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Follow-up to and implementation of the outcome of the 2002 International Conference on Financing for Development and the 2008 Review Conference

Follow-up to and implementation of the Monterrey Consensus and Doha Declaration on Financing for Development

Report of the Secretary-General**

Summary

Pursuant to General Assembly resolution 63/208, the present report describes recent developments in relation to the review process on financing for development and the implementation of the Monterrey Consensus. The main developments are presented under each of the six thematic chapter headings of the Monterrey Consensus document: mobilizing domestic financial resources for development; mobilizing international resources for development: foreign direct investment and other private flows; international trade as an engine for development; increasing international financial and technical cooperation for development; external debt; and addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development. Other recent developments are presented in section VII, entitled "Staying engaged".

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** The report has been prepared in close consultation with staff from the major institutional stakeholders involved in the financing for development process. Responsibility for its contents, however, rests solely with the United Nations Secretariat.

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I. Mobilizing domestic financial resources for development

Impact of the crisis on developing economies

1. The global financial and economic crisis, which originated in developed countries, has become a development emergency of global reach, putting at risk the very survival of poor people.[1] The world is entering a period of markedly slower economic growth[2] which will have a strong negative impact on developing countries, which are affected by a collapse in world trade, a sharp reversal in private capital inflows, falling commodity prices and a slowdown in remittance flows to poorer countries, as well as the loss of income and employment due to the contraction of global economic activity.[3] As if this were not enough, there is a risk that existing commitments of official development assistance (ODA) may not materialize, or that aid levels may even be scaled down owing to concomitant fiscal pressures on industrialized countries. As a result, developing countries will have fewer resources to undertake critical investments in, inter alia, infrastructure, human development and social safety nets, and building trade and productive capacities. More immediately, Governments will also have less space in which to undertake fiscal expansionary measures to counter the economic downturn.

2. Developing countries have been affected by the crisis to varying degrees, depending on their economic structure, their integration into the global economy and their vulnerability to shocks. The impact of the crisis will also be shaped by the ability of Governments to implement countervailing macroeconomic policies and social programmes. This may influence how different groups within societies, including the poorest and marginalized communities, are affected. The poorest countries are especially vulnerable in that they are heavily dependent on external finance (notably aid) and trade, they rely on a few commodities for their foreign exchange earnings and their social protection systems are unable to respond fully to the crisis.[4] The crisis is having a negative impact on economic and social prospects in developing countries, even in those which have made significant improvements in macroeconomic management and fundamentals in recent years.

3. Few developing countries are in a position to undertake significant countercyclical spending. While most of the global stimulus is correctly being undertaken by developed countries, a concentration of this spending in the more industrialized regions could further skew the distribution of global income. There has as yet been no explicit coordination of the fiscal measures being undertaken by Governments. For developing countries to play their part in boosting demand, it is important that resources be transferred to them. The members of the Group of Twenty recognized this during their meeting in London in April 2009, although the resources they agreed to transfer are insufficient to enable developing countries to

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[1] See World Bank, *Global Monitoring Report 2009: A Development Emergency* (Washington, D.C., 2009).

[2] World Bank, Global Development Finance database, June 2009.

[3] See United Nations, *World Economic Situation and Prospects 2009*, Update as of mid-2009. Available from http://www.un.org/esa/policy/wess/wesp2009files/wesp09update.pdf.

[4] Report of the Secretary-General on the world financial and economic crisis and its impact on development, to be submitted to the General Assembly at its present session.

ensure a more balanced global stimulus aligned with their long-term development needs.[5]

4. This issue of how developing countries could counter the effects of the crisis, and the roles of the United Nations and the international financial institutions in this area, was a theme in most interventions at the special high-level meeting of the Economic and Social Council with the Bretton Woods institutions, the World Trade Organization and the United Nations Conference on Trade and Development, held in New York on 27 April 2009. Many made the point that greater supplementary funding should be made available by the international community, including through the International Monetary Fund (IMF) for countercyclical stimulus measures in such countries. Procyclical measures involving reductions in fiscal spending should be avoided. Procyclical adjustments by individual countries induced by the lack of required resources would be in direct conflict with the agreed global effort to overcome the collapse in private consumption and investment afflicting all countries. As requested at the meeting of the Group of Twenty in London, IMF and other lending institutions must demonstrate greater flexibility in their lending practices.

Effect on poverty and sustainable development

5. The current global crisis will lead to rising poverty in many developing countries through a reduction in employment and income opportunities. The precise overall impact of the crisis on global poverty is difficult to estimate since the problems have yet to bottom out, countries are affected to varying degrees and their capacity to respond and provide social protection also varies significantly. According to International Labour Organization (ILO) estimates, at least another 50 million people worldwide could become unemployed,[6] many owing to the closure of export-oriented industries. In addition to unemployment, there will also be increased underemployment as, in the absence of adequate social protection, many people who have lost their jobs move to working in the informal sector. According to estimates by the Department of Economic and Social Affairs of the United Nations Secretariat, a significant drop in per capita income growth in 2009 would significantly slow progress towards poverty reduction. Between 73 and 103 million more people are estimated to remain poor or fall into poverty as a result of the crisis, with all developing regions being affected.[7] Indeed, the poverty impact of the crisis may be even greater than these figures suggest once its distributional consequences are factored in. Inequality is likely to rise as lower-income workers are more likely to face unemployment or cuts in wages. At the same time, possible cutbacks in social expenditure as a result of the budgetary pressures brought about by the crisis would disproportionately affect the poorest segments of the population.[8] Finally, declining remittances may also contribute to rising poverty, especially in those countries for which remittance flows are large relative to gross domestic product (GDP).

