CHAPTER 5

Policies to enhance the development impact and effectiveness of external financial resources

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A. Strengthening State capacity to steer structural transformation and its financing

1. Main issues

The Addis Ababa Action Agenda envisions the development process and the mobilization of the corresponding financial means along the following lines: countries have a responsibility to lead the national development process; countries should have national ownership of development; countries need to mobilize the resources required to finance the process; and the international community commits to supporting countries in their development, including with regard to its financing. The Agenda states that "cohesive nationally owned sustainable development strategies, supported by integrated national financing frameworks, will be at the heart of our efforts" and reiterates that "each country has primary responsibility for its own economic and social development" (United Nations, 2015b, para. 9). The Agenda thus implies a central role for States in steering the pursuit of the Sustainable Development Goals and in the mobilization of the financing required to provide the investment and current spending needed to achieve the Goals. Domestically, key elements in the implementation of the 2030 Agenda include capable Governments and public institutions, real partnerships and the formulation of country-specific plans and road maps to achieve the Goals and uphold long-term sustainability. This raises the question of the capacity of States to take on the responsibilities assigned to them.

State capacity is crucial in several ways. First, the 2030 Agenda assigns responsibility for the implementation of the Goals to States. The breadth and depth of the Goals and their indicators presuppose, and demand, a high degree of State capacity, required to design and put in place public policies in the economic, social and environmental fields, as part of long-term development strategies. This includes analytical, planning and financing skills, as well as the capacity to mobilize the necessary resources and monitor and evaluate policy implementation. Development-related policymaking comprises the design of long-term development plans, the formulation of clear national development strategies and the implementation of development policies. It therefore also requires building efficient institutions and the necessary bureaucratic capabilities that can mobilize the political, economic and financial resources required to roll out such development projects. Second, achieving the Goals requires the structural transformation of an economy, as previously emphasized in The Least Developed Countries Report (see, for example, UNCTAD, 2014b). In the context of underdevelopment, this transformation can best be achieved by means of the stewardship of a developmental State, that is, "a State whose ideological underpinnings are developmental and one that seriously attempts to deploy its administrative and political resources to the task of economic development" (UNCTAD, 2009, p. 29). This requires the capacity to design and implement structural, rural and industrial policies aimed at transforming the productive structure of the economy according to a normative concept of structural transformation (see chapter 1). Third, there is a link between State capacity and its ability to deliver on human rights in general and, more specifically, on the right to development. The United Nations High Commissioner for Human Rights states that "reforming policy with a people-centred approach means taking concrete action to strengthen State role and responsibilities to secure freedom from fear and want" (Bachelet, 2019).

The Goals assume, and demand, a high degree of State capacity

The structural transformation imperative is particularly strong in LDCs, most of which are in the initial phases of the process of transformative change. Therefore, the hurdles to be overcome are the highest in LDCs. Economic growth helps transition away from aid dependence, and spurring structural transformation remains the key long-term solution to redressing primary commodity dependence, boosting the development of productive capacities, improving competitiveness and enhancing domestic resource mobilization. Achieving this goal entails a development-friendly macroeconomic policy framework (UNCTAD, 2018c). There is a reciprocal influence between the level of State capacity and the stage of socioeconomic development (Besley and Persson, 2009; Besley and Persson, 2011; Dincecco, 2017; Singh and Ovadia, 2018). Thus, in general terms, State capacity in LDCs is constrained by the early phase of socioeconomic development in which most LDCs are located.

State capacity is understood in diverse ways in different contexts. It refers to the capacity of a State to ensure the sovereign functions of the State, such as enforcing security, peace and order and the rule of law. This is often the focus of assistance from donor countries to several LDCs (Kharas et al., 2014). However, such an emphasis on security tends to be reactive and short term, and does not entail a holistic and long-term vision of the development process. Security concerns require attention in several countries, yet the medium to long-term solutions of many of the problems that give rise to security concerns require the strengthening of States and their capacities in a holistic manner. This includes not only the sovereign functions of States but also, critically, their development functions. Aid and external assistance are therefore most effective if they help to build and strengthen developmental States, whether countries have serious security concerns or not at the time. This means building or strengthening State capacity to undertake economic planning, policy planning and execution (Singh and Ovadia, 2018; UNCTAD, 2009). It implies, critically, the bolstering of State capacity to mobilize financial resources for structural transformation, and development more broadly, from both domestic and external sources; the former is referred to as fiscal capacity (Besley and Persson, 2009; Besley and Persson, 2013; Bräutigam, 2008). This section focuses on State capacity to steer the process of structural transformation and, specifically, on the related need to mobilize and allocate the necessary financing for the investment and expenditure that can bring about structural transformation.

To achieve the structural transformation of their economies, LDCs need to mobilize and allocate the financing required for long-term investment in new productive sectors and activities, as well as investment in the technological and organizational upgrading of existing sectors and productive units. They also need to mobilize and allocate financing to current expenditure related to structural transformation. These financing requirements exist at the micro, meso and macro levels. State capacity is crucial to ensure, directly or indirectly, the availability at reasonable conditions of financing at these three levels. Ensuring availability at the micro level is the task of financial policies and, possibly, monetary policies. At the macro level, by contrast, it requires the capacity to put in place development-friendly macroeconomic policies, to formulate national development finance plans and strategies and to consider the options available to finance different areas, types of projects and Goals-related activities.

LDCs need proactive policies for national control over external support

LDCs need proactive foreign policy positions that cement creativity and national control over external support. The possibilities and instruments for negotiations between States and sources of external financing vary as a function of the different sources. For example, enhancing the development impact of worker remittances mostly depends on financial policies and regional and rural development policies, and the impact of policies is typically only indirect (UNCTAD, 2012). In addition, the contribution of FDI to the structural transformation of a host country largely depends on the innovativeness of the sectors and activities to which it is directed and on the linkages and embeddedness of multinational enterprises in the domestic economy of the host country. This, in turn, is influenced by the fiscal policies and policies on external investment in the host country as well as on the direct negotiations that often take place between prospective external investors and national, regional or local governments, resulting in deals or agreements. State capacity is therefore important in steering FDI towards developmental outcomes. In LDCs, State capacity is critical in influencing the contribution of official external financing to structural transformation, given the state of aid dependence as analysed in this report. The importance of the role of the State refers to the crucial role of traditional aid, other development finance associated with non-State actors under the new aid architecture and development finance channelled through South–South cooperation. States need to have the institutional capabilities and skills to assess and evaluate the development impact of alternative external financial flows, their financial, institutional and political costs and their explicit and implicit liabilities, in order to evaluate their relative merits.

Based on such assessments of alternative financial flows, LDCs need to negotiate with source institutions. The corresponding financial flows are typically the result of negotiations between source institutions and domestic recipient institutions and of the decision-making process, both of which determine priorities and where and how external official resources will be allocated (Whitfield and Fraser, 2010). This process shapes the terms and conditions under which external resources enter an economy, as well as the ensuing outflows in the form of factor payments, capital repatriation, etc. There is a virtuous circle between developmental leadership and a strong negotiating position vis-à-vis sources of external finance; governments that place a strong emphasis on development achieve a better level of human and economic development performance and thereby reach stronger negotiating positions (Whitfield and Fraser, 2010). Having a stronger negotiating position in turn allows Governments to negotiate better deals, that is, obtain external financing aligned with their national development priorities and with better conditions.

