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International Monetary and Financial Committee (IMFC) of the Board of Governors

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“We need to massively scale up affordable long-term financing by aligning all financing flows to the SDGs and improving the terms of lending of multilateral development banks. The high cost of debt and increasing risks of debt distress demand decisive action to make at least $500 billion dollars available annually to developing countries and convert short term lending into long term debt at lower interest rates.”¹

United Nations Secretary-General Mr. António Guterres

Three years after the start of the COVID-19 pandemic our world looks much different. Scarring effects from the pandemic combined with the war in Ukraine, high inflation and monetary tightening have created a challenging financial and macroeconomic situation.

The historic allocation of $650 in Special Drawing Rights by the International Monetary Fund, boosted liquidity at the height of the crisis. However, this allocation demonstrated the inequality built into the global financial system. Based on current quotas, developed countries received 26 times more than Least Developed Countries, and 13 times more than all the countries of Africa combined. Emergency financing should automatically go to the neediest countries. Under the current system, it is widening inequalities.

At the same time, uncertainties and risks remain exceptionally high and are exacerbated by growing geopolitical and economic fragmentation.

The reversal of monetary policy in advanced economies has begun to expose weaknesses in the banking sector fueling fears that the price of taming inflation could be financial sector instability accompanied by a global recession. Policymakers have acted swiftly to quell fears with liquidity measures. As so often is

the case when uncertainty is high, international financial markets tighten disproportionately for many developing economies thereby exacerbating issues of already heavy debt-burdens and overhangs. The number of low- and middle-income economies suffering from severe debt problems has risen sharply since 2020 and remains highly elevated, --and international debt relief efforts continue to be inadequate.

Financial and fiscal pressures are in many of the poorest countries accompanied by depreciating currencies, a cost-of-living crisis, sociopolitical tension, and a rising cost of dealing with the impacts from climate change. The UN and the World Bank have warned that per capita growth is set to slow significantly in emerging markets and developing economies in 2023-2024, especially hurting the poorest where poverty rates could go up.² Similarly, the IMF has revised their growth projections for low-income countries showing that the current outlook threatens to reverse a decades-long trend of converging living standards, and that reestablishing convergence will require an estimated $440 billion through 2026.³ The poorest and most vulnerable countries face the heaviest development impacts associated with high levels of global economic and financial uncertainty.

The climate crisis poses the greatest international coordination challenge of our lifetimes. As the IPCC has made crystal clear in their latest report, actions are not commensurate with agreed global targets to limit warming to 1.5°C, as end-of-century warming is on course for 3.2°C under implemented policies, and 2.8°C under Nationally Determined Contributions (NDC) targets. Climate transitions will require significant additional sums of climate finance for mitigation and adaptation for countries to make the necessary investments, without having to compromise on other fronts of sustainable development. Adaptation funding is especially needed in many of our poorest and most vulnerable countries as they are low emitters, but among the worst affected by the impacts of climate change.

The United Nation’s SDG Stimulus Plan to Deliver the 2030 Agenda (the SDG Stimulus)⁴ calls for a target of $500 bn in additional financing per year, aimed at mitigating the effects of cumulative shocks and providing developing economies with better access to long-term and affordable finance for sustainable

² The World Bank estimates that income per capita from 2023-2024 is expected to average just 1.2%, a rate that could cause poverty rates to raise. See World Bank Global Economic Prospects Report 2023 and the UN World Economic Situation and Prospects Report 2023.
³ https://www.imf.org/en/Blogs/Articles/2023/03/31/the-time-is-now-we-must-step-up-support-for-the-poorest-countries
development, including dealing with climate change. Implementing the SDG Stimulus will require urgent action from the G7 and G20 countries and the multilateral system at large.

More specifically, the SDG Stimulus puts forward three action areas for the international community: 1) tackle the high cost of debt and risks of debt distress; 2) massively scale up affordable long-term financing for development; and 3) expand contingency financing to countries in need.

**Action area 1: Tackle the rising risks of debt distress and high cost of debt**

Sovereign debt has reached critical levels with more than a dozen countries in technical default or on the brink of default. Policy makers are in many countries facing stark choices between paying creditors and fulfilling obligations to their citizens, postponing the long-term investments necessary for continued progress on sustainable development.

According to the IMF, about 15 percent of low-income countries are already in debt distress and another 45 percent face high debt vulnerabilities. And about a quarter of emerging economies are at high risk and facing “default-like” borrowing spreads. For many countries key debt-burden indicators are back at, or approaching, levels last seen during the start of the last major international debt relief, the heavily indebted poor countries initiative.