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[5] United Nations, *World Economic Situation and Prospects 2009*, Update.

[6] ILO, *Global Employment Trends, January 2009* (Geneva, International Labour Office, 2009).

[7] See United Nations, *World Economic Situation and Prospects 2009*, Update.

[8] Note by the Secretariat on the current global crises and their impact on development (E/CN.5/2009/CRP.2). Available from http://unstats.un.org/unsd.

6. It is clear that the global financial and economic crisis will have long-term developmental implications for developing countries. It has already seriously set back the development efforts of the poorer countries and increased the magnitude of the challenges confronting them. Even before the crisis, many countries were having difficulties, exacerbated by the food and volatile energy prices, in staying on track to meet most of the Millennium Development Goals. Rising poverty and lower government revenue to finance social expenditures will further set back their efforts to achieve the Goals. The precise impact of the crisis on the achievement of the Goals will vary from country to country, as will the cost of the additional efforts needed to bring countries back on track towards meeting the targets.

7. It is therefore critically important that attention be directed to protecting the poor by the sustainment of employment and livelihoods and targeted social spending, including expanded safety nets. More than at any other time, countries should align their fiscal stimulus programmes with longer-term development objectives in areas such as infrastructure, education and health. In addition, funds can also be targeted towards microenterprises and small and medium-size enterprises which play an important role in helping to generate employment and lifting individuals and communities out of poverty. According to the World Bank, a number of initiatives are under way to support the provision of finance to small and medium-size enterprises, including through the use of public guarantees to private financial institutions.[9]

8. The crisis also presents a resource mobilization challenge in global efforts to address climate change. Adaptation to climate change needs to be included in development plans, including investment programmes, in all countries. Moreover, the investment requirements of adaptation may be significant in relation to government budgets for countries that are especially vulnerable to the effects of climate change. The overall cost of adaptation to climate change risks in the developing world is estimated to be in the range of $4 billion to $37 billion per year. It is imperative that the increasing challenge of financing climate change adaptation and mitigation be addressed by the international community during the fifteenth session of the Conference of the Parties to the United Nations Framework Convention on Climate Change, to be held in Copenhagen in December 2009.

Broader policy lessons

9. While the immediate priority for all countries is to hasten an economic recovery, it is also important for developing countries to distil longer-term lessons learned from the crisis in respect of financial sector development and development strategies. The given wisdom relating to financial sector development has tended to emphasize the importance of greater diversification and competition, a balance between debt and equity forms of finance, and better enforcement of contracts and regulations. Recent experience, however, suggests that it is equally necessary for relevant national authorities to adopt a regulatory approach that can serve to protect financial systems from crises while preserving their ability to conduct efficiently their core activities. In this context, various proposals have been given serious

[9] "Swimming against the tide: how developing countries are coping with the global crisis", background paper prepared by World Bank staff for the Meeting of Finance Ministers and Central Bank Governors of the Group of Twenty, Horsham, United Kingdom of Great Britain and Northern Ireland, 13 and 14 March 2009.

consideration in both national and international policy circles, including measures that encourage countercyclical lending by financial institutions and stronger oversight by policymakers, at the national and international levels, of financial market activities. In addition, within the framework of multilateral cooperation, the enhancement of regional cooperation and dialogue, the institution of regional economic and financial monitoring mechanisms or the establishment of reserve funds and arrangements for effective currency swaps in times of crisis can also help to reduce the impact of abrupt changes in private capital flows.

10. The role of countercyclical policy towards achieving macroeconomic stability in a broad sense, which includes not only price stability and sound fiscal policies but also business cycles of smaller size, sustainably competitive exchange rates, sound external debt portfolios and healthy domestic financial systems and private sector balance sheets (see A/59/800, para. 21), has garnered much attention. Countries should consider expanding the range of policy tools to include the establishment of countercyclical funds, selective and targeted public spending and the enhanced use of tax systems to manage booms and busts.

11. Many of these issues were explored during deliberations in the run-up to the Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus, held in Doha from 29 November to 2 December 2008. With respect to domestic resource mobilization, an important new commitment was made by Governments on the issue of taxation. Strengthened international tax cooperation should form a critical element of a more effective global system of financial regulation. In the Doha Declaration on Financing for Development,[10] Governments specifically requested the Economic and Social Council to examine the strengthening of existing institutional arrangements, including the Committee of Experts on International Cooperation in Tax Matters.

II. Mobilizing international resources for development: foreign direct investment and other private flows

12. Private capital flows to developing countries have dropped sharply in the wake of the global financial crisis. Net private capital inflows to developing economies have declined, from a peak of around $700 billion registered in 2007 to less than $400 billion in 2009. In tandem with this trend, there has been a sharp rise in the costs of external financing for developing countries, illustrated by the huge increase in the risk premium on lending to emerging economies from 250 to about 800 basis points during the third quarter of 2008. Moreover, the increase in risk spreads has been uniform across developing regions, confirming the existence of contagion and a general aversion to investment in global financial markets.