The importance of State capacity in LDCs has become even more critical in the context of the evolution of the aid architecture. As suggested in this report, this architecture has become more complex, less transparent and more difficult to deal with, given the increasing number of agents, instruments and financing modalities and the growing complexity, which often blurs the distinctions between concessional and non-concessional finance or between private and official funds, potentially hampering the adequate monitoring of different transactions. LDC institutional capacities are also faced with the growing complexity involved in dealing with unfinished progress with regard to the aid effectiveness agenda, in particular in terms of the persistent volatility and unpredictability of aid flows, the prevalence of tied or informally tied aid and fragmentation, among others. There is a risk that the advantages of accessing a broader range of financial instruments in international markets may be outweighed by capacity constraints in assessing, monitoring and managing the related risks. Moreover, given the modus operandi of the new aid architecture, the allocation of external resources often escapes the influence and awareness of recipient States, as decisions are often taken without involving the latter, often in the context of private sector engagement. Such developments raise the stakes in building capable and efficient LDC State institutions with the required skills to understand the trends in aid architecture and international flows of resources and that can implement strategies and put in place institutions to steer flows to their countries so as to enhance or maximize development impacts.

Despite the crucial role that States need to have in mobilizing and steering development finance, the new aid architecture is largely silent on recipient State agency and there is little evidence of systematic involvement by recipient countries in private sector engagement design or implementation. This not only undermines the role of LDC Governments in their national development but could further weaken their capacity. It could negatively impact their effectiveness in domestic resource mobilization, while also eroding the social contract between States and citizens that underlies taxation systems (Bräutigam, 2008). The need for inclusiveness is often interpreted as including an increased voice for domestic civil society and the private sector, yet the effectiveness and meaningful outcome of such a strategy rests on a responsive and capable State. Finally, on the domestic front, ensuring financing for sustainable development requires strengthening State capacity to mobilize domestic resources, including in particular institutions and bureaucracies to design and implement fiscal policies.

The new aid architecture could weaken State capacity

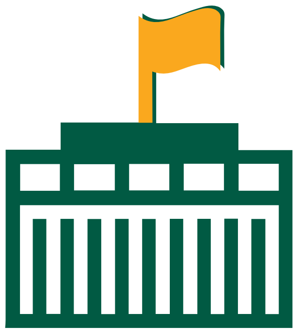
2. Policy options

In order to strengthen State capacity, in particular in the area of structural transformation and mobilizing the required financing, the following options may be considered by LDCs and their development partners.

a. Enhance development policymaking capacity in the least developed countries

LDC authorities need to adopt structural transformation as a major policy objective in the economic field. This should be the basis of major elements of development policymaking, namely, drawing up national development plans on the basis of domestic consensus-building, designing the related financial analysis and planning and mobilizing financial and political resources for such plans. UNCTAD has capacity-building activities related to strengthening LDC capacity in the field of development policy and implementation.[1] Given its track record in this field,

[1] For example, UNCTAD has launched a project on South–South integration and the Goals – enhancing structural transformation in key Belt and Road Initiative partner countries The project aims to strengthen developing country capacity in designing and implementing development policies in the context of South–South cooperation. In recognition of the fact that Governments in many partner countries of the Belt and Road Initiative face limitations in their capacity to effectively design, manage, coordinate, implement and evaluate strategic economic interventions that are the key policy levers of structural transformation, the project targets national institutional capacity-building in key policy areas. The project draws lessons from the development strategy of China, to assist the pilot partner countries of Ethiopia, Indonesia and Sri Lanka. In 2019, UNCTAD commissioned a series of papers that will discuss in detail the policy framework in China for aligning financial sector development, macroeconomic policy, trade, value chains and the digital economy with the overall objectives of structural transformation.



Strengthen
LDC State
capacities

UNCTAD should pursue this work in the medium and long terms.

b. Set up capacity-building and training programmes for least developed country policymakers in development planning, financial analysis and understanding of the aid architecture evolution

The beneficiaries of such training should be officials from central banks and ministries of planning and finance, as well as other ministries such as those of agriculture and industry. Greater attention by donors to building State capacity is a prerequisite of sustainable development and effective multi-stakeholder partnerships in development cooperation. In an unequal world, a narrative of equal partnerships can be counterproductive and/or disingenuous. Technical cooperation activities undertaken in the context of South–South cooperation can be particularly valuable, since partner developing countries have faced, in the not-so-distant past, development challenges similar to those faced at present in LDCs. Therefore, the institutional memory of successful development policymaking is available in many other developing countries, along with the potential for experience and knowledge-sharing (UNCTAD, 2011a). The financing for development component of such capacity-building should assist LDCs to build up human and institutional capacities for aid management and coordination.

LDC public sectors need assistance with regard to the implications of and ways to leverage opportunities that may be offered under the new aid architecture. Projects with such an aim will be critical in the era of the new programme of action for LDCs, to be adopted in 2021 at the Fifth United Nations Conference on the Least Developed Countries. LDCs stand to gain considerably, for example from capacity-building in the area of debt data quality and transparency and from enhanced technical assistance in debt management. Given their increasing exposure to commercial and bilateral non-Paris Club creditors, LDCs need to enhance understanding of the implications that such a shift in the composition of external debt could have on debt servicing, rollover risks and the costs of negotiating potential restructuring. This entails strengthening debt management practices and learning how to best engage bilateral lenders in ways that enhance overall debt sustainability and minimize costs in the event of restructuring.

UNCTAD is well positioned to have a leading role, given its track record in both the research and technical assistance aspects of financing for development, financial and macroeconomic policies and debt management. This work is reflected in the technical assistance provided by UNCTAD. For example, the Debt Management and Financial Analysis System programme currently supports 21 LDCs using the programme's software in building capacity to effectively manage their central government and government-guaranteed debt and to achieve sustainable debt levels. The programme has improved the availability of timely, reliable debt records, which are essential for prudent risk analysis and the elaboration of strategies for ensuring debt sustainability.[2]

c. Establish a unit in charge of the financial planning of national development plans

State capacity to design a development plan needs to go hand in hand with strengthening capacity for the planning and execution of the financing of sustainable development. This implies the mobilization and allocation of the necessary financing, particularly in the medium and long terms, given the typically long maturation period of development projects. It is essential for LDCs to strengthen domestic systems and accountability frameworks with a view to: learning how to best harness complementarities and synergies across development partners and engage them in the most effective manner while retaining ownership

[2] As at early 2019, 95 per cent of the supported countries had a comprehensive central government and government-guaranteed debt database and nearly 67 per cent had complete domestic debt records using the programme's software. In addition, 70 per cent of the LDC users that have also subscribed as participants in the quarterly external debt statistics database of the International Monetary Fund and the World Bank have reported on time. With regard to improved analysis, seven countries publish a debt portfolio analysis report on a regular basis.

of their own development agendas; putting in place strong measurement and monitoring frameworks to better measure the concessional resources obtained; gauging the development footprint of an increasingly complex array of transactions, involving both official and private actors, as well as official external sources from developed and developing countries; and strengthening the monitoring of financing, including by means of good data sets. A monitoring framework should appropriately take into account the distinct nature of the various types of funds (for example, concessional or non-concessional and private, blended or purely public, among others) and assess their development impacts accordingly. Such functions are usually carried out in different institutional settings, which may include a ministry of finance or planning, a national planning commission or an interministerial task force (see chapter 4). Whatever the institutional arrangement, it is important to ensure the strengthening of bureaucratic capabilities in the field of financial planning and the management of national development plans.

