WORLD ECONOMY UPDATE

June 12, 2015 | Vol. 5 No. 11

Financing for Sustainable Development in the Post-2015 Era

ISSN 2233-9140

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1. Background

With only a few months left until the target date for the Millennium Development Goals (MDGs), the international community is actively in the process of arriving at a global development agenda for the post-2015 period. Centered on the core values of human rights, equity, and sustainability, the post-2015 development agenda is expected to include a long-term vision in tackling global challenges and enabling transformative change. A set of sustainable development goals (SDGs) will be adopted at the UN summit this September.

One of the most significant features of the current discussion on the post-2015 development agenda is its particular focus on global partnership and means of implementation in order to achieve the new goals. The global partnership in the post-2015 era means mutual cooperation among actors in development cooperation. Beyond the relationships between developed and developing countries or donors and recipients, emerging developing nations, civil society and the private sector will play a major role in the evolving global development landscape. Financing for sustainable development as a means of implementation is more important than ever to achieving the global development goals.

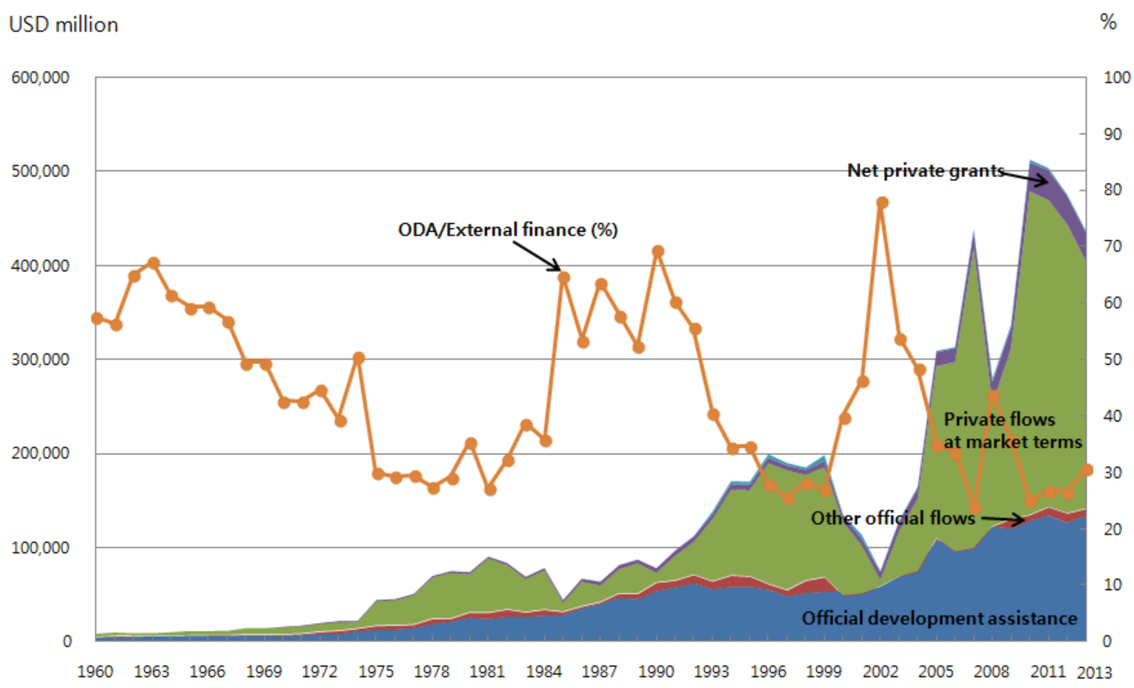
Considering that the challenges the international community is facing become broader in scope and more complicated in context, additional resources and innovative financial instruments are absolutely necessary in the pursuit of renewed development agenda. A high-level discussion will be scheduled at the 3rd International Conference on Financing for Development which is to be held in Addis Ababa, Ethiopia in July 2015.

