CENTER FOR GLOBAL DEVELOPMENT

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An Ambitious IDA for a Decade of Crisis

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Large and growing financing needs

Low-income countries are in a battle for their lives and livelihoods, but they lack the resources to respond effectively. As the largest single source of development finance for the world's poorest countries, the World Bank's International Development Association (IDA) must be at the center of the solution. The Covid-19 pandemic ushered in the first recession in over 25 years for many, disrupted supply chains, and upended markets and trade. The war in Ukraine triggered increases in the cost of fuel, fertilizer, and food, and the historic increase in interest rates by the US Federal Reserve and European Central Bank have not only exported inflation to the developing world but have led to massive and unpredictable increases in debt service obligations.[1] Many low-income economies are struggling with over 40 percent food inflation and governments lack the fiscal space to provide additional subsidies.[2] Financial stability concerns in developed economies have further tightened global market conditions. For many countries still trying to recover from the shocks of the Covid-19 pandemic, this second wave of shocks has proved fatal. For low-income countries the most important need now is access to consistent, predictable low-cost resource flows.

In addition to these economic challenges, countries are also confronted with the worst climate events in over two decades. From the floods in Pakistan, Mozambique, and Madagascar to the droughts in Horn of Africa and the Sahel, livelihoods are being threatened and public services strained. Responding to these weather events costs countries 5–7 percent of their already shrinking

1 https://www.cnbc.com/2023/05/04/european-markets-live-updates-stocks-fed-reaction-ecb-rate-decision.html#:~:text=ECB%20hikes%20rates%20a%20quarter%20point%20as%20expected&text=A%20day%20after%20the%20U.S.,range%20of%205%25%2D5.25%25.

2 https://tradingeconomics.com/country-list/food-inflation

GDPs.[3] In addition to climate countries must deal with biodiversity, pandemic preparedness, cross border migration, and rising conflict.

These economies are rowing against the tide to respond to overlapping challenges. In low- and middle-income countries, learning losses due to school closures from Covid have left up to 70 percent of 10-year-olds unable to read or understand a simple text, up from 53 percent pre-pandemic.[4] More than 370 million children globally missed out on school meals during school closures, losing what is for some children the only reliable source of food and daily nutrition and brain development.[5]

Maternal mortality rates are still 29 times higher in least developed countries than they are in Europe and North America, and hospital beds per 1000 are one hundredth the amount, as the COVID pandemic highlighted.[6] Low-income countries account for only 3 percent of global road networks worldwide, whereas high-income countries account for 43 percent, despite having only 16 percent of the population.[7]

Productivity growth has also slowed in many of these economies, sometimes even falling below population growth. In South Asia population growth was at 2 percent in 2021 while agriculture productivity was at 2.1 percent. In Africa population growth is at 2.8 percent and agricultural productivity at 1 percent.[8] Labor productivity displays similar trends. To turn the tide for these economies, transformational new investments will be needed to lift output, build infrastructure, and increase employment and productivity.

Development finance over the last 25 years has not delivered the scale and impact needed to improve lives and livelihoods at scale. Of the 81 countries that were part of the International Development Associate (IDA) in 1996 only 17 have graduated.[9] Over these 25 years only 7 countries have seen their GDP per capita triple. Less than 35 percent have seen GDP per capita double, many of these being countries that started at a very low base such as Rwanda and Ethiopia. 10 countries have seen their GDP per capita drop over the last 25 years.

3 https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2022/11/IHLEG-Finance-for-Climate-Action-1.pdf https://repository.uneca.org/handle/10855/43948
4 https://www.worldbank.org/en/news/press-release/2022/06/23/70-of-10-year-olds-now-in-learning-poverty-unable-to-read-and-understand-a-simple-text
5 unicef-irc.org/publications/pdf/COVID-19_Missing_More_Than_a_Classroom_The_impact_of_school_closures_on_childrens_nutrition.pdf
6 https://www.who.int/publications/i/item/9789240068759
7 https://documents1.worldbank.org/curated/en/383071468739248249/pdf/multi-page.pdf
8 https://datatopics.worldbank.org/world-development-indicators/
9 https://ida.worldbank.org/en/about/borrowing-countries/ida-graduates; https://documents1.worldbank.org/curated/en/191401468140658727/pdf/428770WP0BOX0321445B01PUBLIC1.pdf; not including Serbia and Montenegro, which were not IDA eligible in 1996, but later became so and graduated in 2008.