d. Eliminate State-weakening features in the present aid architecture

Some important practices under both the traditional and the new aid architecture weaken national ownership and thereby also impact State capacity. First, there tends to be a vicious circle of aid dependence, weak recipient country institutions and diminished bureaucratic competence, resulting in low State capacity. This is not inevitable, and its emergence depends critically on how ODA is managed and delivered (Bräutigam, 2000; Bräutigam and Knack, 2004; Knack and Rahman, 2007). This circle needs to be broken and aid system actors, including donor countries, have a crucial role in doing so. Second, under the traditional aid architecture, donors have often taken a project-based approach to aid and set up independent implementation units and accountability procedures that fall outside the scope of official State structures and often lead to human capital flight (Bräutigam and Knack, 2004; UNCTAD, 2008). This feature tends to go along with recent emphasis away from budget support towards projects as a mode of aid delivery (Lundsgaarde and Engberg-Pedersen, 2019). Ironically, donors have tended to move away from country systems despite recognized improvements in the quality of recipient country systems (OECD, 2012; OECD and United Nations Development Programme, 2019). Third, the recent evolution of the aid architecture has included a shift away from the focus on national government ownership towards a multi-stakeholder approach that accepts the role of different levels of government and actors beyond the State in addressing development challenges. This tends to dilute the scope for learning and institution-building among central governments and bureaucracies in recipient countries. Fourth, a similar effect results from the decision-making process often adopted with regard to ODA or private sector engagement. LDC Governments are frequently not involved in decision-making concerning project selection and aid allocation, which typically involves donor country Governments or agencies and the private sector in donor countries, but not beneficiary country institutions (Bhattacharya and Khan, 2019; see box 3.4). For solid transformative results, public investments, whether funded from domestic resources or through external support, should be implemented in the context of national systems, rather than being channelled through structures that bypass government institutions by setting up parallel structures (see chapter 4). Acquiring the capacity to do so is a long-term process that requires investment in capacity-building, learning by doing and the strengthening of bureaucratic capabilities.

Transformative results are best achieved through national systems

B. Revamping international development partnerships and building up aid management systems

1. Main issues

An increasing number of voices in the international community highlight the need for renewed action to face the challenges related to sustainable development, revamping the international cooperation framework and sustaining global demand, through concerted efforts to finance much-needed investments and redress inequality. The need for such different policy actions is even more acute because of the insufficiency of private sector engagement in delivering on the leveraging of ODA to mobilize significantly greater amounts of private finance for investment in the Goals (see chapter 3). The traditional aid system was beset by challenges and inefficiencies, including weak country ownership, misalignment between aid and recipient-country priorities, policy conditionality, insufficient aid flows with regard to country needs

Box 5.1 The rise and fall of the aid effectiveness agenda

Origins

The aid effectiveness agenda developed as a reaction to critiques made since the 1990s by recipient developing countries, development practitioners in donor countries, civil society organizations and other development stakeholders of the shortcomings, inefficiencies and adverse effects of the traditional ODA system. The concept emerged in 2002 at the first International Conference on Financing for Development and has evolved through a series of declarations and plans of action, as well as accompanying implementation mechanisms that were the result of negotiations between donor and recipient countries and multilateral institutions, later broadened to include new actors under the aid architecture.

Objectives and processes

The objectives of the aid effectiveness agenda were to reduce aid fragmentation and conditionalities, improve the impact of aid and correct the inefficiencies and negative aspects of the existing aid architecture. However, throughout the process, the results achieved have been far less than intended under the initial targets. Crucially, the intentions and priorities of the agenda have changed since the initial agreements. The first phase evolved through the High-level Forum on Harmonization and the High-level Forum on Aid Effectiveness, held in Rome in 2003, Paris in 2005, Accra in 2008 and Busan, Republic of Korea, in 2011. The Rome Declaration on Harmonization had as its objective the harmonization of the operational policies, procedures and practices of donor institutions with those of developing country systems, to improve the effectiveness of development assistance. The Paris Declaration on Aid Effectiveness was built around the five principles of ownership, alignment, harmonization, managing for results and mutual accountability. It was expected to provide a tool for donor countries and developing countries to hold each other accountable and thereby significantly increase the impact of aid. It set hopes for a radical shift in the donor–recipient relationship and in the aid-related decision-making process, as well as a shift from a donor-driven aid paradigm to a partner-driven one. The agenda continued to evolve in the Accra Agenda for Action, which reiterated the Paris Declaration principles and set out three further principles on which to concentrate efforts, namely, inclusive partnerships, delivering results and capacity development. The Accra Agenda has been termed “a high point of the aid effectiveness paradigm [when] recipients appeared to have genuinely (if still partially and problematically) asserted a stronger voice”. It began the broadening of stakeholders under the agenda by encouraging the engagement of new stakeholders, in particular civil society organizations, the private sector and diverse national actors. Since the Paris Declaration, the aid effectiveness agenda has been accompanied by quantitative targets of achievement and monitoring mechanisms. Donor and recipient countries set ambitious targets to be achieved by 2010, yet progress was below the levels expected. Donors globally met only 1 of 13 targets, namely, the coordination of technical assistance, but made progress in development strategies and results frameworks. They achieved limited progress in putting aid into the government sector on budget, common donor procedures for joint missions and analytical work, reducing fragmentation and the predictability of aid.

The limited and uneven progress is due to three main reasons. First, some difficulties in implementing the Paris Declaration stemmed from the fact that it was presented as a universal agenda while its implementation varied considerably according to national conditions, such as the degree of aid dependence in beneficiary countries, which weakens the negotiating power of recipients vis-à-vis donors. Second, the Paris Declaration implied that the principles reinforced each other, yet pursuing them proved to involve trade-offs, for example between ownership, harmonization and results. Another critical trade-off was between the will to reach short-term results and the need for long-term capacity-building and institutional development in recipient States, a time-consuming and resource-intensive process. Third, donors generally lacked the willingness to bear the economic and political costs associated with the implementation of effective development cooperation.

Reorientation

Since the High-level Forum in Accra, the aid effectiveness agenda has taken a different direction with regard to its objective, focus and actors. Under the Busan Partnership for Effective Development Cooperation, donors and developing countries collectively decided to broaden the aid effectiveness agenda. Focus was given to the effectiveness of the global partnership on development, welcoming contributions made through other initiatives, such as South–South cooperation, or from the private sector, as well as other financial flows, such as remittances, trade and investment, in promoting development strategies in developing countries. The Busan Partnership marked a paradigm shift from aid effectiveness to development effectiveness centred on the broadening of the agenda to involve new actors and shifting the focus away from the driving role of recipient countries as foreseen in the Paris Declaration. The Busan Partnership put less emphasis on some core principles of the Paris Declaration, in particular, alignment and harmonization, which were replaced in the Busan Partnership by the principles of transparency, inclusiveness and flexibility. Moreover, the Busan Partnership presented the private sector as a development driver.

Box 5.1 (continued)

Since the High-level Forum in Busan, monitoring of the aid effectiveness agenda has been undertaken by the Global Partnership for Effective Development Cooperation. The outcome document of the second High-level Meeting of the Global Partnership for Effective Development Cooperation, held in 2016, goes in the same direction. It reaffirms the principles of national ownership of development priorities and a focus on inclusive partnerships, transparency and accountability and results. It acknowledges the importance of new actors in the evolving aid architecture by emphasizing multi-stakeholder partnerships and attributes differentiated commitments to effective development cooperation according to stakeholder groups, recognizing different roles in and contributions towards shared effectiveness principles. Crucially, it confirms the downplaying of the Paris Declaration principles of alignment and harmonization, as already done in the Busan Partnership.

