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Intergovernmental Group of Experts on Financing for Development

Second session

Geneva, 7–9 November 2018

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II. Annotations

Item 1

Election of officers

1. In accordance with established practice, it is suggested that the Intergovernmental Group of Experts on Financing for Development elect a Chair and a Vice-Chair-cum-Rapporteur.

Item 2

Adoption of the agenda and organization of work

2. The Intergovernmental Group of Experts on Financing for Development may wish to adopt the provisional agenda reproduced under chapter I above.
3. It is proposed that the opening plenary meeting of the second session of the Intergovernmental Group of Experts, which will start at 10 a.m. on Wednesday, 7 November 2018, should be devoted to procedural matters (items 1 and 2) and opening statements. The closing plenary meeting on Friday, 9 November 2018, will consider the adoption of the report of the second session of the Intergovernmental Group of Experts to



the Trade and Development Board, including agreed policy recommendations, and the provisional agenda of its third session (agenda items 4 and 5, respectively), to be held in the final quarter of 2019, as stipulated in the terms of reference for the Intergovernmental Group of Experts (TD/B(S-XXXI)/2, annex IV, II. 6).

4. The remaining meetings will be devoted to substantive discussions of issues under agenda item 3.

Documentation

TD/B/EFD/2/1

Provisional agenda and annotations

Item 3

Financing for development: Debt and debt sustainability, and interrelated systemic issues

5. At the first session of the Intergovernmental Group of Experts on Financing for Development, held on 8–10 November 2017, member States agreed that the topic of the second session should be debt and debt sustainability, and interrelated systemic issues (see TD/B/EFD/1/3, annex I).

6. Ten years after the global financial crisis, the global economy continues to exhibit an unhealthy dependence on debt. Between 2008 and the end of the third quarter of 2017, global aggregate debt stocks rose from \$142 trillion to \$230 trillion, more than three times the gross world product.¹ According to the Bank for International Settlements, the ratio of global debt to gross domestic product is now 40 per cent higher than at the onset of the global financial crisis.² The resultant fragility and sluggish growth performance of a highly financialized global economy have negatively affected developing country debt sustainability for some time, threatening to undermine the achievements of the relatively tranquil decade of the 2000s, during which many developing countries managed to stabilize and improve their debt positions due to a combination of international debt relief, a favourable external economic environment and consequent strong domestic growth.³ Although mixed data availability for many developing countries makes it difficult to produce precise data, it is estimated that their share in global debt stocks rose from 7 per cent in 2007 to 26 per cent in 2017.⁴ Alarm bells are now ringing about the dangers of a new systemic developing country debt crisis: Seventy low-income developing economies are eligible for concessional loans under the Poverty Reduction and Growth Trust of the International Monetary Fund. According to the Fund, of the 68 countries for which there are data, 7 are in default (up from 3 in 2015), 23 are at high risk of default (up from 15 in 2015) and 26 at moderate risk of default, down from 33 in 2015.⁵ Only 12 of these countries (17 per cent) are assessed to be at low risk of default, compared with 20 in 2015, and this does not include higher-income developing countries, known to be in debt distress or approaching that point.

7. Many of the specific features of growing debt vulnerabilities in developing countries are familiar from earlier developing country debt and financial crises in the 1980s and 1990s. Recessions in advanced economies, or more broadly, sluggish global aggregate demand, undermine developing countries' ability to service existing external debt. Increasingly large procyclical flows of cheap international credit, triggered by economic policy decisions in developed economies, cause financial and macroeconomic instabilities in developing economies; volatile commodity markets, themselves affected by financial

¹ Institute of International Finance, 2018, Global Debt Monitor Data, January 2018.

² G Tett, 2017, How we all became addicted to cheap debt, Financial Times, 20 October.

³ See International Monetary Fund, 2018, Macroeconomic developments and prospects in low-income developing countries, International Monetary Fund Policy Paper.

⁴ Institute of International Finance, 2018, Global Debt Monitor, available at www.iif.com/publication/global-debt-monitor/global-debt-monitor-February-2018 (accessed 27 August 2018).