2. Key Issues in Financing for Sustainable Development

A. Emphasizing the Importance of ODA as a Traditional Source

For the past 50 years or so, official development assistance (ODA) has been serving as the key financial resource in developing countries. ODA volumes have risen steadily; however, the relative importance of ODA has been diminishing in many developing countries in comparison to other sources of external finance. In 2013, ODA volumes hit an all-time high at USD 135 billion, but the portion of ODA to total external finance has dropped from 58% in 1960 to 35% in 2013 (Figure 1). Nonetheless, ODA will remain a crucial part of international development cooperation in implementing the post-2015 agenda, particularly for countries most in need. In 2013, ODA still represented over 90% of the USD 32 billion in financial inflows to least developed countries (LDCs, Figure 2).

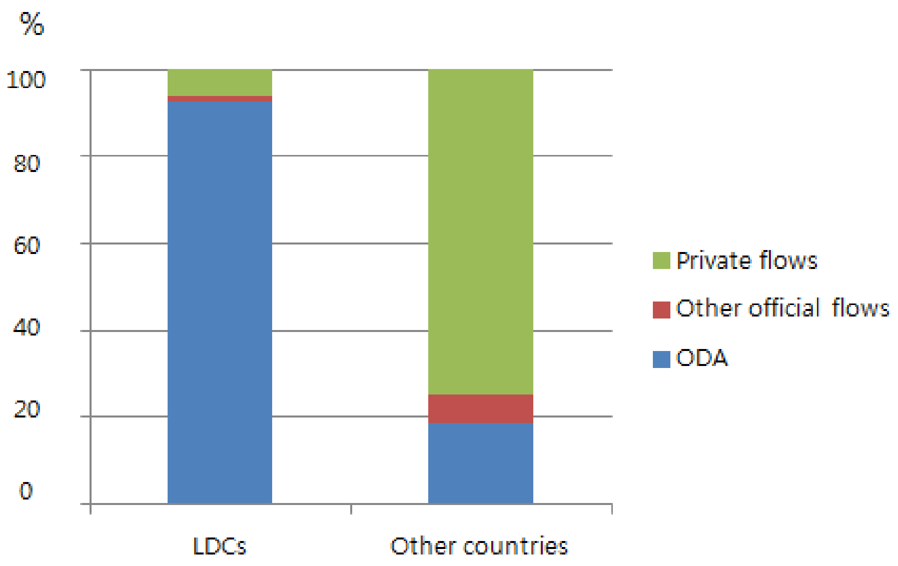
[Figure 1] External financial resources for development



Note: Net disbursement, current prices.
Source: Calculation based on the OECD Stats (http://stats.oecd.org/).

At the 2014 OECD Development Assistance Committee (DAC) high level meeting, the members agreed to allocate more ODA to countries such as LDCs, small island developing states, land-locked developing countries and fragile and conflict-affected states, and to commit to reversing the declining trend of ODA to LDCs. The members who have committed to the UN target of 0.15% to 0.20% of GNI as ODA for LDCs reconfirmed their commitment.

[Figure 2] Distribution of external development finance in LDCs and other countries, 2013



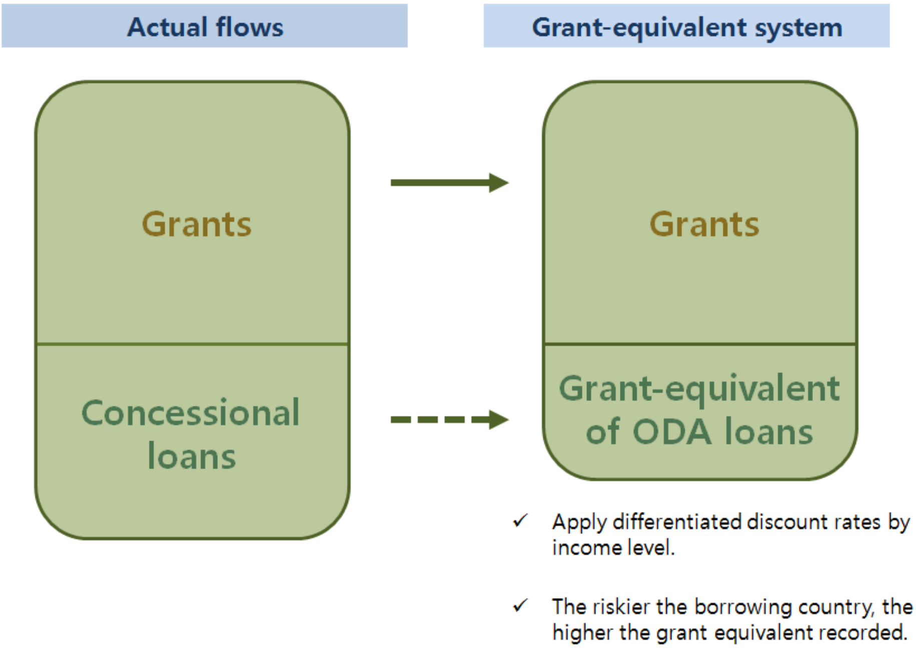
Note: Remittances are excluded. Other countries include Other LICs, LMICs, UMICs and Part I unallocated by income groups.
Source: Calculation based on OECD aggregate geographical data.