Since the High-level Forum in Accra, the aid effectiveness agenda along the lines of the Paris Declaration has lost momentum among donors. As the 2030 Agenda was being formulated, effectiveness fatigue was perceived as contributing to declining commitments to improve performance in areas such as donor coordination and the use of country systems. Donor agendas shifted further away from defining aid as guided by partner interests, as in the Paris Declaration, to emphasizing the contribution of development cooperation to advancing the national interests of donors. This reflected the return of national interest as a rationale for development cooperation and increasingly adopting a discourse of mutual benefit in defining relations with partners. It was in line with the effects of austerity measures following the global financial crisis of 2008/09 and with demands for a value-for-money approach to external aid, and was part of a movement towards greater integration between external aid and other policy areas such as trade, investment and migration.

Sources: Brown, 2016; Lundsgaarde and Engberg-Pedersen, 2019; Keijzer and Janus, 2016; Mawdsley et al., 2014; OECD, 2006; OECD, 2012; OECD, 2015.

and low levels of efficiency in the aid delivery system. Dealing with such long-standing problems has been a major challenge for the limited institutional capacities of LDCs, in particular given the asymmetry between their capacities and those of traditional development partners. The problems under the traditional aid system have given rise to proposals to simply eliminate it rather than taking action to improve its functioning and effectiveness (Easterly, 2006; Moyo, 2009). Such a drastic measure could, however, have negative economic, social and political effects in beneficiary countries, in particular those that are the most dependent on aid. Moreover, following decades of enquiry into the effects of ODA, researchers have concluded that it has a positive effect on the growth and development of recipient countries, despite the problems and inefficiencies. This has given rise to proposals to improve the workings of the aid system and enhance its development effectiveness. These issues are continuously discussed in development policy circles and have been taken up under the aid effectiveness agenda (UNCTAD, 2008). Despite improvements in terms of practices and modalities, the aid effectiveness agenda remains unfinished business and there is a need for better policy coherence and the alignment of priorities between LDCs and donors to avoid the wasteful allocation of resources and, in particular, to enhance the development impact of aid (box 5.1).

Ongoing discussions on the modernization of ODA respond to the need to better measure the resources made available for sustainable development purposes including, in some cases, by addressing long-standing criticisms, for example with regard to capturing the grant equivalent of ODA loans. However, such discussions risk lessening the significance of the aid effectiveness agenda by redefining the contours of financial flows that qualify as ODA. There is a risk that related decisions may undermine transparency and statistical rigour, weakening the principle of aid concessionality, conflating ODA and other official flows and, ultimately, defining a variable that lends itself more to politicization than to effective monitoring. For example, the inclusion of private sector instruments in the modernized measurement of ODA potentially entails a wide range of implications, not only in terms of concessionality, but by blurring key notions underpinning the aid effectiveness agenda, such as that of tied aid, further complicating the task of assessing alignment and the development footprint of any given intervention. The new aid architecture and its profusion of actors and instruments raises questions of how emerging development partnerships are managed and how LDCs can best make use of new opportunities, while at the same time minimizing the challenging or negative aspects of the changing landscape. As the pool of development actors expands, the ways in which development cooperation is being implemented are becoming increasingly opaque, even with regard to traditional ODA. The need for increased transparency has so far been focused on South–South cooperation, for which quantitative measurements are recognized as more complicated, yet greater transparency is equally

The new aid architecture requires new policy responses

relevant to other actors under the new aid architecture, such as philanthropic organizations, non-governmental organizations, the broader spectrum of civil society and, crucially, agencies using private sector instruments. This includes the beneficiaries of such instruments, for example business and investment funds that are intermediaries, with ownership structures that are often obscure. The lack of transparent and reliable information undermines planning and coordination functions in recipient States, hinders their ability to deliver on accountability for development and, ultimately, lessens democratic credentials. Put together, such developments point to the need to redefine the terms of the development partnerships of LDCs. This amounts to the transformation of the terms of the partnership between LDCs and development partners, both traditional and new. Specific ways and means of reaching this goal are discussed in this section.

2. Policy options

a. Implement policies for the new aid architecture

LDCs need to successfully manage their insertion into the new aid architecture. This means reviewing the terms and modalities of their relationships with sources of external finance, whether public or private. Crucially, LDCs need to occupy a central position and have a driving role in the decision-making processes of aid allocation and management. The immediate objective is to significantly strengthen aid effectiveness and boost its contribution to sustainable development by targeting structural transformation. In the medium to long term, enhanced development efficiency in aid allocation and administration will strengthen the capacity of LDCs to mobilize domestic resources and tap into other sources of external funds on commercial terms, leading to reduced dependence on aid.

i Revamp development partnerships

LDCs and their development partners could review the terms and modalities of their development partnerships, which could be (re)shaped around the following precepts:

- Recipient country ownership of decision-making concerning the allocation of financial resources, project selection and the determination of priority areas and issues;
- Alignment of programmes, projects and activities with national development plans and priorities;
- Standards of efficiency in financial resource disbursement, allocation and use;
- Mutual accountability in practices, data collection and reporting, standards of transparency and monitoring;
- Transparency in the origin and destination of funds and the relationship between funding sources and executing agencies and organizations;
- Mutually agreed methodologies and measurements to evaluate the development impact of external financing for development, as it is essential for LDCs to be actively involved in the formulation of methodologies, rules and data collection and in carrying out evaluation exercises; apart from being a precept in itself, enforcement has two desirable effects, namely, strengthening ownership and capacity-building in LDCs;
- Mutually agreed mechanisms to monitor the implementation of the above precepts.

Several of these elements were included in discussions on the effectiveness of traditional aid and form part of the Paris Declaration and the Accra Agenda, yet there are currently two major differences. First, it is necessary to return to the unfinished business of the aid effectiveness agenda. Second, contrary to the traditional aid effectiveness agenda, the precepts above refer to a broader range of LDC partners. Beyond traditional donors, they also apply to the new actors under the aid architecture, in particular, the private sector, philanthropic organizations and non-governmental organizations. The precepts should be common to all actors, yet their implementation and corresponding mechanisms should be differentiated according to the different types of actors.

