IFAD POLICY BRIEF

IFAD Investing in rural people

A task list for multilateral agencies: the possibilities of Bridgetown

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Against a backdrop of a polycrisis, the world is failing to mobilise the scale of finance needed to deliver on the Paris Agreement and the SDGs.

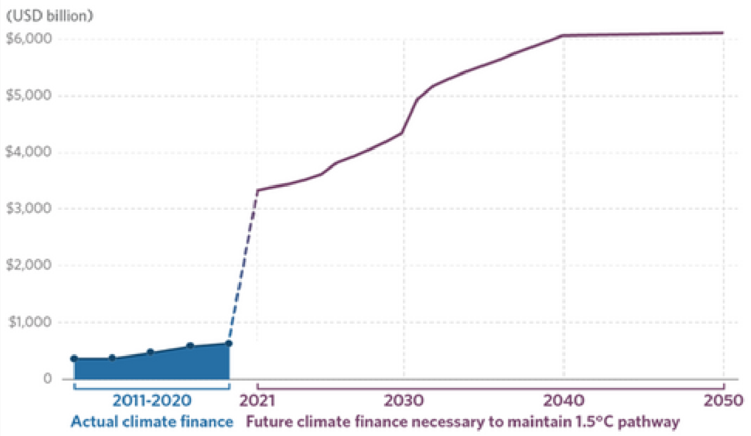
Further countries are facing high interest rates making borrowing more burdensome. Bringing into focus the challenge of equitable and sustainable development for all, in this IFAD Policy Brief we consider the Bridgetown Initiative and propose a task list for multilateral development agencies, offering potential for reform.

I. SHOW ME THE MONEY: THE ELUSIVE CLIMATE GOAL

In 2020, USD 83.3 billion[1] in climate finance was channelled to developing countries. This fell far short of the support countries require to meet their climate goals in Nationally Determined Contributions (NDCs). CPI estimates, to meet our climate objectives, by 2030 annual climate finance must increase by at least 590% to USD 4.35 trillion (see Figure 1)[2].This gap is becoming more consequential because today more than one-third of countries are either at risk of being indebted or at risk of defaulting[3],[4]. High interest rates mean that most countries are reluctant to continue borrowing on unfavourable terms to address the climate challenge.

In response, Prime Minister Mia Mottley of Barbados proposed the Bridgetown Initiative in July 2022. It contains amongst others, calls for changes and new mechanisms that can provide financing to address the climate and development crises, to address immediate needs, while also setting out a plan for systems change

Figure 1. Global tracked climate finance flows and the average estimated annual climate investment need through 2050 (Global Landscape of Climate Finance 2021)



1. COP27 changes climate finance architecture with loss and damage decision, urges MDBs to transform | Climate & Development Knowledge Network
2. Global Landscape of Climate Finance 2021, Climate Policy
3. The Economics of Climate Change: The Stern Review. 2006. HM Treasury .
4. IMF, 2023. Countries Should Act Now to Limit Rising Risks From Corporate Distress

to transform the financial system, and specifically the multilateral lending system. This is important because as the Global Crisis report tells us, nearly a quarter of a billion people today are now facing acute hunger or worse. And this is set to worsen before it improves with climate change, interest rates and conflict multiplying to make this crisis worse.

Mottley calls for enacting a debt 'freeze' when a disaster strikes and expanding the eligibility for lending below market rates for climate vulnerable countries. She also stresses the need for MDB reform: MDB alignment with Paris Agreement Article 2.1c on facilitating financial flows to reach climate goals is required.

Importantly, these calls are not new and more recently are reflected in a report of the Independent High-level Expert Group on Climate Finance[5].

II. WHAT AILS THE GLOBAL FINANCIAL SYSTEM?

The multilateral system is fragmented and has redundancies built into it. Over 40% of official development assistance (ODA) is channelled through multilateral development organisations. This is fragmented across hundreds of organisations with overlapping mandates but diverse objectives, blurring roles and responsibilities. The Independent Review of the MDB's Capital Adequacy Framework (CAF) reported that from 2015 to 2020, 42 multilateral organizations were actively involved in agriculture, forestry, and fishing; 45 agencies focused on health, while another 45 addressed industry and mining.

Funds being channelled to these organizations are increasingly being earmarked to address specific issues. This leads to further siloes.

The UN system receives 72% of the earmarked funding compared to other multilateral organisations, and of this, 28% is specific to a particular project type.

