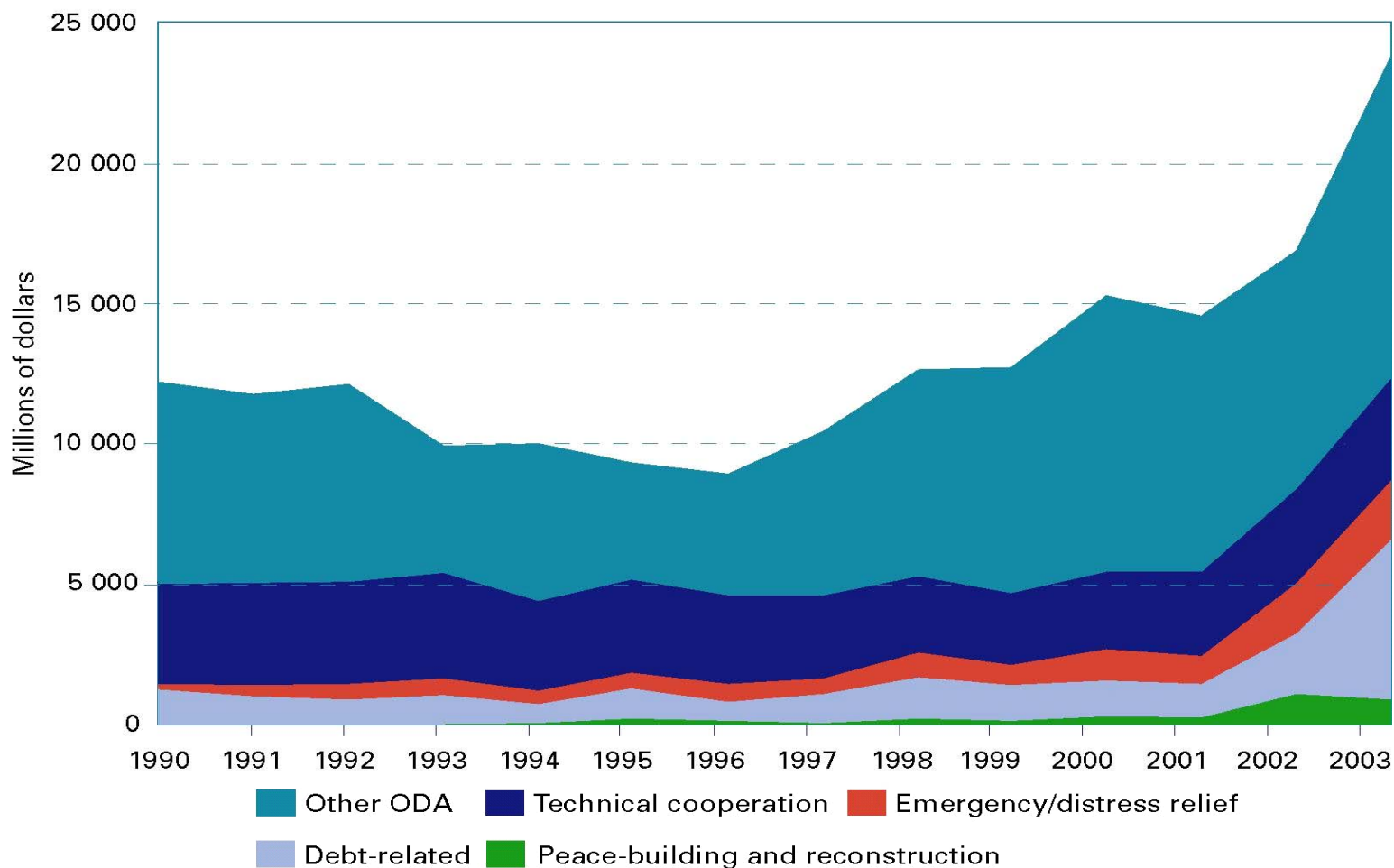
# ... BUT ODA CHANNELED THROUGH BUDGETS HAS NOT INCREASED...