FIGURE 1. Change in GDP per capita of 1996 IDA-eligible countries (1996–2021)

Source: World Bank
Note: Constant 2015 USD data used; bolded countries have graduated from IDA.

A new development model partnership

There is an urgency to the development challenge and a rapid need for innovation. Secretary Yellen's call for more collective ambition is timely and accurate.[10] We need increases in the scale of resources, speed of deployment, and magnitude of impact to address the polycrisis, reverse the climate crisis, and build prosperous societies. The development challenge faced by countries is also a climate challenge—one cannot be won without the other. Winning these battles calls for a different growth model, one that endogenizes climate and works to build complementarities between more sustainable infrastructure models, more robust education systems and health systems, more resilient housing for the cities, and better agriculture and waste management. Leveraging these complementarities to pursue a new kind of industrialization would create more and better jobs, fast track the transition to cleaner and greener economies, and make the Sustainable Development Goals (SDGs), now off track, more achievable.[11] The new climate economy is real and presents many opportunities if countries design their development agendas to be complementary and take advantage of all the innovation in the climate field.

As the largest single source of development finance for the world's poorest countries, the World Bank's International Development Association (IDA) must be at the center of this new model. Though all development finance institutions will play a part, IDA is unique in its leverage, concessionality, and breadth, and warrants special consideration.[12] Unlike most bilateral aid agencies and vertical funds, IDA is leveraged, meaning it borrows against its equity to lend out greater volumes of finance than it takes in as donor contributions—almost $4 in concessional lending for every $1 from donors. This leverage has allowed it to achieve tremendous scale. Since 2020, it has led all other multilateral development banks in annual commitments, including its older sister institution, the International Bank for Reconstruction and Development (IBRD).[13]

IDA's performance in recent years also highlights its role as a counter-cyclical finance provider—no other institution scaled up commitments more during the first year of the COVID crisis.[14] IDA's lending is highly concessional, with rates of approximately 1–3 percent, and maturities between 30–40 years. Importantly, these terms are not directly tied to global interest rates, meaning that when financial conditions elsewhere tighten, as they are now, IDA provides critical liquidity at a low cost. For many countries, IDA is the only certain source of sustainable long-term financing. Finally, as a part of the World Bank, IDA has tremendous breadth across geographies and sectors, which enables it to serve as a platform on which to drive forward the multiple complementary development priorities mentioned above, from sustainable infrastructure to health systems.

10 https://home.treasury.gov/news/press-releases/jy0997
11 https://www.un.org/sustainabledevelopment/blog/2021/07/tremendously-off-track-to-meet-2030-sdgs-un-chief/
https://www.brookings.edu/wp-content/uploads/2023/02/Chapter-9.-Delivering-Africas-great-green-transformation.pdf
12 https://ida.worldbank.org/en/about/contributor-countries
13 https://www.cgdev.org/blog/road-better-world-bank-starts-commitment-ida
14 https://www.cgdev.org/blog/mdbs-first-responders-covid-19-record-so-far

Despite its strengths, IDA alone cannot meet the plethora of multiplying development challenges facing low-income countries today. For these countries to get back on track, a new development partnership is needed. Both multilateral banks and their shareholders, as well bilateral aid agencies, philanthropy, and the private sector, must come together to scale and accelerate the transformation to a new green growth model. Business as usual or incremental measures that put bandages on the problem and hope to address it later would prove fatal.