13. The decline in private capital flows encompasses all developing regions, with the most substantial fall taking place in emerging Europe. This trend will also have an impact on parts of Africa since the continent has also been relying increasingly on private capital inflows, although the flows are small in global terms. Given the size of most domestic capital markets in Africa, even a small decline in these flows could have a sizeable impact on the prices of securities. There were no international bond issues by African countries in 2008 as a consequence of the global credit

[10] General Assembly resolution 63/239, annex.

crunch. Some countries, notably Kenya, Nigeria, the United Republic of Tanzania and Uganda, have had to cancel plans to raise funds in international capital markets for infrastructure projects.

14. The sharp fall in foreign direct investment (FDI), which contracted by about 15 per cent in 2008, has been driven by a marked weakening in corporate profits and falling global capital spending. Of most concern is that falling FDI flows could also have implications for infrastructure projects which are critical for longer-term growth. A significant infrastructure financing gap has already emerged in many developing countries, with longer-term needs far exceeding the amounts that are currently being invested. According to World Bank estimates, developing countries would at present need to invest an estimated 7-9 per cent of their GDP in infrastructure annually if they are to achieve growth and poverty reduction goals, in comparison with the 3-4 per cent that they currently invest. Investments in public and private infrastructure projects tend to decline substantially during and immediately after economic crises. For example, infrastructure investment dropped substantially after the financial crisis of the late 1990s in East Asia and had not recovered to pre-crisis levels by 2007. According to the World Bank's Public-Private Infrastructure Advisory Facility, the value of public-private infrastructure projects that reached financial closure between August and November 2008 was down 40 per cent compared to one year earlier.

15. Looking beyond the circumstances and impact of the present crisis, attracting adequate amounts of private finance into infrastructure projects will continue to be a challenge in many countries owing to concerns among private investors about regulatory risk, credit risk and currency risks. While public provision of infrastructure remains fundamental, rising financing needs and fiscal pressures have led many countries to seek private participation in the provision and financing of infrastructure projects. Through measures to mitigate some of the risks facing private investors, multilateral organizations and Governments can try to attract a greater volume of private capital into infrastructure projects. As suggested in a recent study issued by the United Nations Conference on Trade and Development (UNCTAD),[11] current risk mitigation programmes are not sufficiently tailored to circumstances in low-income countries.

16. Risk mitigation and capacity-building, as well as measures to improve the enabling business environment, can also serve to expand the distribution of FDI to a greater number of developing countries and to sectors such as human resources, transport, energy, communications and information technology. At the same time, these efforts should be accompanied by measures to maximize the development impact of these flows. In this regard, the Doha Declaration on Financing for Development contains a specific commitment by Governments to strengthen national and international efforts aimed at maximizing linkages between transnational corporations and domestic production activities, enhancing the transfer of technology and creating training opportunities for the local labour force.

17. There has also been a sharp drop in other categories of private capital flows to developing countries. The sharpest drop has been in bank lending to emerging economies, reversing inflows of about $400 billion in 2007 into a projected net

[11] UNCTAD, "Assessing the impact of the current financial and economic crisis on FDI flows" (UNCTAD/DIAE/IA/2009/5), Geneva, April 2009.

outflow in 2009. Moreover, a large volume of international bank debt to corporations in developing countries matures in 2009. A number of corporations, including small and medium-size enterprises, may run into difficulties in rolling over their debt. Furthermore, corporations that previously relied on foreign funding may try to shift to domestic funding markets, adding to pressures on smaller local enterprises. Portfolio flows to developing countries have also contracted sharply owing to contagion and an increased risk aversion by institutional investors.

18. In the longer term, however, it is necessary for policymakers to address issues relating to the inherent instability of many categories of private capital flows. The problems begin with inadequacies in regulation and oversight at the national and international levels. Existing regulatory approaches have been traditionally confined to improved disclosure, prudential controls and risk management. These are now generally seen as insufficient to mitigate the inherent procyclicality of private capital flows and need to be accompanied by the establishment on further development of countercyclical regulations and instruments and institutions that effectively supervise all of the sources of systemic risk emanating from financial markets, including the activities of hedge funds and cross-border flows. There should, moreover, be greater scope for countries to employ measures to effectively curb excessive short-term capital inflows without discouraging inflows of longer-term finance.

19. Officially recorded remittance flows to developing countries have been registering double-digit annual growth in the past few years and totalled more than $300 billion in 2008 (three times the level of ODA flows to developing countries). For several small economies, remittances account for more than 20 per cent of GDP. The projected decline of remittances in 2009, across all developing regions, is therefore expected to create hardships in many poor countries, since they have been important sources of support for consumption and development.

III. International trade as an engine for development

20. The role that trade can play in fostering economic development is well established. Trade can generate gains for developing countries, in most cases more than any other area of international economic cooperation. The impact on growth and employment of the collapse in the volume of trade in the current crisis amply demonstrates this critical role.

Declining trade volumes

21. The World Trade Organization (WTO) reports that world merchandise trade growth slid to 5.5 per cent in 2007 from 8.5 per cent in 2006.[12] Initially, WTO projected 4.5 per cent growth in 2008, but has since reduced this estimate to 2 per cent in view of the sharp drop in global production in the fourth quarter of 2008.

[12] WTO press release No. 554 dated 23 March 2009.

22. For 2009, WTO has predicted that trade growth will slide a further 9 per cent. UNCTAD predicts that goods exports globally will fall between 6 and 8 per cent.[13] The mid-2009 update to *World Economic Situation and Prospects 2009*[14] projects an even steeper fall, with world trade declining 11.1 per cent in 2009 (the largest such decline since the Great Depression of the 1930s). The update gives a baseline scenario of 4.1 per cent growth in world trade in 2010, based on a bottoming out in the fall in real economic activity by the end of 2009.

