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No transformation, just business as usual

Financing for the 2030 Agenda is missing its targets

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Bonn, 8 July 2019. In September 2019, heads of state and government are set to meet at the UN General Assembly to assess progress made on the global Sustainable Development Goals (SDGs) for the first time. The 2030 Agenda for Sustainable Development was adopted in September 2015 and applies to all countries. The SDG Summit will also look at how the 2030 Agenda is financed. Three recent studies by the OECD, UN and IMF paint a sobering picture of the current state of affairs, particularly in developing countries.

The OECD data shows that the increase in financial resources that was envisaged in order to achieve the SDGs has yet to be forthcoming. Quite the reverse, in fact: official development assistance is stagnating, while foreign direct investment and private lending are falling. The only thing steadily rising is remittances from migrant workers, which in 2018 exceeded total development assistance from OECD countries by around three to one.

The UN bemoans the fact that the necessary transformation of the global financial system from short-term to long-term financing and sustainable investment is making scarcely any progress. Despite innovative instruments such as green bonds, impact investing and sustainable financial investments, too much capital is still being put to unsustainable uses. Of the estimated USD 200 trillion moving around on the global financial markets, only a very small proportion is flowing into explicitly sustainable investments and even less into developing countries.

In its study on financing the SDGs, the IMF points out that public development investment is actually falling rather than rising: in developing countries, public investment as a percentage of gross domestic product (GDP) fell from roughly 3 per cent in the 1990s to less than 1 per cent in 2018, if the depletion of the public capital stock is taken into account. This was due to increasing expenditure, for example on food and energy subsidies, and, more recently, on debt servicing as well.

In principle, middle-income countries such as Indonesia could use their own resources to close the SDG financing gap – which the IMF estimates at around 4 per cent of GDP for this group of countries – if they grew their tax revenues accordingly. This is something that low-income countries such as Rwanda will not be able to manage as their financing gap is some 15 per cent of GDP and can only be closed with the aid of external financing.

Private financing is often seen as a way out of this problem. The approach known as “blended finance” involves mobilising more private capital for development purposes supported by public subsidies. The multilateral development banks are working hard to finance infrastructure in developing countries increasingly with private capital. Results to date have been modest, with private capital only playing a significant role in the energy and transport sectors.

The IMF’s observation regarding the scope that middle-income countries have to mobilise their own resources is therefore good news. Although tax revenues have already risen in many countries, they often make up nearer 10 than 20 per cent of GDP, as in India or Indonesia for example. This is far too little to undertake sufficient investment in sustainable infrastructure, healthcare and education.

So, what does that mean?

In developing countries, the SDGs cannot be financed predominantly by the private sector or by loans. In middle-income countries, the middle and upper classes need to be more involved in financing public services. International cooperation on combating tax avoidance and tax evasion has enjoyed little success to date. Tax havens, a tax avoidance “industry” driven by banks and law firms and a deficient tax system for international companies require a concerted effort if public revenues are to meet the requirements of SDG financing.

Private financing is better suited to advanced countries because private-sector financial institutions shy away from the risks in developing countries despite government incentives. The need for subsidies via blended finance mechanisms is often great and difficult to calculate. Most of the USD 200 trillion already mentioned that is moving around the global capital markets will continue to be invested in advanced countries. If this persists in the same vein, there will also be a question mark over SDG financing. A number of central banks have already recognised the systemic risks of unsustainable private financial investments and are demanding greater risk transparency from banks and big business. There are signs of a shift in strategy towards sustainable investments in the private sector, including amongst insurance companies. Major financial firms such as BlackRock are taking sustainability more seriously but remain driven by their need for short-term returns. Meanwhile, the EU Commission has approved an action plan for a sustainable financial system in Europe.

Both elements – public revenues and the sustainability of the financial system – are important for financing the SDGs. And both now require a change of gear from “business as usual” to “transformation under way”.

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