MDB risk appetite is too low: The independent CAF report commissioned by the G20 also finds that multilateral lenders are constrained by capital-adequacy requirements that place excessive limits on how much risk they can assume. As a result, capital is underutilized at a time when the world needs it the most. The report recommends a series of measures including valuing callable capital and an accurate risk assessment that would enable MDBs to increase their lending capacity. This reform has the potential to increase MDBs' lending capacity by hundreds of billions of dollars without hurting their AAA-ratings, whilst also providing developing countries with sorely needed liquidity.

MDBs also neglect to account for their preferred creditor treatment. Preferred creditor status means that they are repaid first and ahead of other creditors in sovereign-debt repayment. We know that borrowing countries are 3-4 times less likely to default on sovereign loans owed to multilateral institutions than they are on sovereign debt owed to commercial lenders. MDBs' expected credit losses are 14 times lower than their commercial counterparts. Currently MDBs' existing capital-adequacy frameworks underestimate the value of this preferential status, as do the methodologies of credit-rating agencies.

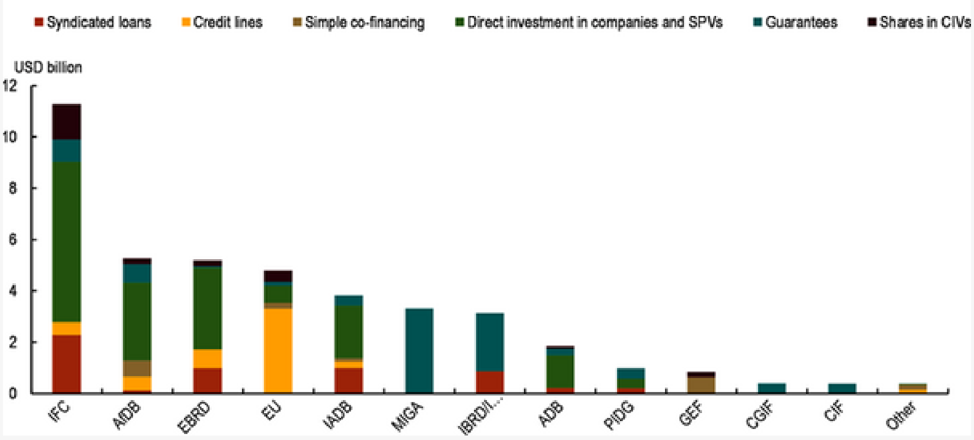
Table 1. Number of active multilateral entities by thematic sector (2015-2020) (Source OECD, 2022). Calculations based on OECD Creditor Reporting System, with green-red, lowest to highest.
Multilateral development finance in context. Multilateral Development Finance 2022, OECD iLibrary.

Sector	MDBs	Vertical funds	UN	Other	Total
Action Relating to Debt	7	0	1	4	12
Agriculture, Forestry, Fishing	19	5	13	5	42
Banking & Financial Services	20	5	10	6	41
Business & Other Services	15	2	11	5	33
Communications	17	2	9	5	33
Development Food Assistance	7	1	12	2	22
Disaster Prevention & Preparedness	14	5	13	3	35
Education	17	3	15	5	40
Emergency Response	13	1	15	4	33
Energy	19	6	12	6	43
General Budget Support	6	1	5	3	15
General Environment Protection	15	5	15	6	41
Government & Civil Society	17	5	17	8	47
Health	18	3	18	6	45
Industry, Mining, Construction	20	5	14	6	45
Other Social Infrastructure & Services	17	5	15	6	43
Population Policies/Programmes & Reproductive Health	11	3	15	3	32
Reconstruction Relief & Rehabilitation	13	2	12	2	29
Trade Policies & Regulations	15	1	8	4	28
Transport & Storage	19	4	7	5	35
Water Supply & Sanitation	17	5	14	5	41

5. Finance for climate action Scaling up investment for climate and development Report of the Independent High-Level Expert Group on Climate Finance, 2022.

MDBs are not mobilising private finance sufficiently: Currently, MDBs are not sufficiently promoting private sector financing. While many development banks aim to mobilize private finance, they could use a wider array of instruments, such as portfolio level guarantees and hybrid index insurance products, to attract more private capital to their projects. Information asymmetries between private investors and developing countries present challenges in connecting bankable projects with much-needed capital. MDBs can address this gap by de-risking investments and providing technical assistance at scale and speed for developing bankable projects.