There are fundamental qualitative differences in the relationship between LDCs and different external sources of finance. Traditional ODA is qualitatively different from development finance arising in the context of South–South cooperation, as it has different motivations, decision-making processes, modus operandi and delivery channels, among others. In particular, the application of these precepts to South–South cooperation should be done in a manner that ensures that these precepts serve to implement the principles of such cooperation as agreed by the international community, in particular that South–South cooperation and its agenda "should continue to be guided by the principles of respect for national sovereignty, national ownership and independence, equality, non-conditionality, non-interference in domestic affairs and mutual benefit" as reflected in more than one resolution of the General Assembly of the United Nations.[3] Similarly, philanthropic development financing differs from traditional ODA and South–South development finance and should therefore be subject to different mechanisms in the implementation of the above-mentioned precepts. Given lingering dependence on aid in LDCs and the importance of the changes in the aid architecture, the evolving terms of development partnerships should receive greater policy attention when the international community discusses the new programme of action for LDCs in the process of the Fifth United Nations Conference on the Least Developed Countries and in the final phase of implementation of the 2030 Agenda in LDCs.

ii Establish or reinforce aid coordination mechanisms

Aid coordination is a crucial element in implementing the principles of ownership and alignment of external financial flows with national development plans and priorities. Effective aid management and coordination policies are required for LDCs to maintain ownership of their development agendas and harness the benefits from the increased availability of development partners. However, this is one of the principles of the Paris Declaration that has seen the least effective progress in implementation. Aid coordination can be enforced through different mechanisms, such as the following: interministerial and sectoral processes for coordinating aid (as adopted in Angola, Burundi, Ethiopia, the Lao People's Democratic Republic, Senegal, Tuvalu, Uganda and Vanuatu); international cooperation policies that spell out how sectoral support should be treated (as implemented in Afghanistan, Kiribati, Malawi, Nepal, Rwanda and Sierra Leone); the channelling of aid through existing institutions such as a ministry of finance; and United Nations mechanisms such as multi-donor trust funds or the United Nations Sustainable Development Cooperation Framework, a "strategic, medium-term results framework that describes the collective vision and response of the United Nations system to national development priorities and results on the basis of normative programming principles" (see chapter 4).[4] These are ways of strengthening LDC ownership of financial resources and allocation, as well as the alignment of allocation and disbursement with domestic development plans. In some instances, establishing strong national aid management systems has led countries to reject funding offers that are not aligned with national priorities. This is a difficult

decision for countries subject to resource and foreign exchange constraints, but it has served to signal beneficiary country commitment to strengthening national ownership. The experience of LDCs in which aid coordination has been successfully implemented shows that strong recipient country systems contribute to ensuring donor coordination, even in situations where donors do not give priority to the principle of coordination. The channelling of ODA through budget support rather than projects and/or parallel structures also contributes to aid coordination (Bräutigam, 2000).

b. Implement Aid Effectiveness Agenda 2.0

The present relationship between traditional donors and beneficiary countries is largely a result of two factors, namely, lingering issues on the original aid effectiveness agenda on which progress has been limited or incomplete; and rapid changes in the aid architecture, which present new challenges to recipient countries. To take into account both lingering and emerging issues, traditional donors and beneficiary countries are advised to launch a new agenda, namely, Aid Effectiveness Agenda 2.0. This agenda should have two components, namely, addressing the unfinished business of the original agenda and dealing with the challenges that have emerged from ongoing changes in the aid architecture. The implementation of Aid Effectiveness Agenda 2.0 should therefore effect changes to the existing aid architecture and correct for many of the challenges faced by LDCs under the traditional system.

i Deal with unfinished business

Over 10 years after the signing of the Paris Declaration and the Accra Agenda, their principles remain relevant, as does the principle of putting recipient countries

3 See paragraph 11 in United Nations (2010b) and paragraph 8 in United Nations (2019d), both of which echo paragraph 13 of United Nations (1978).

4 See https://undg.org/document/2017-undaf-guidance.

Support for transformative national development has to be strengthened

and their priorities at the centre of the aid system. This is consistent with the role attributed to States by the 2030 Agenda and the Addis Ababa Action Agenda. Developing country policymakers still place a higher priority on ownership, alignment with national priorities and effective delivery, for example, the speed of project delivery, in raising project finance (Prizzon et al., 2016). Yet, to a great extent, these principles have not been implemented and have decreased priority in mainstream aid policymaking. Therefore, a core element of Aid Effectiveness Agenda 2.0 is to reaffirm these principles and address the unfinished business of the original aid effectiveness agenda. There is a need to fully implement international commitments made following previous negotiations and affirmed in major international declarations.

(a) Implement previous commitments on the volume of official development assistance

Donor country commitments on the volume of ODA were made before aid effectiveness became a key issue on the international development agenda. However, given that most donor countries have not delivered on their commitments, this issue remains as part of the pending items on the traditional aid agenda. It is critical for traditional partners to deliver on long-standing commitments and the ODA targets reaffirmed in target 17.2 under the 2030 Agenda, in relation to both developing countries and LDCs. The additional inflow of development finance this would have brought to LDCs in 2017 was $32.5 billion–$58.3 billion (see chapter 2). ODA resources fall short of investment needs to achieve the Goals, yet such a step is critical in mobilizing additional resources, in particular in vulnerable countries such as LDCs, and in reinforcing mutual accountability. Such an increase in ODA might accentuate dependence on ODA in LDCs yet, while this may occur in the short term, on the contrary, the desired effect in the medium and long terms would be to lessen such dependence, as may be expected on the path towards economic development. At present, ODA remains a key tool in enhancing the development and long-term prospects of poor countries, in particular LDCs (Arndt et al., 2010). For an increase in aid dependence in the short term to lead to the end of aid dependence in the long term in LDCs, one condition is that a significant portion of the additional resources should be directed towards the development of productive capacities, in particular, to productive investment that leads to structural transformation. This would help to create good quality employment, which is a precondition for achieving several of the Goals, including Goal 1. Moreover, structural transformation in LDC economies would shrink chronic current account deficits, reducing their external indebtedness and lessening their dependence on external resources and, by the same token, gradually eliminating aid dependence. In other words, such a long-term process presupposes the rebalancing of the allocation of traditional aid in favour of productive sectors in such a way as to accelerate structural transformation. Targeted aid earmarked for specific sectors, in particular infrastructure investments, can facilitate improved fiscal outcomes in LDCs and reduce debt burdens. Development partners should therefore increase support for transformative national development agendas to maximize the effectiveness of aid. It is important for commitments on ODA volume to be implemented ahead of the Fifth United Nations Conference on the Least Developed Countries, in order that they may form part of the basis for the planning of the financing for development landscape for LDCs for the next decade. Such developments should be reflected in the next plan of action.

(b) Ensure donors align with national priorities

A crucial aspect of the aid effectiveness agenda has been the alignment of donors with beneficiary country priorities. The divergence between the concentration of donor resources on social sectors and the neglect of productive sectors and infrastructure shows that alignment remains an issue in traditional aid delivery that needs to be addressed. Critically, LDCs receiving aid above 50 per cent of government expenditure but with a similarly high tax revenue-to-government expenditure ratio face significant aid alignment problems. A threat to the achievement of the Goals in LDCs is path dependency in the pattern of aid allocation, whereby a concentration in the social sector remains prevalent. It is therefore important to align aid allocation with recipient country priorities and development plans.

ii Tackle new challenges

Private sector engagement implies an increased reliance on FDI and public–private partnerships. Negative experiences with such partnerships are common in both the global North and South. Many of the donor countries championing such partnerships abroad through the strategies of their development finance institutions are changing their approaches to domestic public–private partnerships, but similar developments are lagging in recipient countries.

Giving primary consideration to the singular issue of accountability can help LDCs affect private sector engagement in ways that enhance its contribution to structural transformation and sustainable development. Regardless of the outcomes of the modernization of the ODA architecture, the redefinition of what counts as ODA warrants a careful assessment of development impacts, to determine whether the evolving notion of ODA is appropriate in the era of the 2030 Agenda. For Aid Effectiveness Agenda 2.0 to be meaningful, it is important that DAC members strengthen ODA-linked private sector engagement accountability in beneficiary countries including, in particular, LDCs, which are the most dependent on ODA among all beneficiary countries. The need for accountability and transparency applies across all development cooperation actors in private sector engagement, and the following elements are critical.