**Composition of official development assistance, 1990-2003  
(corrected for inflation and exchange rates)**



# ... EVEN IN LDCs, WHERE THERE IS A STRONG POSITIVE TREND OF ODA

**Composition of official development assistance to least developed countries, 1990-2003**



## **PRINCIPLES OF AID EFFECTIVENESS (PARIS DECLARATION):**

- ❖ Ownership of development strategies by partner countries
- ❖ Alignment of donor support to those strategies
- ❖ Harmonization of donor actions
- ❖ Managing for results
- ❖ Mutual accountability of donors and partners

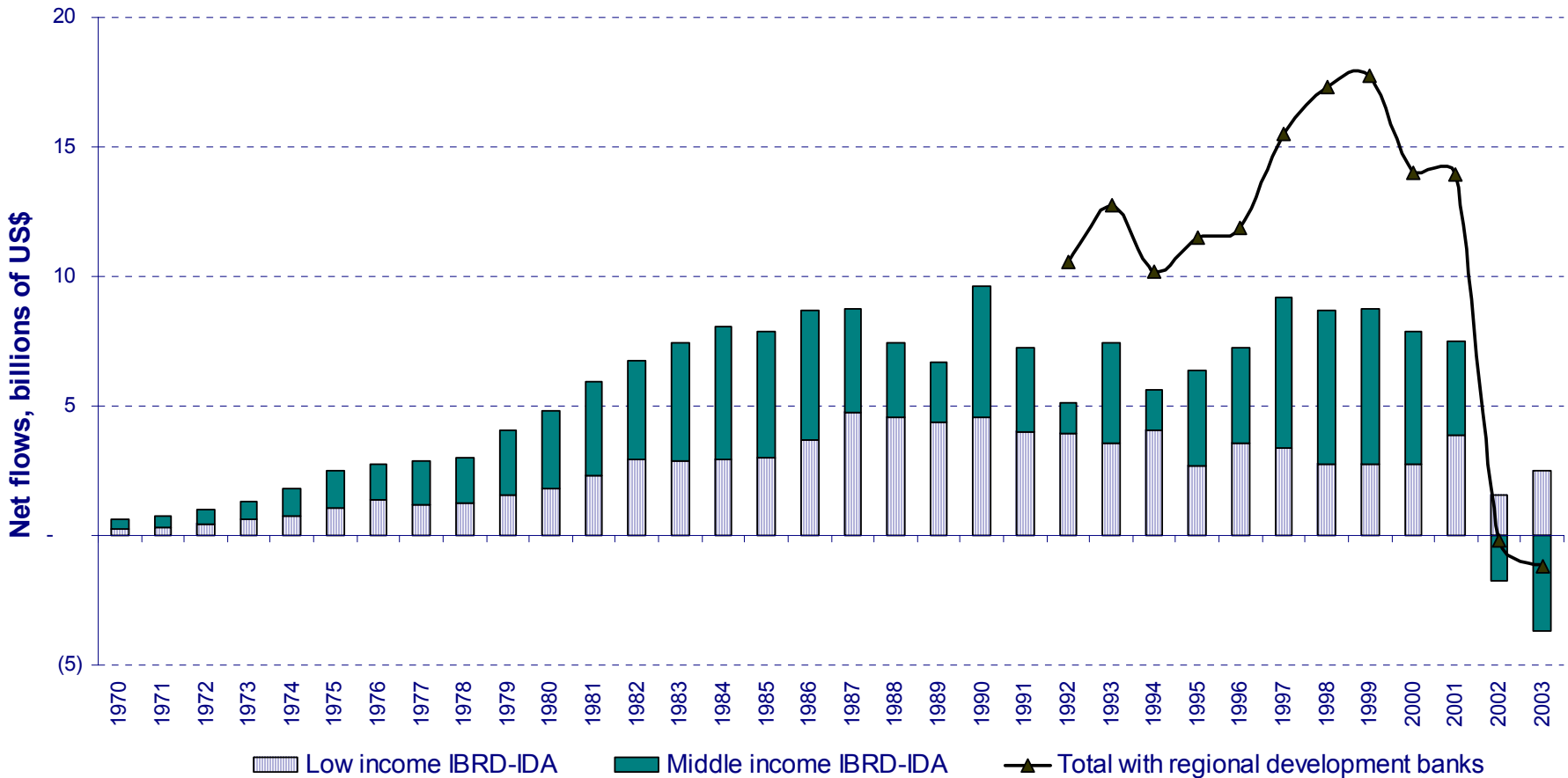
## **PRINCIPLES OF AID EFFECTIVENESS:**

- ❖ This means that an increasing share of aid should be channeled through the budgets of recipient countries, and used according to their priorities
- ❖ Need for agreement on targets for untying aid as an indicator of donor support
- ❖ We should add an additional principle:
  - Longer term commitments/more predictable aid

