How to ensure effective sustainable financing of international development

The world is committed to the development of low-income countries. Christine Lagarde considers the obstacles that must be overcome

Our focus today is on sustainability. Sustainable debt for sustainable growth—and, may I add, on a sustainable planet and for a sustainable future.

The challenge of attaining the SDGs

We are all committed to see low-income countries make decisive and lasting advances in development. This commitment is embodied in the Sustainable Development Goals, or SDGs—the noble trifecta of economic prosperity, social inclusion, and environmental sustainability. Attaining the SDGs is both an economic and ethical imperative.

Yet we face a steep uphill climb. Our work at the IMF has shown that many countries need to significantly scale up spending to meet the SDGs by 2030. The additional spending needs in vital areas such as health, education, and priority infrastructure represent as much as 15 percentage points of GDP on average in low-income developing countries—which is equivalent to about half a trillion US dollars in 2030. This is clearly a considerable challenge.

How can this be financed in a way that is sustainable? This is the key question. The first step begins at home—raising more domestic revenue, making spending more efficient, reducing corruption, and improving the business environment.

We believe that countries can raise as much as 5 percentage points of GDP in additional tax revenue—ambitious, but doable. But this alone will not be enough. Developing countries will also need support from the international community—from bilateral donors, international institutions, and the private sector.

On the latter: it is high time for the private sector to embrace a greater sense of social responsibility, focusing more on long-term development and less on short-term profit. Fortunately, we are seeing far greater interest in 'impact investing' and financial instruments that embrace environmental, social, and governance issues. This certainly bodes well for the SDGs.

The financing conundrum

We also need to talk about debt financing, which has become again an issue of concern. Let me drill down a little on this topic. On one level, of course, there is nothing wrong with borrowing for development—if it is done sustainably. Here, let me share some good news and some not-so-good news.

Over the coming decade, mobilizing financing to support the SDGs will be one of the most important challenges faced by the global community. But financing needs to be more sustainable than before

First, the good news. In recent years, low-income countries have been able to access more financing. This partly reflects relatively easy global financing conditions. More importantly, we have also seen a diverse group of official creditors step up to make funding available, and sometimes on a very significant scale in support of potentially transformative infrastructure investment.

China's Belt and Road Initiative has attracted considerable attention in this regard. The Asian Infrastructure Investment Bank (AIIB) has also emerged as an important source of financing, and the Islamic Development Bank's capital was more than tripled recently.

Now for the not-so-good news. Unfortunately, not all borrowers have managed this increased financing well, and others have been hit by significant economic shocks. The result has been a rapid rise in the median debt burden to 47 percent of GDP in 2018 for low-income developing countries. The rise has been particularly concentrated in commodity producers.

Forty-three percent of low-income developing countries are currently assessed at either high risk of debt distress or are already in debt distress, compared with 21 percent in 2013. So how can we get past the conundrum that countries need to spend more while their macroeconomic stability is in jeopardy?

International initiatives

As I survey the landscape, I do see a lot of efforts in the global community to find solutions that contain debt vulnerabilities.

Just to give some examples:

- The German Presidency of the G-20 initiated the Compact with Africa. It stressed the need for better public financial and macroeconomic management, as well as legal and regulatory frameworks to encourage private investment and strengthen borrowing countries' ability to better manage debt.

- China just announced a new framework for evaluating debt sustainability in Belt and Road recipients—closely aligned with the framework employed by the World Bank and the IMF. We welcome this initiative by an important official creditor.

- And Caribbean countries have been exploring ways to adapt their debt instruments to build resilience against shocks—with the support of the Paris Club, the World Bank, and the IMF.

These are all excellent examples of multilateralism at work, of global solidarity. We need to continue to push these initiatives forward together.

The role of borrowing countries

Of course, borrowing countries themselves have a role to play, first and foremost by raising the payoff from public investment. Moving from the lowest to the highest public investment efficiency quartile could double the impact of investment on output, and thereby better underpin debt sustainability.

Strengthening debt management will also be crucial. This can be quite tricky. As debt instruments get more complicated, debt management capacity needs to become more sophisticated. Yet today, only 40 percent of countries meet basic standards for debt recording, while just a third meet standards for reporting and monitoring of guarantees.

Technical assistance will be critical here. Many of you have made contributions to the World Bank-IMF Debt Management Trust Fund, to support this kind of capacity building, and I am extremely grateful for your support.

Backed by this Trust Fund, we will scale up our assistance over the next five years, with the aim to double it. Better debt management also leads to greater transparency. This is fundamental to sustainable financing.

The role of creditors

Let me now talk about the role of creditors, who have a vital role to play in encouraging greater transparency. As we have seen in Mozambique, private lenders can effectively facilitate hidden debt. Even for official creditors, non-disclosure agreements or complicated financing modalities can work against transparency.

I therefore welcome the work being done by the Institute of International Finance (IIF) on *Principles for Debt Transparency* of private creditors. I also welcome the G-20's self-assessment relative to its operational guidelines for sustainable financing. I encourage all G-20 members to participate. It is vitally important to push ahead with further reforms. The new creditor and instrument landscape is making it much harder to help countries restructure their debt.

Recent cases, such as the Republic of Congo and The Gambia, showed that restructurings can be drawn out, in part because we cannot rely on established creditor coordination mechanisms. And there is no one-size-fits-all solution here. In each of these cases, there was a different set of creditors. There is no one creditor to single out; it is a deeper and broader problem. Yet there are potential solutions on the table.

The role of the Paris Club

Most importantly, the Paris Club can play an important role in coordinating debt resolution because it incorporates best practices and has a wide membership—recently expanded to include Korea and Brazil. Wider membership of the Paris Club, including new official and plurilateral creditors, could help secure more rapid and coordinated debt resolutions.

Short of that, any debt restructuring efforts involving non-members would do well to closely follow the tested rules that Paris Club members have used for many years.

Conclusion

Let me conclude by mentioning the role of the IMF and the World Bank in all of this. Our two institutions have been collaborating closely on a detailed multi-pronged work program to address debt vulnerabilities. This includes strengthening debt analytics to help lenders and borrowers better understand risks. It also includes improving the quality, comprehensiveness, and transparency of debt data; and strengthening countries' capacity to manage debt.

Over the coming decade, mobilizing financing to support the SDGs will be one of the most important challenges faced by the global community. But financing needs to be more sustainable than before.

We look forward to working with the international community to develop and implement the ideas to resolve these issues, and welcome today's forum to help advance our efforts.

After all, it is about the flourishing of all people in a way that respects the limits of nature. What can be more important? We have identified and acknowledged the challenge, now we must act together to deliver. ■

Christine Lagarde is Managing Director of the International Monetary Fund

This article is based on a speech delivered at the Paris Forum, May 7, 2019