23. This collapse in world trade is disproportionately affecting developing countries. Falling demand for imports of both commodities and finished goods have contributed to this trend, as have falling prices of commodities in particular, the difficulty in accessing, and the high costs of, trade financing, and reduced government expenditure financed through trade tariffs.

24. The situation for commodity exporters is especially difficult. From 2002 to mid-2008, many countries gained from the generally upward trend in the prices of oil and non-oil commodities. The intensification of the global financial crisis since mid-2008 has, however, led to a sharp reversal in this trend. Oil prices plummeted by more than 70 per cent from their peak levels of mid-2008 and although recent rises have been significant, the volatility in pricing creates further difficulties.

25. Similarly, the prices of metals fell by 50 per cent, while the prices of some other commodities also declined significantly. There has been some rebound, but markets remain at a low ebb and are highly volatile. Export earnings and government revenue will likely continue to be depressed in many developing countries. Food and energy-importing countries may see their terms of trade improve, although in most cases these gains may be more than offset by the collapse in export demand, the increased cost of borrowing and/or falling remittance flows. Among net exporters of commodities, low-income countries are being hit hardest by plunging world market prices because primary exports comprise, on average, 70 per cent of their total exports. In addition, a high share of government revenue comes from taxes on these exports.

Risks of protectionism

26. In response to collapsing domestic production and employment, protectionist trade measures have begun to be observed in national recovery policies. World Bank data indicate that 17 of the countries taking part in meetings of the Group of Twenty have, among them, implemented 47 measures that restrict trade at the expense of other countries. Developing countries are likely to suffer disproportionately from any surge in protectionism, because they often export products that are particularly sensitive to protectionist measures, do not have the resources to engage in retaliatory measures and generally lack the safety nets that assist those affected by such actions. In addition to trade protectionism, there could be an increase in anti-competitive practices to preserve market positions.

27. Calls to avoid protectionism have become commonplace in meetings of world leaders, such as at the recent meetings of Asia-Pacific Economic Cooperation and

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[13] UNCTAD, report of the UNCTAD secretariat entitled "Global economic crisis: implications for trade and development" (TD/B/C.I/CRP.1). Available in English only from http://www.unctad.org/en/docs/cicrp1_en.pdf.

[14] Available from http://www.un.org/esa/policy/wess/wesp2009files/wesp09update.pdf.

the leaders of the Group of Twenty. The true test remains whether or not countries in practice engage in such protectionism or reject it, recognizing the corrosive social and economic impact of the beggar-thy-neighbour policies that prevailed in the 1930s, with disastrous consequences. In its annual report for 2009,[15] WTO observed the rise of protectionist tendencies in the context of the crisis, noting that the number of anti-dumping initiations increased by 28 per cent in 2008, compared to 2007.

28. In dealing with the global crisis, it is important to recognize and consolidate the multilaterally agreed, rules-based trade disciplines represented in the WTO and earlier General Agreements on Tariffs and Trade arrangements. These arrangements recognize legitimate trade measures in response to emergencies, particularly in the conservation of foreign exchange. Demonstrating the ability of the system to alleviate the depth of the crisis through the legitimate use by members of their trade policy space is important to making further progress in strengthening it. Differentiating between trade-restricting measures adopted for protectionist purposes and those legally provided for in international rules is therefore important. Moreover, such measures are certainly preferred to competitive devaluations, for which the present international system has no effective disciplines. The ultimate objective of staging a recovery in world trade will involve the return of domestic production and demand in a wide variety of economies. Within the global trade disciplines already agreed, it is in the global interest for individual countries to undertake recovery policies that are appropriate to their particular situation.

29. South-South trade remains a beacon of hope in the current climate. While such trade has also declined, it nevertheless remains robust having experienced dynamic growth in past years. In 2007, South–South merchandise trade, in terms of exports, had increased more than threefold since 1995 and amounted to more than 46 per cent of the total trade of developing countries.[16]

Doha Development round

30. The ongoing WTO trade negotiations under the Doha Development Agenda seek, inter alia, to establish a fairer and more equitable trading system for all WTO members by addressing inequities in current multilateral trading rules.

31. In the Doha Declaration, the international community reiterated its urgent resolve to ensure that ongoing efforts improve the operation of the multilateral trading system to better respond to the needs and interests of all developing countries, in particular the least developed countries. It also called for the implementation of the ministerial declaration of WTO, adopted at its Sixth Ministerial Conference, held in Hong Kong, China, on the central importance of the development dimension in every aspect of the Doha Development Agenda work programme and its commitment to making the development dimension a meaningful reality.

32. The failed WTO ministerial talks held in Geneva in July 2008 signalled, at best, a significant delay in the Doha negotiations. The progress made since has been only limited, especially in the agricultural negotiations so essential to a truly

[15] WTO, *World Trade Report 2009: Trade Policy Commitments and Contingency Measures* (Geneva, July 2009).

[16] UNCTAD data.

development-centred outcome. Yet, several major parties have recently reiterated their interest in pursuing the Doha round, and the necessary impetus at the political level to revive the Doha round appears to be gaining ground. Any such revival must be grounded in the need to put the developmental dimensions at the centre of the negotiations, in particular the principle of special and differential treatment and such practical measures as duty-free and quota-free treatment of all exports of the least developed countries. With one eye on history and one on the future, the current financial crisis makes the successful and speedy conclusion of a development-focused Doha round all the more urgent.