## THE ROLE OF MDBS

- ❖ Channel funds to low-income countries
- ❖ Counter-cyclical financing of middle-income countries
- ❖ Non-financial tasks:
  - Lending-associated technical assistance
  - Knowledge generation and brokering
  - Complementary provision of global and regional public goods. Emerging functions:
- ❖ Emerging functions:
  - Guarantees for public-private partnerships
  - Guarantees for bond issues after crises, and poor countries entering private capital markets.
  - “Market makers” for new financial instruments
- ❖ More active use of guarantees requires less risk adverse practices, and new accounting of guarantees
- ❖ Reduce costs of doing business with MDBs

# THE COUNTER-CYCLICAL CHARACTER OF MULTILATERAL DEVELOPMENT BANKS LENDING

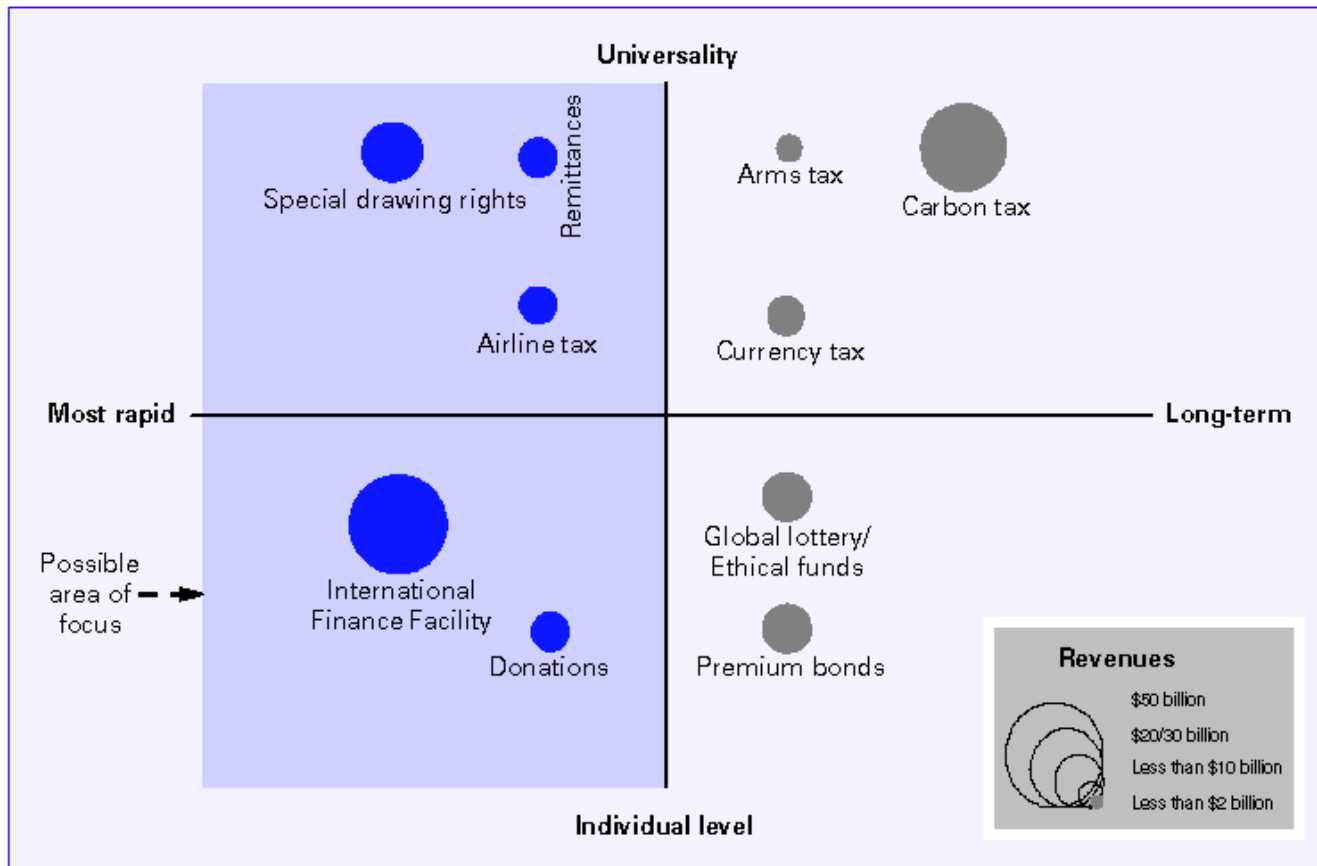


## **INNOVATIVE SOURCES OF FINANCING**

- ❖ International Finance Facility: Pilot project for immunization.
- ❖ Nationally applied but internationally coordinated taxes: Pilot solidarity contribution on airline tickets.
- ❖ Use of SDRs for development purposes
- ❖ Mechanisms to encourage private donations.
- ❖ Increase Development impact of remittances.
- ❖ Global lottery