Figure 2. Private finance mobilised by multilaterals in 2020 (Source OECD, 2022)
Financing from the multilateral system. Multilateral Development Finance 2022, OECD iLibrary.



III.WHAT CAN THE MULTILATERAL DEVELOPMENT BANKS DO?

- **Be the assurer: Strengthen support for countries with limited administrative and institutional capacity:** Where countries face administrative and institutional capacity constraints, multilateral development banks (MDBs) can be a crucial intermediary. This entails taking on the role of quality assurer: assuring the proper use and management of the proceeds derived from additional Special Drawing Rights (SDRs), which, in specific contexts, can be integrated with MDB loans and grants. MDBs could also partner with various ministries, including Finance, Infrastructure, Agriculture, Water and other relevant bodies, and lend policy guidance on use, management and reporting for SDRs. This support could help countries strategize the use of proceeds to boost their rural economies. More specific actions could include offering capacity building sessions and technical consultations to enhance the strategic planning capabilities of these ministries with a focus on low-emission climate-resilient development.

- **Help debt restructuring through food systems:** MDBs can significantly bolster the success of debt restructuring processes. By focusing on low emission climate resilient developmental transitions, conducting fiscal policy analyses to understand trade-offs, and providing evidence-based policy advice, MDBs can ensure that countries maintain authority over the design and subsequent use of additional fiscal space. Using a climate- development-centric evaluation framework, MDBs could assist these countries in pinpointing the most influential interventions that promote fiscal resilience and GDP growth within the rural economy. Most countries are keen to take on policy changes so long as they help to ensure significant change and trade-offs are well understood. MDBs could also develop tailored risk assessment and financial modelling tools that countries can use to make informed decisions about debt restructuring, including through debt-for-adaptation and debt-for-nature swaps.

- **Streamline public-private partnerships through platform-based approaches:** MDBs could facilitate the creation of platform-based approaches for partnerships with the private sector. Such approaches could significantly streamline the process of developing bankable projects by offering end-to-end services to developing countries. These in turn could range from concept development to financing portfolio-level blended finance solutions bringing together institutional investors, international commercial banks, and philanthropic organizations in a focused way. Such a platform approach eschews a piecemeal strategy in favour of a holistic view, can expedite the progression of projects, reduce transaction costs, and increase efficiency of investment processes that exploit differentiated risk appetite.

- **Champion just transitions while focusing on increased financing:** The implementation of the Bridgetown Initiative holds substantial implications regarding advocating for a just transition. MDBs must persist in ensuring that the most vulnerable communities have access to climate finance. Less than 10 per cent of climate finance goes to adaptation and just 2.5 per cent went to agriculture, forestry and other land uses in 2020. Integrating just transition principles into financial mechanisms is critical. These include boosting social protection measures for the most vulnerable in society, ensuring social dialogue with all relevant parties, investing in community renewal as well as jobs, decent work, education and training, amongst others.

- **Lead data driven assessments of the Bridgetown Initiative:** Implementation of the Bridgetown Initiative necessitates appropriate measurement of progress and impact. MDBs could spearhead this effort by designing a robust yet straightforward performance matrix. Currently, no such tool exists, and MDBs' leadership in this endeavour, complete with Key Performance Indicators (KPIs), could be critical. This will not only measure the effectiveness of the Bridgetown Initiative but also promote transparency and accountability, contributing to the Initiative's overall success.

Overall, the Bridgetown Initiative presents a unique opportunity for the multilateral system to reform. By adapting to the new financial frameworks and catering to differentiated risk appetites, the pressing challenges of our time such as climate change, debt crises, and global inequality, can be tackled. It calls for bold and innovative action from Multilateral Development Banks, Ministries of Finance in G20 countries, and other key stakeholders to mobilize the required resources, create enabling environments, and foster sustainable development. But this will require political will and urgent action if we want to ensure a collective commitment to a more resilient, equitable, and sustainable future for all.

IFAD
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International Fund for
Agricultural Development
Via Paolo di Dono, 44
00142 Rome, Italy
Tel: +39 06 54591
Fax: +39 06 5043463
Email: ifad@ifad.org
www.ifad.org

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Dr. Jyotsna Puri

Associate Vice President, SKD, IFAD

Jahan-Zeb Chowdhury

Lead Technical Specialist - Environment & Climate Cluster Coordinator, IFAD