(a) Collaborate on private sector engagement in development cooperation

Recipient governments and beneficiaries have, to date, not been a party to the ODA modernization process and the design of private sector engagement in development cooperation. The direction of accountability in the operationalization of private sector engagement also tends to flow backwards to donors, rather than to beneficiary developing countries. There are no agreed or standard definitions of most concepts related to private sector engagement and blending. In order to enhance development cooperation, donors may create a platform for joint decision-making with recipient countries on a range of issues, such as the following:

- All applicable definitions and methodologies of measurement relevant to the new ODA architecture and private sector engagement;
- Minimum standards of transparency in the use of private sector instruments and additionality;
- Expediting decisions on the unfinished business of ODA modernization;
- Effectively addressing current gaps in the accountability of the private sector as an actor in development cooperation;
- Reaching an agreement to reserve the right of recipient countries to have the final say on the scope and limits of private sector engagement in development cooperation.

(b) Enhance transparency in project selection and implementation

Private sector engagement in development cooperation emphasizes corporate and commercial

The scope and limitations of private sector roles need to be well defined

solutions. Decision-making tends to involve donor agencies and the private sector and can often exclude recipient country institutions, contrary to the principle of ownership. This is in contrast to traditional development finance, which typically results from a process of negotiations between external sources of financing and beneficiary countries (Whitfield and Fraser, 2010). LDC Governments may consider the following:

- Proactively delineating the scope and limits of the roles of the public and private sectors in the delivery of public services, in line with heterogenous interests and socioeconomic contexts at the national and sectoral levels, as well as guarantees and contingent liabilities included in private sector engagement projects that might entail fiscal implications;
- Putting in place the necessary institutional frameworks, laws and regulations to align private sector engagement with national development priorities and goals, that is, implementing the principle of alignment, which may be achieved by, among others, requiring consistency with national development plans; requiring transparency in the ownership information of investees; and establishing the role of the State in assessing the development impact of Goals-aligned investments in the context of private sector engagement in development cooperation.

(c) Develop the endogenous entrepreneurial base in the least developed countries

Fostering domestic entrepreneurship can have a major development impact and is a critical part of inclusive and sustainable economic development (UNCTAD, 2018b). LDC Governments need to proactively engage with private sector engagement in ways that define the role and space of the domestic private sector and its interface with the external private sector. They also need to structure investment incentives in domestic economies accordingly. LDC Governments may consider the following:

- Identifying strategic national interests or sectors in their economies as, for example, countries in the European Union have done following the increased investment by China in their countries;

Development finance should boost

domestic entrepreneurship

- Preserving the necessary space for domestic private sector participation in the most profitable segments of economies, for example by securing access to an equitable distribution of aid-based support for the domestic private sector, which can provide a window for international agreements and/or best practice principles for win-win formulas in addressing the commercial interests of both donors and recipients;
- Exploring innovative ways to enhance linkages with FDI, for example by setting up secondary industrial zones for domestic suppliers, whether at separate sites or adjacent to formal export processing zones that often target FDI (Moran et al., 2018);
- Revisiting entrepreneurship strategies in line with the contribution of different types of entrepreneurship to structural transformation and wealth generation, including with regard to the higher propensity of medium-sized and larger domestic companies to link with external investors in win-win scenarios, compared with smaller counterparts (UNCTAD, 2011c; UNCTAD, 2018b).

(d) Develop an internationally agreed development impact evaluation framework for non-State actors

Accountability for achieving the Goals currently lies only with States, which are constrained in exercising this responsibility by the use of commercial solutions to development that do not have binding and rigorous development impact evaluation frameworks for non-State actors. The need to develop and implement methodologies, metrics and mechanisms for development impact evaluations is an integral and critical gap in the new aid architecture. It raises the risk that development effectiveness and impact will be aligned with commercial and financial metrics rather than the lived experience of development in beneficiary countries. Some Goals are more easily invested in than others. The evidence points to heightened risks of concentration by private sector engagement on a few of the Goals, with other Goals, such as quality public education, in danger of remaining severely underfunded. Moreover, many LDCs remain unattractive to private investment beyond the traditional areas targeted by FDI, in particular in the primary sector. Therefore, a closer alignment of private sector engagement with Aid Effectiveness Agenda 2.0 is desirable. Donors and beneficiary LDC Governments may consider the following:

- Jointly developing indicators and guidelines for measuring and reporting on the development impact of private sector engagement projects to strengthen mutual accountability frameworks for achieving the Goals;
- Limiting the expansion of the share of private sector engagement in total ODA to LDCs, contingent on clear and evidence-based evaluations of the impact and additionality of private sector engagement on recipient country development, given that available evidence does not point conclusively to the acceleration of sustainable development in beneficiary countries;
- Considering the implications of increased incentives for accelerated fragmentation in development cooperation and cross-sectoral impacts as part of development impact assessments of private sector engagement;
- Effectively addressing the issue of implicit subsidies when private companies invest in beneficiary countries, given the potentially negative effects on market structure and competition;
- Agreeing on a common definition of ODA, along with jointly agreed guidelines and boundaries for private sector engagement in development cooperation.

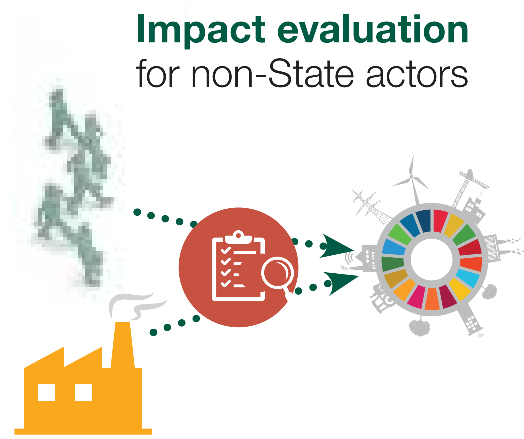
The idea of promoting responsible business conduct and promoting and facilitating investment aligned with the Goals is a major component of private sector engagement. Donor countries can promote business investment in projects and sectors that promote the structural transformation of LDC economies, in order for aid resources to be the most effective in terms of development impacts. In addition, the international community may promote new forms of business and investment for shared value that boosts productivity, inclusiveness and development and that replicates and scales up best practices; and traditional donors have suggested that they are increasing coherence between domestic policies and development objectives by using evidence of the development impacts of their policies in developing countries (OECD, 2018a). This should be an element of Aid Effectiveness Agenda 2.0.

(e) Ensure additionality

A central issue of the unfinished business of aid effectiveness agenda which has become increasingly important under the new aid architecture is additionality. The trends in external financing, in particular the emergence of new donors, private actors and blended resources, are creating additional coordination problems in LDCs, and it is not clear how much additional external financing is being provided. Countries should ensure that the new forms of cooperation are bringing additional financing that complements domestic resources and are not substitutes that entail costly private financial flows and additional public liabilities.

c. Expand and strengthen South–South cooperation

The relevance of South–South and triangular cooperation has increased in recent years and could have a critical role with regard to sustainable development prospects in both LDCs and other developing countries. Given the development needs of the former, increased South–South development cooperation by non-traditional partners in a position to do so could bring considerable benefits. It is critical to adequately reflect LDC needs in existing frameworks for economic integration among developing countries at regional or interregional levels. Challenges remain, in particular with regard to regional imbalances in access to development finance by beneficiary countries, along with the need for increased clarity in the definition of concessional and non-concessional lending, given the present lack of a common definition among sources of development finance in the South. These issues should be addressed through the revamping of development partnerships and enacting of general precepts, including mutual accountability and development impact evaluations. Development partners in the South have not yet agreed on a single definition and methodology for reporting on South–South cooperation, yet it is important to build upon existing country-level efforts to improve the transparency and monitoring of sustainable development footprints. This would be consistent with the outcome document of the second High-level United Nations Conference on South–South Cooperation, which encourages the development of "country-led systems to evaluate and assess the quality and impact of South–South and triangular cooperation programmes and improve data collection at the national level" (United Nations, 2019d, para. 25). In this context, the engagement of beneficiary countries, including LDCs, could prove particularly promising in progressively building institutional capacities to monitor development cooperation activities and enhance their quality, as well as taking into account the specificities of LDC economies. The United Nations has traditionally had an important role in fostering South–South cooperation and has been requested to pursue and strengthen its action in this field (United Nations, 2019d, para. 27). A United Nations system-wide strategy on South–South cooperation is being developed.