# IT IS ESSENTIAL TO GUARANTEE THAT THE RESOURCES ARE ADDITIONAL TO EXISTING ODA COMMITMENTS

Map of main proposals on innovative sources of financing



## **PRIORITY 5**

# **ACHIEVE DEBT SUSTAINABILITY**

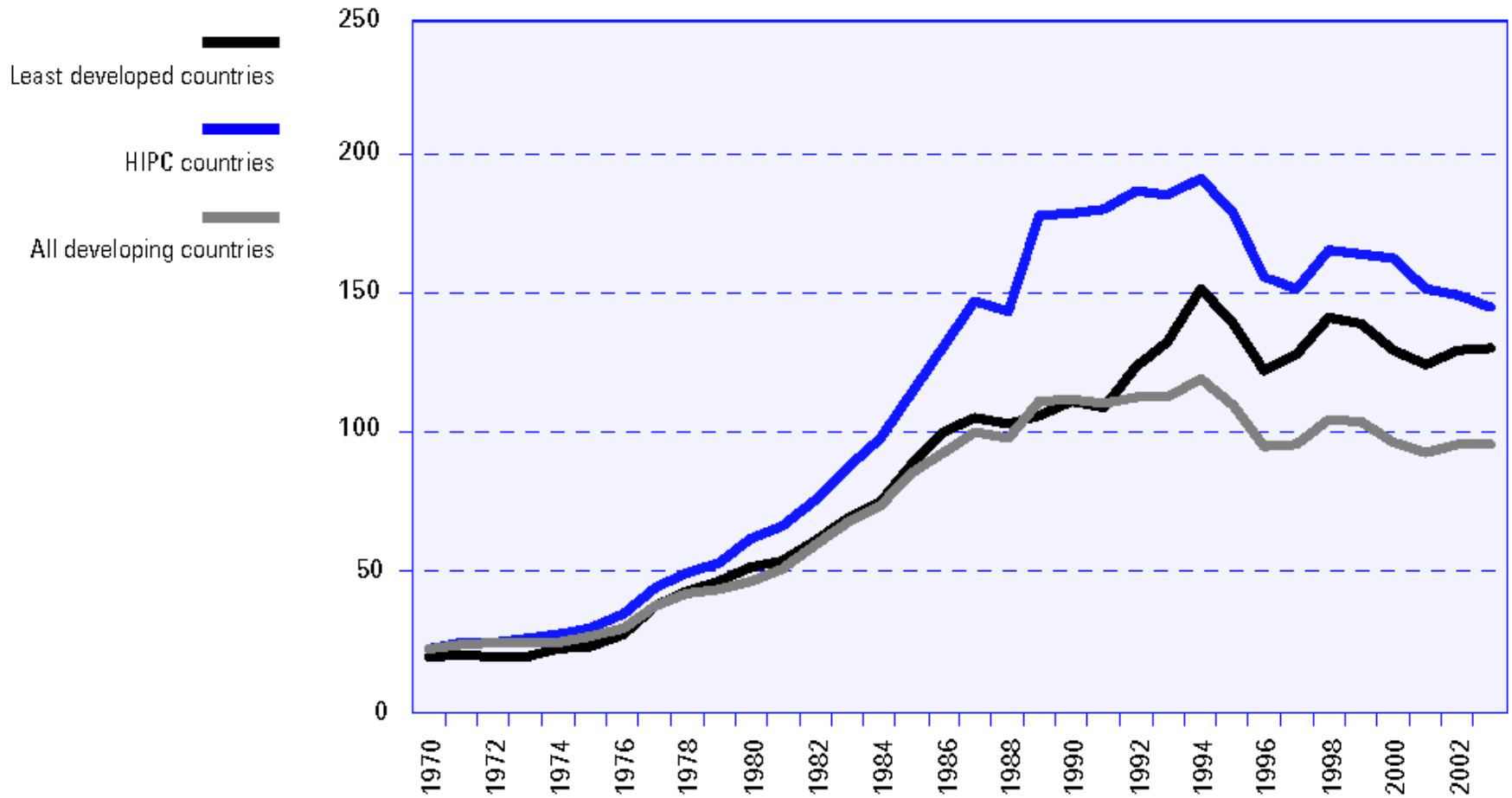
## **ACHIEVE DEBT SUSTAINABILITY**

- ❖ The postwar period has been characterized by repeated cycles of excessive borrowing by developing countries...
- ❖ ...followed by debt crises...
- ❖ ...and repeated renegotiations.

**DEBT OVERHANGS ARE VERY COSTLY  
IN TERMS OF DEVELOPMENT**

# ACHIEVE DEBT SUSTAINABILITY

Ratio of total debt to gross national income, 1970-2003



## **EXISTING DEBT INITIATIVES**

- ❖ Complete HIPC write-off.
- ❖ Paris Club: fully apply Evian approach, to avoid repeated renegotiations.
- ❖ Improved framework for overhang with private creditors: CACs, voluntary schemes. Continue discussion on mediation and arbitration mechanisms.