Recently, the DAC introduced a grant equivalent system and modernized the reporting of concessional loans (Figure 3). Under the new reporting system, loans with greater concessionality will earn more ODA credit than less concessional ones. Concessionality is now assessed based on different discount rates[1] with an adjustment factor of 1% for upper middle income countries, 2% for lower middle income countries, 4% for LDCs and other low income countries (LICs). Furthermore, loans to LDCs and other LICs will be reportable as ODA only if a grant element is higher than 45%.[2] This change is expected to give greater incentive for increased provision of ODA and lending on highly concessional terms to LDCs and other LICs.

[1] The IMF discount rate, 5% will be utilized as a base factor.

[2] To be counted as ODA, loans to lower middle income countries need to have a grant element of at least 15%, and those to upper middle incomes countries of at least 10%.

[Figure 3] Measuring donors' efforts



Source: OECD (2014). "Background Paper: The treatment of loan concessionality in DAC statistics," p. 3.

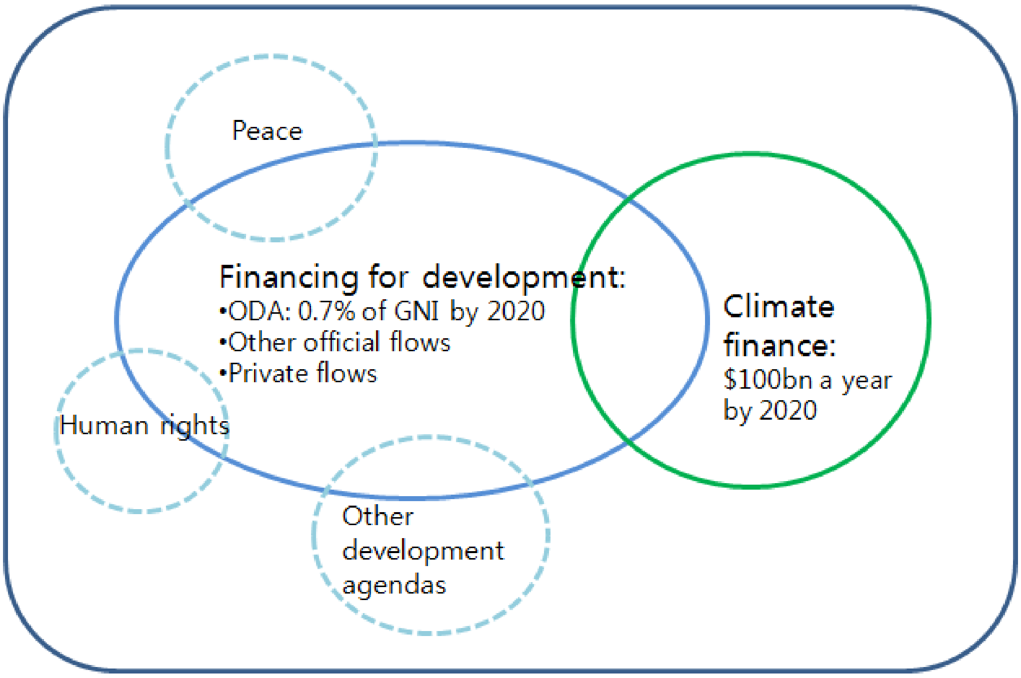
B. Catalyzing Private Sector Investment

Recognizing the role of the private sector in development, the utilization of ODA is encouraged in order to mobilize private sector resources. Also, innovative financial instruments are needed for leveraging additional finance for sustainable development. The so-called "smart ODA" means the use of limited official concessional resources towards countries most in need. The private-sector instruments such as guarantees, equity, and mezzanine finance are essential in unlocking private investment. Bilateral development finance institutions (DFIs) in some developed countries make use of the resources for their development cooperation activities from not only the government budgets but also private capital markets. The DFIs utilize the various financial instruments that have leveraging potential. The DAC is currently engaged in efforts to quantify the efforts of official sectors that have mobilized private sector finance and is considering two different options as private-sector instruments as ODA; first would be to incorporate support that a donor government provides to its DFI. The other option would be to report ODA-eligible flows or grant equivalents of a certain private-sector instrument in the same manner as grants and concessional loans. Such debate has significant implication for countries like Korea which rely on the government budget and implement most development cooperation projects on the basis of grants and concessional loans.

C. New Measure: Total Official Support for Sustainable Development