C. Bolstering the fiscal systems of the least developed countries

1. Main issues

It is crucial for LDCs to place the strengthening of their fiscal systems at the centre of their development strategies, for two main reasons. First, building fiscal systems is an integral part of State-building and there is a reciprocal relation between the quality of a fiscal system and State capacity. In order to finance the building of institutions and the formation of bureaucratic capabilities, States need to mobilize resources. Along the development trajectory of countries, there is typically a transition from dependence on external finance towards domestic resource mobilization, as noted in this report. In addition, State capacity to raise and allocate fiscal revenue in a sustainable way depends on a social contract that confers legitimacy to the fiscal system, in both developed countries and as part of the ongoing development process in developing countries (Bräutigam, 2008). State-building

It is vital that LDCs expand their tax bases

and the strengthening of State capacity is in turn required for a State to be able to steer the process of structural transformation and, thereby, sustainable development. Second, there is a relationship between taxation and aid dependence. It is often argued that aid dependence prevents the development of fiscal capacity in recipient countries, as well as State capacity more generally, and that it tends to perpetuate a low-level equilibrium that characterizes underdevelopment traps (Bräutigam, 2000). Aid and taxation are often seen as imperfect substitutes, on the grounds that the availability of ODA is a disincentive to the construction and strengthening of a domestic fiscal system. However, the extent of such negative side effects is questionable and, moreover, they may be the consequence of problems in the system of aid itself. In addition, multilateral and regional development banks have traditionally been active in the fiscal field through the implementation of capacity-building programmes on fiscal policy and budget management, which have resulted in building islands of high-level bureaucratic competence in LDCs, typically within ministries of finance and central banks. Yet such capacity-building activities have often largely been oriented towards fiscal prudence and decreased expenditure, rather than raising taxes and managing the longer term development impacts of fiscal policy (Therkildsen, 2002).

2. Policy options

a. Strengthen fiscal capacity

If correctly used, aid can become an instrument for breaking the vicious circle between aid dependence and weak State capacity, if it is applied to strengthening bureaucratic capacity in recipient countries, in particular with regard to tax collection and public expenditure allocation and management. Partner countries and institutions have an important role in this endeavour. They should have not merely a technocratic approach to building fiscal capacity in LDCs but a focus on the development impacts of fiscal policy. Strengthening LDC fiscal capacity is warranted on the following grounds:

- Gradually reducing aid dependence in LDCs and progressively attenuating the negative features of aid dependence;
- Strengthening ownership of development policies and thereby providing the resources required to boost the investment needed to accelerate structural transformation in LDCs;
- Bolstering LDC negotiating positions vis-à-vis external public and/or private sources of financing;
- Helping LDCs attenuate the missing-middle trap of development finance as they graduate from the LDC category or as income levels rise.

Sources of bilateral development finance and technical assistance can also be mobilized to strengthen fiscal systems in LDCs with regard to both human and institutional capabilities. This presupposes synergies between ODA and domestic taxes. Aid can be targeted to strengthening domestic fiscal systems, in particular through capacity-building among public officials and strengthening the related institutions, such as the ministry of finance, tax authorities and tax legislators. Aid should be used to bolster bureaucratic capacities on both the revenue and expenditure sides, as efficiency gains are required in allocation, spending and fiscal resource management. It is important to build fiscal capacity in most developing countries and even more critical in LDCs. However, the expectation placed on LDCs to mobilize adequate domestic financial resources for their development should be tempered by reality. Low levels of diversification in economies limit the extent to which LDCs can rely on taxes on income and profits. Moreover, due to its procyclical nature, tax revenue in LDCs is bounded by the weak growth potential of their economies. Macroeconomic shocks and structural vulnerabilities in LDCs also contribute to underperformance in tax revenue collection, in particular in countries with weak institutions. Most LDC economies have a large informal sector, which limits the scope for strengthening taxation. Therefore, it is important to strengthen State capacity in mobilizing and managing both domestic and external sources of financing for development and to ensure that aid is geared towards gradually reducing aid dependence.

b. Expand the tax base

The limits of domestic resource mobilization in LDCs are due to the narrow productive base and low levels of income, although there are income and wealth sources that have typically been underexploited by policymakers in LDCs, traditionally in the following areas (UNCTAD, 2010):

- Natural resources, for example, the low level of taxation of mining activities is a traditional shortcoming in LDC fiscal policy, in particular in resource-rich LDCs;

- Tax loopholes and exemptions given to transnational corporations, expatriates and private sector engagement projects; over 80 per cent of low-income countries and lower-middle-income countries offer tax incentives and exemptions on investment, yet tax incentives are often not among the most important factors in investment and location decisions and LDCs should therefore consider revising the terms of their FDI policies and bilateral investment treaties (OECD, 2018a);
- Urban property, which is typically taxed at low levels or not taxed at all;
- Luxury consumption, which typically faces the same shortcomings as urban property as a taxable base.

These sources of income have traditionally been accessed by LDCs to a low extent. The development of a new aid architecture and the significant increase in the number of agents active in the economies of LDCs implies that there are other potential sources of taxation that should be considered but are typically neglected, including taxing private sector engagement projects and aid workers, closing ODA loopholes and tax exemptions and participating in the profits of public–private partnerships.

D. Reinforcing the voice of the least developed countries in international financial forums and restoring the primacy of multilateralism

1. Main issues

LDCs should renew efforts to reassert the importance of the global partnership for sustainable development and take a more assertive and proactive role in engaging development partners, articulating their needs and stakes with regard to systemic issues at the bilateral and, in particular, at the multilateral level. With regard to broader issues on the international agenda, LDCs have a particularly strong vested interest in preserving and strengthening multilateralism. This is the sphere where the voice and interests of smaller countries and weaker actors in the international community are best represented and defended (Kahler, 1992; Súilleabháin, 2014). Multilateralism is, moreover, a means of pursuing the realization of human rights, including the right to development (box 5.2). Yet the current economic and geopolitical conjuncture is placing an enormous strain on the multilateral system and it has recently come under criticism in the fields of trade, finance and geopolitics.