## DEBT SUSTAINABILITY

- ❖ Current frameworks focus on sustainability of debt dynamics
- ❖ ...but sustainability should also focus on capacity to achieve internationally agreed development objectives

### UN SECRETARY-GENERAL'S DEFINITION:

*Allow countries to meet MDGs by 2015, without accumulating unsustainable debt ratios*

# **PRIORITY 6**

## **ADDRESS SYSTEMIC ISSUES**

## **MAJOR SYSTEMIC ISSUES**

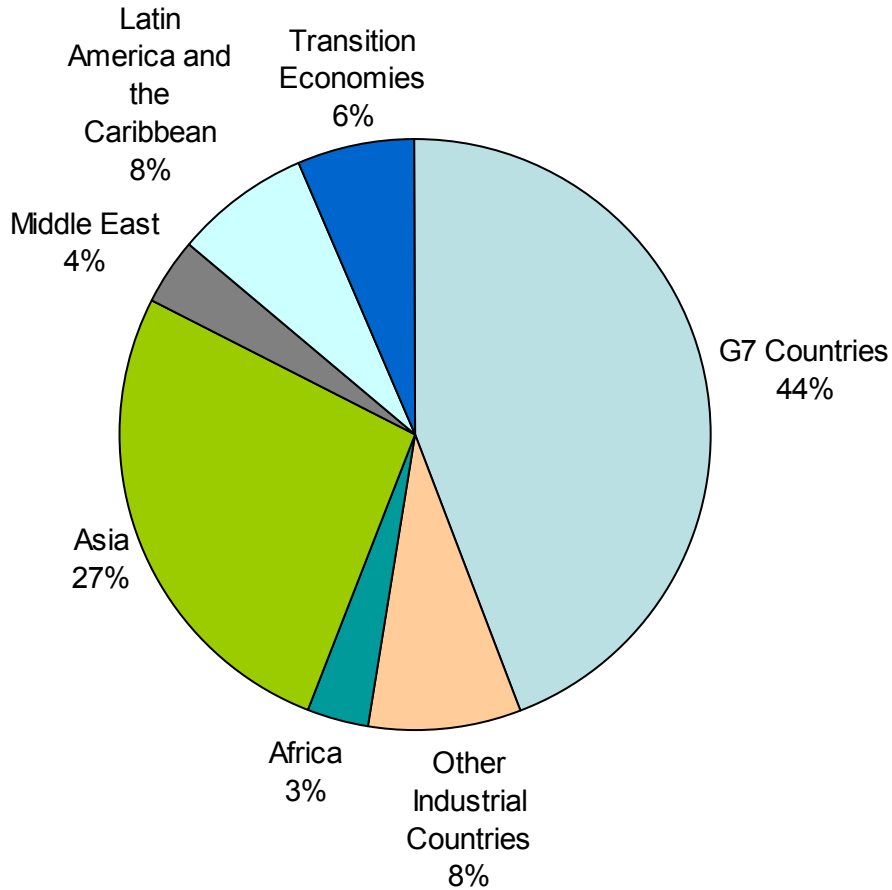
- ❖ Vulnerabilities associated to the structure of the international financial system:
  - Global macroeconomic imbalances.
  - Risk is increasingly concentrated in un- or under-regulated market segments.
  - Pro-cyclical pattern of capital flows to developing countries, and associated vulnerability to crises.
  