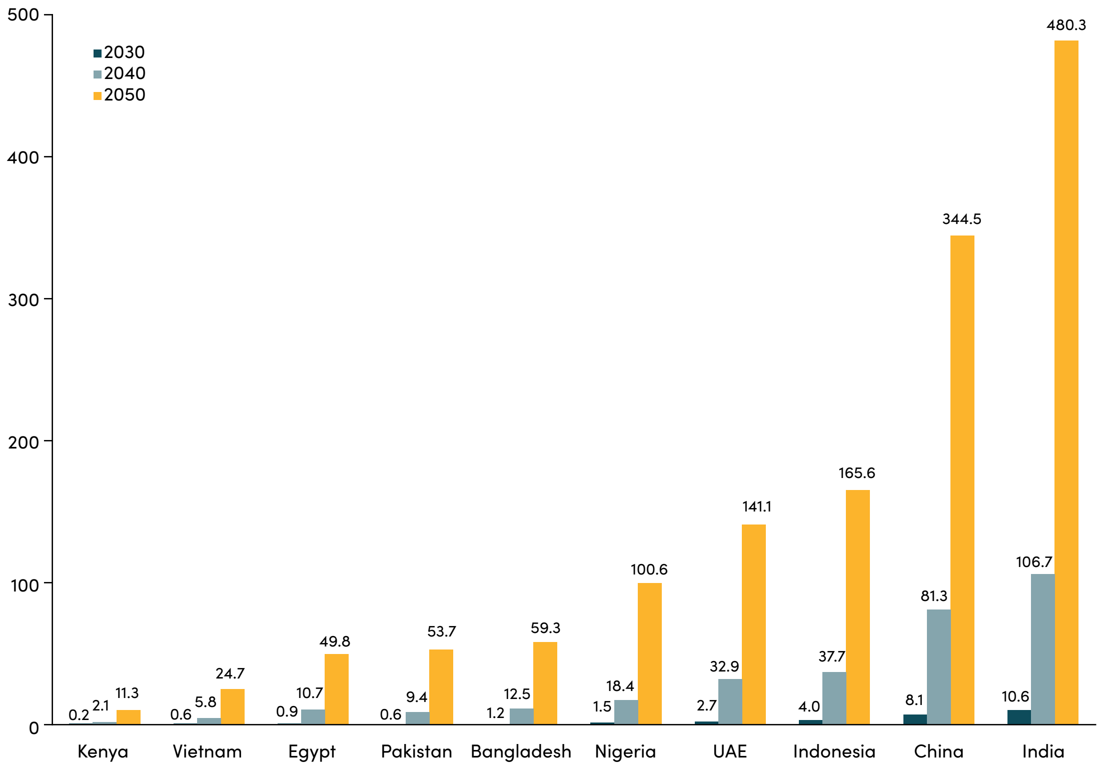
The Songwe, Stern, Bhattacharya report calls for $2.4 trillion dollars a year between now and 2030 to deal with the climate crisis for emerging and low-income countries excluding China. Of this $2.4 trillion, $1 trillion must come from external sources, including a tripling of annual flows from the multilateral development banks.[15] Recognizing its vital role at the center of this scale up, for IDA we call for a corresponding tripling of donor contributions from 2012 levels by 2030 to enable of overall tripling of IDA resources to $279 billion by IDA22 (2029–2031).

The report calls for action on the climate front in three areas which complement, reinforce, and enhance the overall development and growth ambitions of countries to deliver robust and more resilient growth. First is the transformation of the energy systems. Second, building resilience and responding to growing asset erosion caused by climate events. Third, protecting and restoring natural capital and biodiversity and investing in sustainable agriculture. Early action will reduce the cost of adaptation down the line. For example, for Nigeria will require at least $1.5 billion a year in adaptation resources by 2030, with a substantial portion of these resources going to agriculture adaptation. However, with no action, by 2050 it would require over $100 billion in investment, or over 67 times the 2030 amount (Figure 2).

Alongside the $1 trillion from external resources, of which MDBs must contribute a major portion, the Songwe et al. report assumes $1.4 trillion will be raised from domestic sources. This implies substantial improvements in savings rates in low-income countries and doubling in domestic resource mobilization in many countries. Political will and a global social contract are critical for the achievement of the objectives ahead. The vision of a world free of poverty is still achievable if this combination of increased external financing and a credible verifiable commitment to reforms by countries is coupled with increases in efficiency in the MDB system. Never has there been an opportune time for this contract to be activated as now.