The G20 Common Framework for Debt Treatments (CF) has been slow in addressing debt restructuring, foremost on the issue of creditor coordination amongst and between official and commercial creditors. Despite broad agreement on the shortcomings of the CF, the G20 has not yet found a consensus on the way forward and additional steps are needed to speed up debt resolution. The SDG Stimulus calls for both immediate and longer-term debt actions.

Immediately, the G20 should conduct an independent review of the Debt Service Suspension Initiative (DSSI) and the CF with the aim of putting in place an improved multilateral debt relief initiative to support debt payment suspensions, debt exchanges and/or haircuts, including a clear mechanism to include private creditors in official debt relief efforts. Among possible debt relief instruments considered should be debt for SDG and climate swaps and greater use of risk-sharing debt instruments such as state-contingency clauses. At the same time, the international community must work towards developing long-term solutions.

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6 It is estimated that in 2022 total debt service on public external debt alone is higher than 20 percent of total government revenue for 25 developing economies (see details in Box 1 of the SDG Stimulus). This has not been the case since the year 2000 which also marked the early years of the HIPC initiative.
term comprehensive and structural solutions to sovereign debt challenges. In addition, debt sustainability analysis should distinguish better between liquidity and solvency risk and should also include scenarios of better access to long term affordable finance and SDG spending needs. At the same time, concrete steps must be taken toward a permanent mechanism to address sovereign debt distress as called for in the Addis Ababa Action Agenda.

**Action area 2: Massively scale up affordable and long-term financing for development**

In conjunction with improved debt management, the SDG Stimulus calls for a massive boost in investment on SDGs in developing countries, including financing climate action. Here, public development banks (PDBs), including multilateral development banks (MDBs), are uniquely positioned to play a more important role.

MDBs could, with stronger capital bases and better use of existing capital, increase lending from $100 billion per year to at least $500 billion per year. Special drawing rights (SDR) rechanneling should feature as part of the discussion on MDB reform. Several promising proposals have been put forward on how to leverage SDRs (or other reserves) -- for instance by using them as MDB hybrid capital -- without compromising their reserve asset function.

MDB reform, including capital infusions, should aim at improving lending terms. First, by offering ultra long-term funding with significant grace periods to allow time for large scale SDG-related investments to yields results in terms of contributing to growth, wellbeing and productivity from human capital investments, and savings from investing in resilience to shocks. Second, by offering low interest rates which is especially important during periods of global financial tightening to act counter-cyclically. Third, by making use of state-contingent debt clauses that automatically provide fiscal breathing space when hit by exogenous shocks. Fourth, by providing a greater share of lending in local currency as this would contribute to lowering the borrower’s debt risk profile.

Similarly, there is also scope for many national development banks to increase lending. The SDG Stimulus also calls for strengthening the system of public development banks, including greater cooperation between MDBs, as well as between MDBs and PDBs.

Many developing economies will still need grants to support financing of the SDGs. Official development assistance (ODA) has failed to keep pace with rising needs and demands from the COVID-19 crisis and the impacts of the war in Ukraine. ODA remains at less than half the agreed target of 0.7 per cent of donor
country gross national income. Meeting ODA commitments would provide over $150 billion per year in stimulus for the SDGs.

Finally, a new approach to blended finance is needed to draw in more private funding for sustainable investments. This includes a focus on development impact rather than bankability, use of non-concessional loans, and structures where the public sector can share both risks and rewards fairly.

**Action area 3: Expand contingency financing to countries in need**

The current international monetary and financial system exposes developing countries to sudden changes in financial market sentiment and high volatility of capital flows. The SDG Stimulus includes steps to strengthen the global financial safety net and address immediate liquidity needs to help countries improve their crisis response.

Developing countries drew down an estimated $379 billion in reserves in 2022, almost double of the amount of SDRs they received in the 2021 allocation. The SDG Stimulus calls for more ambitious international efforts in rechanneling SDRs at scale and ambition.

The international community should also continue to explore or accelerate the implementation of other mechanisms that can increase liquidity and boost available resources for sustainable development. Initiatives such as the IMF’s Resilience and Sustainability Trust, the Food Shock Window and the Loss and Damage Fund agreed to at COP27 are promising initiatives --keeping in mind that new instruments should be quick disbursing, with low interest rates, and parsimonious conditionality. Regional mechanism can be explored to enhance liquidity and increased global access to Central Bank swap lines could help calm markets in periods of volatility.

In the long-term, the international financial architecture could also be made more shock-absorbent and resilient by ensuring that financial resources can automatically be provided to countries during periods of shocks where capital often rush into assets denominated in hard currencies. This could include integration of state-contingent and disaster clauses into loan contracts, as well as mechanisms to enable countercyclical issuance of SDRs in a more automatic or timely manner.