- ❖ Institutional design of the current international financial system

## **SOME IMPORTANT INSTITUTIONAL QUESTIONS**

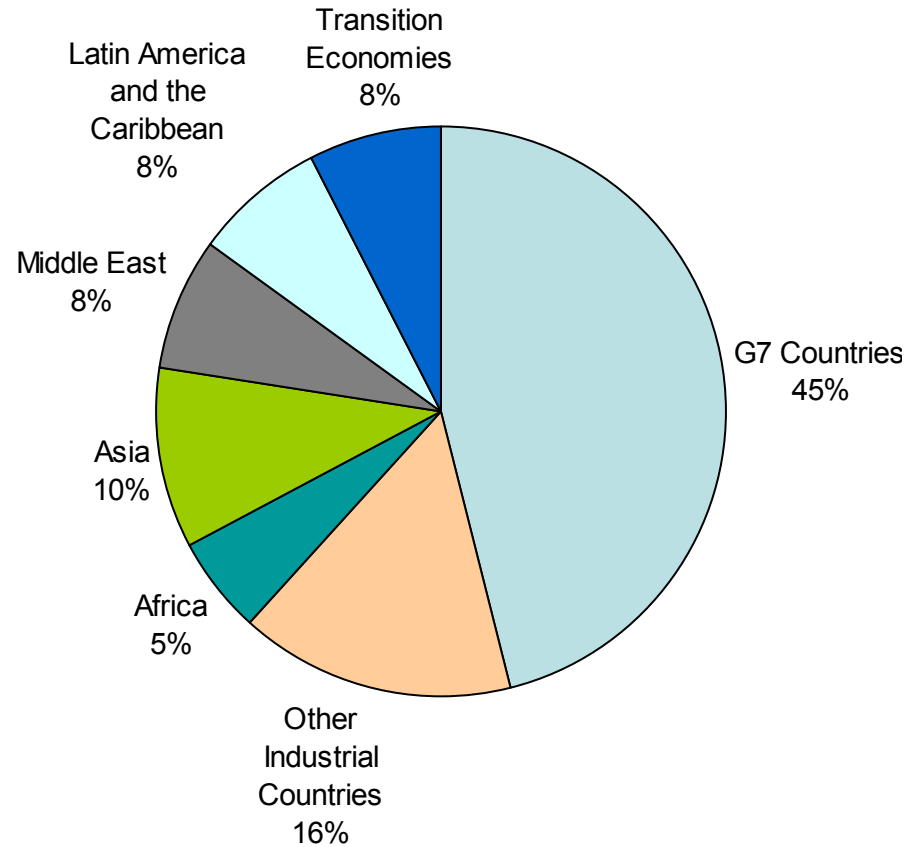
- ❖ Role of the IMF in ensuring consistency of macroeconomic policies of major countries
- ❖ Strict application of the principle of ownership of economic policies
- ❖ New for more automatic IMF facilities for countries with good fundamentals suffering from capital flow reversals
- ❖ Need for low/no conditionality IMF facility to fully compensate terms of trade shocks, especially for low-income countries
- ❖ More active use of SDRs, either as temporary financing mechanism, or as a way to have a more even distribution of seignorage powers
- ❖ Voice and participation of developing countries in decision making

# VOICE AND PARTICIPATION OF DEVELOPING COUNTRIES IN DECISION MAKING

**Share in GNI PPP**



**Share in IMF quotas**



## **PRIORITY 7**

**BRING SOUTH-SOUTH FINANCIAL  
COOPERATION TO NEW LEVELS**

# **BRING SOUTH-SOUTH FINANCIAL COOPERATION TO NEW LEVELS**

Rising role of the South:

- ❖ in technical cooperation
- ❖ growing South-South trade

Beyond that:

- ❖ Development banks totally owned by developing countries:
  - The Arab Institutions
  - The Andean Development Corporation
  - The Asian Bond Market Initiative
- ❖ Support during crises:
  - The Latin American Reserve Fund
  - Chiang Mai Initiative
- ❖ Macroeconomic policy consultation

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