15 https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2022/11/IHLEG-Finance-for-Climate-Action-1.pdf

FIGURE 2. Estimated minimum adaptation investment required in a 1.5°C warming scenario (minimum at given year, USD billions)



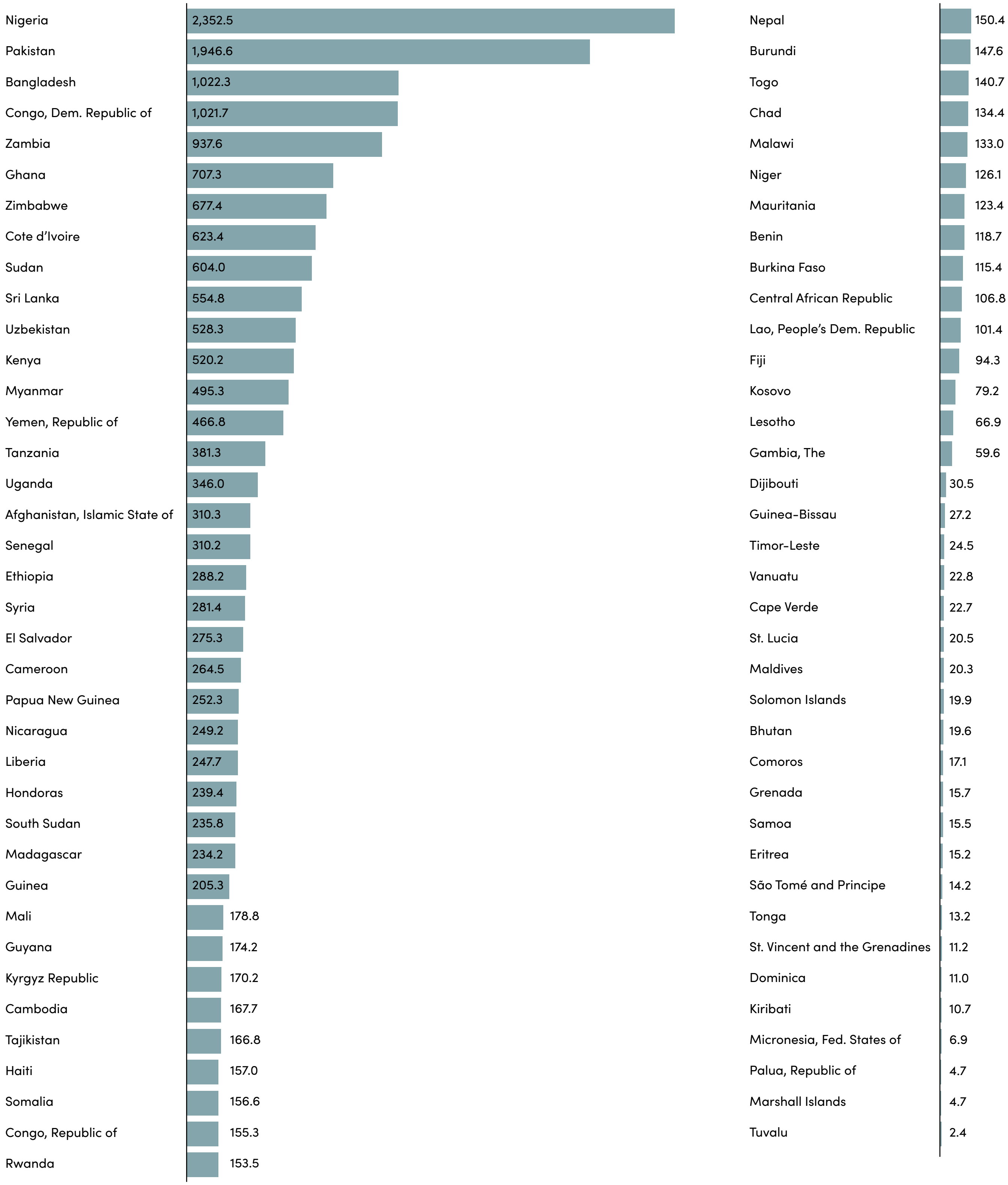
Source: Standard Chartered

An incremental approach will not deliver rapid results

We must learn the lessons of the last three years; a slow response to the crisis sets development back substantially. The immediate response of the international community to the multiple crisis and the need for resources as the pandemic spread was slow and inadequate. After over a year of waiting the G20 approved the release of a historic $650 billion of Special Drawing Rights. However, this did not provide much relief for IDA countries, who received only 4 percent of the total SDR allocations.[16] Efforts to on-lend more from the developed countries are still under discussion.[17]

