# Challenges and Opportunities in Financing for Development

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# Intergovernmental Expert Group on Financing for Development

"Support UNCTAD and the Economic and Social Council in formulating contributions to the Inter-Agency Task Force on FfD"

Two guiding questions:

1) **<u>Domestic resources</u>**: what can be done to enhance the mobilization of domestic public resources for development in developing countries?

2) **<u>International cooperation</u>**: how can international development cooperation maximize its contribution to achieving the 17 SDGs?

# UNCTAD’s T&D Report 2017
# Beyond Austerity: Towards a Global New Deal

- UNCTAD’s 2017 report already presented a comprehensive analysis of challenges and opportunities for growth and development
- In a context of slow growth and low real interest rates, one of the main challenges for development is the uncertainty of effective demand
- Financial structure can help in mitigating risks, but it does not compensate for insufficient expected demand
- Some form of autonomous demand growth has usually been necessary for structural change

# Two views, one problem

- We have a demand problem: Y= C+G+I+X-M
- We have a supply problem: Y=f(K,L)
- Economic history shows that both things are interrelated (Kaldor-Verdoorn laws, hysteresis, path dependence, etc)
- Even the mainstream NK consensus is that demand is the most pressing problem (Summer's secular stagnation)
- In face of idle or sub-utilized resources, what can be the demand impulse in different countries or situations?

# Usual types of demand-led expansion

- **Export-led growth**: can be very successful for one country, especially small economies, but does not function globally (fallacy of composition).
- **Government-led expansion**: investment boom pushed by infrastructure, technology and other autonomous demand (green Keynesianism?)
- **Financial bubbles**: debt-fueled expansion of private demand based on expected capital gains
- **Income redistribution**: once-off income transfers in cash and services to reduce poverty and inequality (UBI, ELR, universal health care, etc)

# Can better financial instruments alone do the trick? Taxonomy of investment projects

| | Low FX risk | High FX risk |
|---|---|---|
| Low demand risk | Proper financial instrument is sufficient | Currency mismatch blocks investment (FX hedging is needed) |
| High demand risk | Even favorable financial conditions cannot compensate for demand uncertainty | No financial instrument capable of reducing uncertain demand and price volatility |

# Example: Public-Private Partnerships in Brazil

PPPs were thought as a mixed solution, in which the government enables private investment taking part of the demand risk

So far the Brazilian experience indicates that

- PPP works in low-scale brownfield projects with certain demand and no currency mismatch (maintenance of public facilities)
- PPP does not work in large-scale greenfield investments, due to high demand uncertainty (multiyear government budgets) and exchange-rate volatility

# Is there still any role for active fiscal policy?

- Government investment in infrastructure to build capacity ahead of demand and generate jobs
- Traditional cost-benefit analysis of the social rate of return can justify more investment temporarily financed by debt or taxes even under Ricardian equivalence
- But after almost 40 years of predominantly "neoliberal" views of public policy, today there is only cost analysis (zero or no benefit from government initiatives by assumption)

# What are the risks of a demand-led expansion?

| Risk | Problem | Solution |
|---|---|---|
| Inflation | Full capacity or sectoral bottlenecks | Investment to accelerate productivity + inflation targeting |
| Balance of payments | Excessive current account deficits and financial fragility | Floating ER + high international reserves of liquidity assistance |
| Public debt | Excessive primary deficits and fiscal fragility | Balanced budget multiplier and/or expenditure switching |
| Private debt | Excessive leverage (private Ponzi process) | Prudential regulation and directed credit |

# And there is also the risk that self-reinforcing inequality blocks development

High inequality comes together with market-power concentration and tends to reinforce itself

- Increasing monopolist rents (ICT)
- Regressive tax-transfer policy

Conservative narratives (post-truths)

- Blame the immigrants (US, EU, UK, etc)
- Blame the left or “populistas” (Latin America)

More transparency and accountability is always necessary, together with proper cost-benefit analysis

# The Prisoner's Dilemma and International cooperation

| Problem | Coordinated Solution |
|---|---|
| Competitive wage repression to gain competitiveness in face of globalization and new ICT | Antitrust policies and increase in labor power together with labor flexibility |
| Tax wars to attract and maintain private investment and production | More progressive personal taxation and less corporate tax evasion (BEPS) |
| Competitive financial liberalization to attract short-term foreign capital | Prudential regulation to attract long-term foreign capital + taxation of one-way financial bets with derivatives |

# Challenges and Opportunities

High inequality and real-wage stagnation calls for more active fiscal policy, with transparency and accountability.

Global warming requires a green Keynesianism, which is economically equivalent to war (creative destruction of capital), but with no human losses.

New ICT and international integration allows more coordination in regulation, taxation and financial issues (cooperation vs isolation at least in information)

Can a multipolar world foster independent “Marshall Plans” by the major blocks? What can be the UN role in this? Start with pilot cost-benefit analyses!

# Suggestions of topics for case or pilot studies by the UN (applied economics)

- The dynamics of the balanced-budget multiplier in the 21st century
- Reduction of FX risk through multilateral initiatives (Global fund, hedging facility, etc)
- Potential job creation by green projects around the world
- Financial regulation of negative externalities coming from the derivatives’ markets
- Reduction in inequality by income (UBI vs ELR) and services’ transfers (health, education, etc)
- Immigration, growth and development