33. Protectionist surges in response to the current economic slowdown around the world highlight the importance of actions to ensure that the global trading system remains open to support the development efforts of all countries, particularly the poorer countries. It emphasizes once again the need for an early but development-oriented conclusion to the Doha development round.

Aid for trade and the trade financing gap

34. At the London Summit in April 2009, the leaders of the Group of Twenty agreed to the provision of additional trade financing support by multilateral development banks in the amount of $250 billion. While significant, this measure will only play one part in addressing a trade financing gap and needs to be implemented in concert with other actions, such as the scaling up of aid for trade, to ensure that practical advantage can be taken of market opportunities.

35. The World Trade Organization convened the second Global Review of Aid for Trade in Geneva on 6 and 7 July 2009. The review showed that aid-for-trade flows had grown annually by more than 10 per cent in real terms since 2005, bringing total new commitments to more than $25 billion in 2007, an increase of $4 billion. In addition, non-concessional loans added a further $27 billion to tackle binding supply-side constraints. Calculations by the Organization for Economic Cooperation and Development (OECD) show that 9 of 10 commitments in aid-for-trade projects and programmes do generate actual activity.

36. In relation to the decline in the supply of trade finance, data on trends in export and import credits are not readily available, but many countries have reported problems in accessing various trade finance instruments. This has led to a compression of trade activity, reflected in the idling of container ships and a precipitous drop in shipping rates.

IV. Increasing international financial and technical cooperation for development

37. It is noteworthy that total net ODA from countries members of the OECD Development Assistance Committee (DAC) rose in 2008 by 10.2 per cent in real terms to $119.8 billion, the highest dollar figure ever recorded, and reached 0.30 per cent of the combined gross national income (GNI) of donors. In particular, bilateral development projects and programmes rose by 12.5 per cent in real terms compared to 2007, indicating that donors are substantially scaling up their core aid programmes. Preliminary data for 2008 show that net bilateral ODA to Africa totalled $26 billion, of which $22.5 billion went to sub-Saharan Africa: an increase

of 10.6 per cent and 10 per cent, respectively, in real terms, excluding volatile debt relief grants. Among DAC member countries, the largest contributors in terms of gross ODA were the United States of America ($26.9 billion), Japan ($17.4 billion), Germany ($15.9 billion), France ($12.4 billion) and the United Kingdom of Great Britain and Northern Ireland ($11.8 billion).

38. The total aid of the United States increased in 2008 by 16.8 per cent in real terms, compared with the decline of 9.9 per cent in 2007; its ODA share of GNI has now risen to 0.18 per cent. While United States aid increased to practically all regions, aid to sub-Saharan Africa rose sharply by 38.3 per cent in real terms, to $6.5 billion, and aid to the least developed countries rose by 40.5 per cent in real terms, to $6.9 billion. Thus, the promise of the United States to double aid to sub-Saharan Africa by 2010 appears to be on track. Japan also reversed the downward trend in its ODA, which had persisted since 2000, excluding 2005 and 2006 when high levels of debt relief occurred. The net ODA of Japan in 2008 was $9.4 billion, representing an increase of 8.2 per cent in real terms compared with 2007, when it fell by 30.1 per cent. The increase is mainly owing to a rise in contributions to international financial institutions. Japan had announced that it intends to fulfil its promise of an overall increase of $10 billion over 2005-2009.

39. The combined net ODA of the 15 countries members of DAC that are members of the European Union, which account for almost 60 per cent of all DAC ODA, also rose by 8.6 per cent in real terms, to $70.2 billion in 2008 compared to 2007, when it fell by 5.8 per cent in real terms. As a share of GNI, net ODA from those 15 countries rose from 0.40 per cent of their combined gross national product to 0.42 per cent in 2008. The United Kingdom, Spain, Germany, Canada, Belgium, Greece, Australia, New Zealand and Portugal also reported significant increases in their ODA in 2008.

40. There is a fear that the strain of the crisis may lead to donor countries cutting their aid efforts, including aid for trade, similar to the global economic recession of the early 1990s, which produced large fiscal deficits in donor countries that led to deep cuts in ODA, from 0.33 per cent of GNI in 1992 to 0.22 per cent in 1997. Estimates differ across donors but, according to a recent study, a 1 per cent negative growth shock implies an 8 per cent reduction in aid budgets five years afterwards. Such a reversal at the present juncture would place a dangerous additional burden on developing countries already struggling with restricted sources of income and increased poverty.

41. At various international meetings, including the special high-level meeting of the Economic and Social Council in April 2009 and the high-level meeting of DAC in May, many developed countries announced their determination not to permit their domestic financing difficulties to reduce their ODA flows and many indicated that they were seriously considering contributing to funds to mitigate the impact of the crisis on the most vulnerable populations.

V. External debt

42. While confined to a select group of countries, the international community has made notable progress in regard to debt relief. These efforts set out basic principles which can be applied in expanding international cooperation in dealing with debt distress, an activity which will become critical in the next few years. In adopting the

Doha Declaration in December 2008, the international community acknowledged the need to continue to address all relevant issues regarding external debt problems, including through the United Nations, and to consider ways to explore enhanced approaches of sovereign debt restructuring mechanisms based on existing frameworks and principles, with the broad participation of creditors and debtors and ensuring comparable burden-sharing among creditors, with an important role for the Bretton Woods institutions.[17]

43. Since the adoption of the Monterrey Consensus, the most important international actions in respect of external debt have been undertaken within the context of the Heavily Indebted Poor Countries (HIPC) initiative and the Multilateral Debt Relief Initiative. Substantial assistance in the amount of $117 billion (in nominal terms) has been committed to the post-decision point heavily indebted poor countries, mostly under the HIPC initiative but also including $49 billion under the Multilateral Debt Relief Initiative, amounting on average to about 50 per cent of their GDP in 2007. About one half of the funds is to be provided by bilateral creditors and the rest will come from multilateral lenders.