Multilateralism has to be safeguarded and strengthened

With regard to specific issues on the aid effectiveness agenda, the United Nations system has effectively promoted the Paris Declaration principles of ownership and alignment, with a commitment to promoting State capacity and decision-making on development priorities and strategies, in contrast to the shifts in the priorities of traditional donor countries away from a beneficiary country-centric approach (Lundsgaarde and Engberg-Pedersen, 2019). This broader movement away from multilateralism seems to be reflected in the current trend in the aid architecture to target the increased use of bilateral development finance institutions. This may ultimately elevate bilateral engagement and intensify unilateral action by a variety of actors that are not necessarily equipped to address all or any development challenges. This change should not come at the expense of the multilateral sector, including the critical role of the United Nations in providing concrete evidence-based guidance on development cooperation for policymakers and practitioners at all levels. The United Nations development system constitutes an essential forum to create greater solidarity across all countries and sectors and to ease tensions between competing national interests. This is an additional reason for the international community to resist the drive away from multilateralism. Among systemic issues of critical interest to LDCs, with increasingly visible impacts, is climate change. Growing evidence has shown that, although LDCs have contributed only marginally to greenhouse gas emissions, they will be disproportionately affected by the consequences of climate change and related extreme weather events, which threaten to exacerbate global inequalities and undermine progress towards sustainable development and poverty eradication (UNCTAD, 2010). Laying the foundations for sustainable development in LDCs entails investing in climate-resilient infrastructure and diversifying economies into sectors and activities with higher productivity and less exposure to climate-related risks. This hinges on the availability of adequate funds for climate change adaptation and mitigation, as well as on bold and concerted efforts to foster technology transfer. Against this background, resources mobilized by donor countries for environmental sustainability objectives are largely not on track to meet the commitment in the context of the Paris Agreement of $100 billion per year by 2020 and less than 20 per

Box 5.2 Multilateralism, international cooperation and the right to development

International cooperation is vital to realizing the transformative vision of the 2030 Agenda, which is grounded in the international human rights framework and informed by the Declaration on the Right to Development. The responsibility of States is anchored in articles 1, 55 and 56 of the Charter of the United Nations, which also highlight the need for multilateralism, as "all Members pledge themselves to take joint and separate action in cooperation with the Organization for the achievement of the purposes set forth in article 55" (article 56). These principles are reaffirmed by the Declaration on the Right to Development, which declares that States should cooperate effectively to provide developing countries with appropriate means and facilities to foster their comprehensive development and should take steps to eliminate obstacles to development. States acting individually and collectively bear primary responsibility for guaranteeing the right to development, which includes an appropriate political, social and economic order for development, appropriate national and international development policies and appropriate economic and social reforms to eradicate social injustice. Resonant with the principles of special and differential treatment and common but differentiated responsibilities, the Declaration on the Right to Development affirms that sustained action is required to promote more rapid development of developing countries. As a complement to the efforts of developing countries, effective international cooperation is essential in providing the appropriate means and facilities to foster their comprehensive development. Moreover, international cooperation is a binding legal obligation in several human rights treaties, including the International Covenant on Economic, Social and Cultural Rights, the Convention on the Rights of the Child and the Convention on the Rights of Persons with Disabilities. This obligation has been further elaborated by the respective treaty bodies. The human rights principles of equality, non-discrimination, participation, accountability and transparency must guide decision-making processes at all levels, including global governance. States, international and regional organizations and all other stakeholders must cooperate to reduce inequalities, in line with Goal 10, including through financing development and debt relief. Policy coherence requires trade and investment agreements to be aligned with human rights obligations and ensuring policy space requires redressing structural and systemic asymmetries. North–South, South–South and triangular cooperation, including to mobilize resources and close technology gaps and digital divides, can help realize human rights, in particular economic, social and cultural rights, including health and education.

Sources: United Nations, 1945; United Nations, 1986.

cent of bilateral ODA commitments by DAC members are reported as focusing on environmental objectives.

2. Policy options

In their quest for development finance, LDCs have a considerable stake in discussions related to systemic issues, notably reserve currency and debt sustainability. Their economic weight may be marginal when assessed on a global scale, but the terms of their integration into the global market are significantly affected by measures in this regard agreed by the international community. It is therefore all the more important that LDC interests be adequately considered and reflected in global forums and debates on systemic issues. A multilateral forum that provides a platform for LDCs to raise concerns to the international community is the Committee of Experts on International Cooperation in Tax Matters, currently working on several issues of particular interest to LDCs, such as transfer pricing, extractive industries, ODA projects and capacity development. This section focuses on such issues.

a. Combat illicit financial flows and international tax evasion

LDCs have experienced significant illicit financial outflows that further erode their taxable bases, in particular LDCs with extractive industries as an important sector of economic activity (Le Billon, 2011; UNCTAD, 2014e). Combating illicit flows requires strengthening international cooperation on tax matters and closing loopholes, to contribute to the domestic resource mobilization efforts in developing countries. This responsibility should be shared by all actors in development. International cooperation is therefore important, in particular at multilateral forums at which all countries, including LDCs, are represented.

b. Agree on a multilateral framework for debt restructuring

The proposal to establish an independent, multilateral and transparent debt restructuring mechanism has been included in international discussions on financing for development for decades, given the cyclical nature of foreign debt crises in developing countries, despite different initiatives taken to address them, such as HIPC. However, an international consensus has not yet been reached, although the need for it is becoming stronger in the present context, in both LDCs and other developing countries, in particular in view of the growing complexity of the aid architecture and the financing for development landscape. LDCs stand to benefit the most from such a mechanism, given their structural current account deficits and the recent deterioration of their external debt situations (see chapters 1 and 2). Ideally, such a framework should go beyond the strict debt sustainability criteria currently in place, and take into account human rights, gender inequalities and climate-related vulnerabilities. UNCTAD had a critical role in assisting the discussions that led to the adoption by the General Assembly of a resolution on basic principles on sovereign debt restructuring processes (United Nations, 2015a). This important step needs to be followed by implementation mechanisms for the agreed principles.

c. Facilitate access to long-term and climate-related finance

Macroeconomic fundamentals and the specific vulnerabilities in LDCs suggest that greater access to long-term development finance could prove vital in addressing infrastructure gaps and investing in technological upgrading and skills accumulation. The current trend in international finance is towards even greater private sector engagement through public–private partnerships, yet it is important to reaffirm the central role of public finance in sustainably financing infrastructure and thereby providing the basis for structural transformation. With regard to climate-related finance, beyond concerns about the additionality of resources provided for environmental sustainability purposes, it is imperative that developed countries step up the mobilization of official development finance in line with international commitments. It is also important to expand the share of such resources provided in grant or grant-equivalent forms and increase in particular the portion targeting climate change adaptation, as it is the type of climate finance most relevant to LDCs.

d. Restore the primacy of multilateralism

LDC have a limited voice at key discussions at which systemic issues are treated and limited chances to articulate their needs and see them adequately considered. Based on historical experience, this lack of representation is unlikely to be addressed in the near future, yet it is important that LDC concerns be adequately taken into account, if the pledge to leave no one behind is to be taken seriously. The need to reinvigorate multilateralism and strengthen global cooperation is increasingly being recognized, not only by the United Nations and UNCTAD, but also by the International Monetary Fund and OECD (International Monetary Fund, 2019; OECD, 2018a; Project Syndicate, 2019b; UNCTAD, 2017b). With regard to aid allocation and delivery, it is crucial to reinforce the role of the United Nations in the evolving aid architecture, given that development is one of the three pillars of the United Nations and given its strong track record with regard to ownership and alignment with national priorities. The United Nations commitment to the principles of the Paris Declaration is confirmed by the ongoing reform of its development pillar, a major element of which is the strengthening of the United Nations Sustainable Development Cooperation Framework. All sources of financing under the new aid architecture can therefore consider strengthening multilateralism by boosting the financing of programmes that give the United Nations system a leading role in collaborating with country authorities.