⁵ International Monetary Fund, list of low-income countries with debt sustainability analysis that are eligible for the Poverty Reduction and Growth Trust as of 1 August 2018. The full list comprises 70 countries; data are not available for 2 of them.

instabilities, speculation and economic downturns, add to the turmoil. This time, these familiar issues are complicated by the high speed of developing countries' integration into volatile and largely unregulated international financial markets, sharply intensifying these economies' exposure – in both their public and private sectors – to often high market risks. Thus, for developing countries as a whole, the share of external public and publicly guaranteed debt owed to private creditors increased from 41 per cent in 2000 to over 60 per cent in 2017. But while not long ago, the amount of debt that even least developed economies could have sold to eager investors from abroad seemed almost limitless, international sovereign bond issuance in these economies rose from \$2 billion in 2009 to almost \$18 billion in 2014. The sudden reversal of net private capital flows to developing economies since 2014 has resulted in steep and widespread yield increases on international sovereign bond markets. Given also the high exchange rate risks associated with debt issuance in foreign currency, many Governments in developing countries have relied more strongly on domestic public debt issued in local currency. This, however, comes with its own risks, such as inflationary pressures and maturity mismatches, arising from the prohibitive costs of long-term government securities in most developing countries. Moreover, where foreign investors hold large positions in domestic bond markets, exposure to volatile global financial and economic conditions in host markets remains high. Not only are the as yet shallow financial and banking systems of developing countries insufficiently equipped to manage such risks, the systemic nature of some of these risks poses substantial policy challenges, even for Governments of developed economies. At present, a core concern in this regard is sharp increases in the debt of non-financial corporate sectors in developed and larger emerging markets alike. By some estimates, globally, over one third of non-financial corporations are now considered highly leveraged, with gearing or debt-to-earnings ratios of 5 and above.⁶

8. These and other challenges to developing country debt sustainability are all the more worrying, since debt instruments are, in principle, an important element of any development financing strategy. To the extent that such debt instruments are used to expand production capacities, they contribute to boosting income and the export earnings required to service the debt. But where debt primarily results from short-term private capital inflows that are mostly unrelated to the long-term financing of productive investment and trade in the real economy, it can trigger asset bubbles, currency overvaluation, superfluous imports and macroeconomic instability. Claims on the debtors can then quickly exceed their capacity to generate the required resources to service their debt. Avoiding such debt traps, while also leveraging the potential opportunities provided by financial innovation in the international financial markets, is a key challenge faced by developing countries in their quest to mobilize both domestic and international resources for the financing of development, including with regard to achieving the Sustainable Development Goals and the 2030 Agenda for Sustainable Development.

9. The first substantive meeting, to be held on 7 November 2018, will explore the nature and causes of current debt sustainability vulnerabilities in developing countries, in the context of their overall need for developmental finance. While debt instruments are important, they are not the only means of financing development. How to use them most appropriately needs, therefore, to be discussed in the context of alternative ways to finance development. The remaining substantive meetings of the second session of the Intergovernmental Group of Experts will focus on international, regional and national policy options to address rising developing country debt vulnerabilities, within the wider financing of development and based on the agreed guiding questions for this session:

(a) How can current debt vulnerabilities in developing countries be mitigated and developing country sovereign debt and financial crises prevented?

(b) How can sovereign debt financing, both external and domestic, be leveraged successfully for sustainable development in the future?

⁶ S and P Global, 2018, Global corporate leverage, trends 2018: Debt high, defaults low – Something's gotta give. 5 February.

(c) What institutional, policy and regulatory changes are required at the international level to ensure that global economic governance structures better support the use of responsible debt financing, by borrowers and lenders, for sustainable development?

(d) How can existing frameworks and tools be improved to ensure effective, fair and transparent sovereign debt crisis resolutions?

10. To facilitate discussion, the UNCTAD secretariat will prepare a background note that reviews recent developments relating to rising vulnerabilities in developing country debt sustainability and main policy options to mitigate these, based on the aforementioned guiding questions. In addition, experts are encouraged to prepare articles on the issues under discussion. These papers will be made available prior to the second session of the Intergovernmental Group of Experts in the form and language in which they are received.

Documentation

TD/B/EFD/2/2

Financing for development: Debt and debt sustainability, and interrelated systemic issues

Item 4

Provisional agenda for the third session of the Intergovernmental Group of Experts on Financing for Development

11. Acting in its capacity as the preparatory body for its third session, the Intergovernmental Group of Experts on Financing for Development is expected to agree on the provisional agenda for its next session, informed by the report of the Inter-Agency Task Force on Financing for Development, entitled “*Financing for Development: Progress and Prospects 2018*”, and guided by the deliberations of the Forum on Financing for Development follow-up of the Economic and Social Council.

Item 5

Adoption of the report of the second session of the Intergovernmental Group of Experts on Financing for Development

12. In accordance with the terms of reference for the Intergovernmental Group of Experts on Financing for Development, agreed policy recommendations, based on its discussions and deliberations, will be prepared for adoption and submission to the Trade and Development Board.

13. Under the authority of the Chair of the second session of the Intergovernmental Group of Experts, a report of the meeting will be produced and submitted to the Trade and Development Board for consideration. The Intergovernmental Group of Experts may wish to authorize the Vice-Chair-cum-Rapporteur to finalize the report after the conclusion of its second session.

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