44. Of the 40 countries eligible or potentially eligible for assistance under the HIPC initiative, 24 have now reached their completion points and have received or are receiving irrevocable debt relief. In addition, 11 countries have reached their decision points and some are receiving interim debt relief. With respect to the Multilateral Debt Relief Initiative, about two thirds of the funds, or an additional $17.8 billion, have been delivered to the 24 post-completion point countries, with two thirds of the cost to be borne by the International Development Association (IDA).

45. With the onset of the global financial crisis, developing country external payments and fiscal balances have come under enormous stress. Many developing economies, including those that have benefited from debt relief initiatives, could fall into debt distress. External financing conditions have tightened, both from public and private sources. Escalating fiscal and financial pressures in both donor and recipient countries are exacerbating the challenges. In the context of reduced capital inflows and strains on the budgets of traditional external lenders, lower revenue and increased reliance on external financing to offset shortfalls in domestic resources constitute the main sources of fiscal stress. Additional fiscal pressures arise from currency depreciations and rising interest rates. All of these factors pose serious risks to the debt sustainability of developing countries and undermine their capacity to service or roll over external debt obligations.

46. For HIPC countries, debt levels are rising quickly and the thresholds set under the Debt Sustainability Framework of the Bretton Woods institutions are now being approached more rapidly. As a result, an increasing number of heavily indebted poor countries are at a higher risk of debt distress. The crisis is unmistakably reversing the progress that has been made under these schemes. In March 2009, IMF identified 28 countries with debt in excess of 60 per cent of GDP and its simulations suggest that another three countries could face debt ratios in excess of 60 per cent if they undertook additional borrowing to offset shortfalls in external financing, possibly leading to debt-related difficulties further down the road. IMF simulations of additional borrowing to offset the shortfalls in external financing suggest that at

[17] General Assembly resolution 63/239, annex, para. 67.

least 20 countries are on the verge of a high risk of debt distress.[18] On the assumption that countries will make up external financing shortfalls with public deficits, IMF estimates that this will cost up to 4 per cent of GDP in 2009 alone.

47. In early April 2009, leaders of the Group of Twenty announced a $1.1 trillion package to help countries to meet their immediate financial needs arising from the crisis and to boost worldwide economic activity. The bulk of the resources counted as part of the package comprised financing from programmes announced prior to the meeting of the Group. At the most, it is estimated that the poorest countries will have access to an additional $50 billion of these resources against a financing shortfall estimated at $165 billion.[19] To the extent that low-income countries are reaching the limit of rolling over scheduled debt-service payments or drawing down their reserves, the international community could consider a debt-service moratorium for low-income countries at no cost (no interest liabilities on delayed payments), as suggested by UNCTAD at the special high-level meeting of the Economic and Social Council in April, or a one-time special allocation of special drawing rights (SDRs) for low-income countries at a level appropriate to meet the financing shortfall and distributed according to population size, as proposed by the States Members of the United Nations that are members of the Group of 77 and China during the negotiations at the Conference on the World Financial and Economic Crisis and its Impact on Development, held in New York from 24 to 30 June 2009.[20]

48. In the period 2003-2007, at a time of abundant liquidity and low interest rates, the debt of middle-income countries from private sources surged. The availability of private debt has since declined precipitously as part of the deleveraging process in advanced countries. The contraction in international financial markets creates substantial fiscal risks which threaten macroeconomic stability in the middle-income countries, even though a few of the more prominent have built up cushions against the downturn in their international reserves. From the perspective of their creditors, these middle-income countries are facing difficulties in rolling over their external debt, particularly in respect of external corporate borrowing. Moreover, unlike low-income countries, the soundness of the domestic financial sectors of middle-income countries has deteriorated owing to an exposure to financial assets in advanced economies and the sectors require public resources to restore their health.

49. Middle-income countries with heavy debt obligations could be compelled to pursue more extensively both conventional options, such as debt restructuring, and more unconventional options, such as bilateral debt relief agreements and debt swaps, in order to manage the impending debt vulnerability. The cumulative effect of these efforts during a period of reconstruction of the international financial sector would increase the fragility of the global financial system and could extend the recovery time over uncertainties about the servicing of developing country debt obligations.

50. Target 15 of the Millennium Development Goals calls for dealing comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable for all developing

[18] A country is considered at high risk of debt distress if the GDP and corresponding debt service relative to exports ratios exceed their respective thresholds.

[19] World Bank, *Global Monitoring Report 2009*.

[20] An SDR allocation would require amendment of the IMF Articles of Agreement.

countries in the long term. In the case of middle-income countries, urgent progress is needed to go beyond the individual country, case-by-case approaches to debt rescheduling and resolution which could become widespread within the next year and to establish more predictable, rules-based and equitable international mechanisms. Revisiting the effort to install a sovereign debt resolution mechanism, which was launched by IMF in 2002 but later suspended, would seem to be timely.