The post-2015 development agenda is growing broader than ever, thus calling for diverse sources and instruments to mobilize development finance to a level that corresponds to the breadth of the agenda (Figure 4). To give greater incentive to efforts for mobilizing resources, and to enhance transparency and accountability of the international support for sustainable development, a new measure of total official support beyond ODA has been proposed. Calculated on cash-flow basis, the new measure would include both concessional and non-concessional finance and consider all types of financial instruments. The new measure is not a replacement of ODA; rather, it will be a complementary statistic that would be shared among providers of development cooperation beyond the traditional ODA donors. The components of the new measure are expected to take clearer shape through the Addis Ababa Accord on financing for development and the post-2015 development framework adopted later. The new measure covers contributions to global public goods such as climate change mitigation and adaptation, and peace and security that are essential for achieving sustainable development goals. In 2010, developed countries agreed to the goal of mobilizing climate finance: USD 100 billion per year by 2020. Total bilateral climate-related ODA commitments made by the DAC members represented 17% of total bilateral ODA in 2013.

[Figure 4] Financing for sustainable development



Source: Jung *et al.* (2014). “Study on the financing for development in Post-2015 era: Policy implications for Korea.”p.70.

3. Conclusion

In the years to come, development cooperation will encompass a broader agenda and require more resources on a significant scale. Maintaining poverty eradication as the most important goal of global prosperity and sustainable development will be an overarching theme in the post-2015 era. Consequently, international discussions on development finance have gained new significance. A wide range of financial resources needs to be mobilized from public and private sources regardless of the nature of finance, concessional or commercial. The DAC's work on modernizing its statistical system regarding development finance and introducing a new measure of total official support for sustainable development will play a crucial role in incentivizing the efforts of providers of development finance. It holds implications for Korea, which relies heavily on ODA, and on grants and highly concessional loans for its development cooperation (Table 1).

[Table 1] Loan shares and their grant elements of the select DAC countries (2013)

	France	Germany	Japan	Korea	Portugal	DAC Average
Loan share of total ODA (%)	32.8	20.7	58.5	45.4	36.4	15.6
Grant element (%)	52.7	38.3	81.4	89.2	66.0	69.1

Note: ODA commitments
Source: OECD Aid Statistics, Table 22 Other terms parameters for loan-giving DAC members.

It is clear that discussions on development finance beyond ODA are not intended to minimize the role of ODA in financing for development. For low income countries in particular, ODA remains a major source of development finance, and by introducing a grant equivalent system and considering differentiated discount rates by income level, donors will have more ODA credits when supporting those countries most in need. Meanwhile, the engagement of DFIs in middle income countries holds greater prospects for mobilizing additional resources other than ODA. In light of this, Korea's next challenge is to keep up with global efforts to extend the scope of development finance in general as well as to continuously increase its ODA volume.