51. For the low-income countries, prospective debt difficulties will increase pressures to expand the coverage of existing approaches, improve the flexibility of the debt sustainability framework (as requested at the meeting of the Group of Twenty in April) and address the obstacles to funding expanded debt relief approaches that will restore the growth dynamics of the economy. IMF is reviewing its policy on debt limits to allow more flexible borrowing strategies while ensuring debt sustainability.

VI. Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development

52. At the high-level meeting of the Economic and Social Council in April 2009, many speakers emphasized that the crisis had revealed major flaws in the financial sector and in financial regulation and supervision at both the global and national level. They also emphasized that to find a way out of the crisis, it would be necessary to restore confidence, ensure proper functioning of financial markets, achieve stricter oversight of such markets and reform the global financial system. Making rapid progress in strengthening the voice and participation of developing countries was deemed necessary to restore the legitimacy and effectiveness of institutions of global economic governance.[21]

Strengthening international financial regulation

53. A consensus is emerging that reforms must involve reshaping regulatory systems to identify and take account of macroprudential risks; expanding the perimeter of regulation and oversight to all systemically important financial institutions, instruments and markets; mitigating procyclicality in prudential regulation; strengthening capital and risk management; reorienting principles on executive remuneration to minimize reckless risk-taking; and improving standards on valuation and provisioning. In a financially integrated world with competing national financial centres in which financial companies can choose to locate specific activities in order to exploit regulatory advantage, these reforms will be successful only if coordinated internationally.

54. More advanced markets should bear a relatively greater burden in oversight and regulatory activities, especially over the risk-sharing features of internationally traded financial assets, so that smaller and less sophisticated markets do not have to

[21] Worth noting is the encyclical letter, *Caritas in Veritate* (Charity in Truth), issued by Pope Benedict XVI on 7 July 2009, which emphasizes, inter alia, the importance of giving poorer nations an effective voice in shared decision-making in the context of the economic crisis and called for reforms in the United Nations, economic institutions and international finance towards realizing the concept of the family of nations.

overregulate to protect the soundness of their own financial and currency markets, thereby sacrificing stronger access to international finance. Previous efforts to strengthen cooperation through the deliberations of the Financial Stability Forum, the Basle Committee on Banking Supervision and colleges of supervisors proved inadequate. The creation in April 2009 of the Financial Stability Board represents a positive step towards the establishment of a new institution that can potentially improve coordination in international financial regulation, even though its membership still does not include the developing countries most severely affected by the current crisis.

Increasing the stability and volume of global liquidity

55. The call of the Group of Twenty in April 2009 for a general SDR allocation by IMF equivalent to $250 billion is recognition by world leaders, for the first time since the early 1980s, of the need to boost significantly international liquidity using an international reserve unit. The cumulative total of SDR allocations was previously equivalent only to $21.4 billion. The ongoing financial crisis has sparked a discussion among world leaders of the deficiencies of the present international monetary system in which a national currency, the United States dollar, serves as a dominant source of international foreign exchange reserves. This issue was also the subject of discussion in the first summit meeting of the BRIC group of countries (Brazil, Russian Federation, India and China), held in Yekaterinburg, Russian Federation, in June 2009. Reforming a global reserve system so that it can provide a stable foundation to growing trade volumes and financing for development will require either supplementary disciplines on dollar emission and/or a purposeful evolution towards a truly global currency reserve system. Technically, it should be possible to move forward on a mix of both, recognizing the difficult political constraints that have to be overcome in making the progress needed in this critical matter.

Role of surveillance and managing global imbalances

56. Surveillance remains the key crisis prevention tool of IMF, but it is generally recognized that progress remains to be made in its design and implementation. Since it is indisputable that the global financial crisis requires global solutions, the world economy now more than ever needs a credible IMF with a governance structure which facilitates its role in promoting international economic stability and sound financial development, most particularly of developing countries, and which can exercise strong policy leadership.

57. Since the 1980s, IMF has mainly focused on problems in emerging markets and developing countries, devoting insufficient attention to major financial centres and vulnerabilities in global financial markets. The financial crisis underscores the need for the Fund to maintain a sharp focus on risks in all systemically important countries, especially the reserve currency-issuing countries, and their potential spillover effects. To close this gap, the IMF vulnerability exercise is being expanded to advanced economies and integrated with the early warning exercise to be conducted jointly with the Financial Stability Board. Much more progress is required in improving surveillance over the major financial markets, including the extent to which national authorities should take account of the impact of their policies on the global financial system.

58. Surveillance by IMF can only be effective to the extent that members are cooperative and responsive as regards the implementation of surveillance recommendations. In the case of the current crisis, there was a clear failure to act on the information made available by IMF. The challenge is to ensure that the relevant information is used proactively to prevent and mitigate future crises.

59. While the traditional emphasis of IMF has been on exchange rates, an area in which some progress had been made, the crisis has pushed macrofinancial and macroprudential issues into the centre stage in IMF surveillance. In this regard, IMF has taken steps to increase the attention given to financial risks, including asset price bubbles, leverage, risk concentration in large banks and hidden or off-balance sheet exposures. A key aspect here is the integration of macroeconomic and financial sector surveillance, the focus on the linkage between the macroeconomy and the financial markets, and the soundness of the financial sectors of member countries, particularly those that have a major impact on the global economy.

60. The primary long-term goal of enhanced surveillance must be to ensure the stability of the international monetary system, notably through the reduction of global imbalances. This can only be accomplished if countries enhance their coordination in fiscal and monetary policies, paying attention to challenges in shifting aggregate demand from deficit to surplus countries. This is why it is more than ever critical to build an effective framework for enhanced multilateral surveillance and policy coordination against the backdrop of the intended governance reform of IMF.

Lending activities of the International Monetary Fund

61. Amid the current financial market turmoil, the need for providing official liquidity has once again become the primary focus of Governments around the world. In its turn, since the onset of the crisis, IMF has been providing large-scale financing to countries experiencing a reduction in the availability of external funding. As of May 2009, IMF lending commitments reached a record level of $157 billion, including a sharp increase in concessional lending to low-income countries. An important characteristic of recent IMF lending arrangements has been their exceptionally large size in relation to country quotas.

62. Even though programmes initiated in 2008 have incorporated the customary public spending cutbacks, IMF has initiated an overhaul in its lending toolkit and conditionality framework to increase the effectiveness of its crisis prevention and resolution efforts. It has doubled all loan access limits, including for low-income countries, and the surcharge framework has been simplified. Two new facilities which are intended to provide contingency financing in large volumes have been put in place: the flexible credit line available to countries with a strong track record of macroeconomic management and which thus does not entail any ex post conditionality, and the high access precautionary arrangement. These changes are intended to make the overall lending framework more flexible and suited to the diverse needs of members, while remaining consistent with the original purpose of providing temporary financing for balance-of-payment difficulties. The changes require increased resources for IMF appropriate to the much larger volume of financial flows occurring in the world economy. The Group of Twenty and the International Monetary and Financial Committee of the IMF Board of Governors have agreed to triple the loanable resources of the Fund, through an increase in its

main standing borrowing arrangement (the New Arrangement to Borrow (NAB)) by up to $500 billion. Of these, about $415 billion have already been pledged by member countries.

VII. Staying engaged

63. The Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus, held in Doha from 29 November to 2 December 2008 and chaired by His Highness the Emir of Qatar, consisted of seven plenary meetings and six multi-stakeholder round tables on the major thematic areas of the Monterrey Consensus. Some 40 Heads of State or Government, 9 Deputy Heads of State or Government, 50 ministers and 17 vice-ministers of foreign affairs, finance, development cooperation and trade, and other high-level officials from 170 States, as well as representatives of all relevant stakeholders, participated in the Conference. The Conference adopted the Doha Declaration on Financing for Development, which was endorsed by the General Assembly in resolution 63/239.

64. The overall theme of the special high-level meeting of the Economic and Social Council with the Bretton Woods institutions, WTO and UNCTAD was "Coherence, coordination and cooperation in the context of the implementation of the Monterrey Consensus and the Doha Declaration on Financing for Development". The two sub-themes of the plenary debates were: (a) addressing the impact of the global financial and economic crisis on development, including issues related to the international financial and monetary architecture and global governance structures; and (b) strengthening of the intergovernmental inclusive process to carry out the financing for development follow-up.

65. As called for in paragraph 89 of the Doha Declaration, the Economic and Social Council, at its high-level meeting, considered the need for a strengthened and more effective intergovernmental inclusive process to carry out the financing for development follow-up. At its substantive session of 2009, the Council, in resolution 2009/30, recommended a number of changes in modalities for a strengthened and more effective multi-stakeholder intergovernmental process to implement the follow-up on financing for development:

(a) The duration of the special high-level spring meeting of the Council with the international financial and trade institutions could last for up to two days and should be timed appropriately, at least five weeks before the spring meetings of the Bretton Woods institutions. Discussions at the first segment of the high-level meeting would concentrate on a topic of current interest and the second segment would be organized under the overall theme of "Coherence, coordination and cooperation in the context of the implementation of the Monterrey Consensus and the Doha Declaration on Financing for Development";

(b) Consideration of the agenda item on financing for development should be allotted up to two full days during the annual substantive session of the Council, when it should normally adopt a substantive resolution;

(c) The General Assembly should give more prominence to its annual agenda item entitled "Follow-up to and implementation of the outcome of the 2002 International Conference on Financing for Development and the 2008 Review

Conference". A programme of multi-stakeholder consultations, including civil society and the private sector, could be reinitiated by the Financing for Development Office of the Department of Economic and Social Affairs of the United Nations Secretariat.

66. The Conference on the World Financial and Economic Crisis and Its Impact on Development, held in New York from 24 to 30 June 2009, consisted of six plenary meetings and four interactive round tables. The Conference adopted an intergovernmentally agreed outcome document[22] which called for, inter alia, increased multilateral resources with an emphasis on grants and non-debt-creating finance for developing countries, the consideration of debt standstills and legitimate trade defence measures for countries facing balance-of-payment difficulties, recognition of the potential of SDRs in providing international liquidity, improvement of the transparency of the global financial system to deter illicit financial flows, strengthening of mechanisms for global economic monitoring and coordination, and further development of and support for the comprehensive crisis response of the United Nations development system.

67. In the outcome document, the General Assembly was invited to set up an ad hoc open-ended working group to follow up on the issues contained in that document, and the Economic and Social Council was requested to consider and make recommendations to the General Assembly on a number of matters. In response, on 31 July 2009, the General Assembly formally established the working group, and the Council, by decision 2009/258, requested the Secretariat to provide detailed reports on a number of issues by 15 September, with a view to reviewing the progress made in the consideration of those issues at its resumed substantive session of 2009.

[22] General Assembly resolution 63/303, annex.