16 https://www.imf.org/en/Topics/special-drawing-right/2021-SDR-Allocation
17 https://www.uneca.org/stories/special-drawing-rights-must-be-re-allocated-to-avail-sustainable-financing-for-africa

FIGURE 3. 2021 IMF special drawing rights allocation (USD billions)



The second liquidity instrument made available globally to IDA countries was the Debt Service Suspension Initiative (DSSI), which allowed countries to postpone debt payments for two years while dealing with the Covid-19 crisis. It is estimated that the DSSI delivered about $12.9 billion in temporary relief to countries.[18] However, debt pressures have persisted as many countries now find themselves in the middle of a new crisis brought by the war in Ukraine, advanced economy interest rate hikes, and worsening climate disasters. Though their spending needs are greater than ever, countries are obliged to honor their debt obligations, even at the expense of social spending, as no extension of the DSSI was offered. As a result, approximately 50 percent of the IDA countries are in debt distress, or at high risk of it.[19]

Amid an inadequate response from the international community, resources from the World Bank and the IMF were crucial in helping countries weather the storm. The World Bank front loaded IDA resources by nearly 12 percent to commit an average of $35 billion annual over FY20–FY22 as opposed to the planned $31 billion, with a record $38 billion committed in FY22.[20] This frontloading helped countries weather the storm momentarily, but most are back in crisis management mode and without substantial additional resources will fall further behind.

Table 1. IDA countries in or at high risk of debt distress (grant-only)

GRANT-ONLY IDA COUNTRIES		
Afghanistan	Grenada	Samoa
Burundi	Guinea-Bissau	São Tomé and Príncipe
Cameroon	Haiti	Sierra Leone
Central African Republic	Kenya	Somalia
Chad	Kiribati	South Sudan
Comoros	Lao P.D.R.	St. Vincent and the Grenadines
Congo, Republic of	Malawi	Sudan
Djibouti	Maldives	Tajikistan
Dominica	Marshall Islands	Tonga
Ethiopia	Micronesia	Tuvalu
Gambia, The	Mozambique	Zambia
Ghana	Papua New Guinea	Zimbabwe

Source: IMF DSA list

18 https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative
19 https://www.imf.org/external/pubs/ft/dsa/dsalist.pdf
20 Corresponding to one third of the $93 billion replenishment, initially intended to cover 3 years.

With crises compounding, liquidity drying up, and the DSSI long since expired, countries are on the brink. Calls for SDR on-lending through the IMF's Poverty Reduction & Growth Trust (PRGT) and Resilience & Sustainability Trust (RST) continue. The subsidy account of $1.6 billion needed to make these instruments active is pending. The Bridgetown Agenda's calls for a renewal of the DSSI, expanded multilateral lending, and greater volumes of private capital mobilization for climate are yet to be fulfilled. Natural disaster clauses calling for debt service suspension by MDBs, while promising and feasible, have yet to be implemented across all creditor classes. As of yet, there is no speedy debt resolution mechanism, and the common framework is limited, unpredictable, uncertain and needs redesigning to help countries in crisis.[21] The June 2023 Paris Summit advanced these agendas, and the Indian G20 is expected to help move them forward, but breakthrough progress has proven elusive.

The penultimate source of substantial additional finance and most secure source of grant and long-term concessional financing is the World Bank's fund for the poorest, IDA. There is ample evidence that countries that weathered the crisis well are countries that used their liquidity lines effectively or in the developed world countries that benefitted from substantial injections of capital into the economy.[22] To build forward better IDA countries will need the similar additional injections of capital and at the very least no reduction in existing commitment envelopes. As a result, donors must step up to maintain IDA's commitments at their FY22 level of $38 billion over the next two years, and eventually triple its commitments in line with the needs outlined in the Songwe et al. report and others.

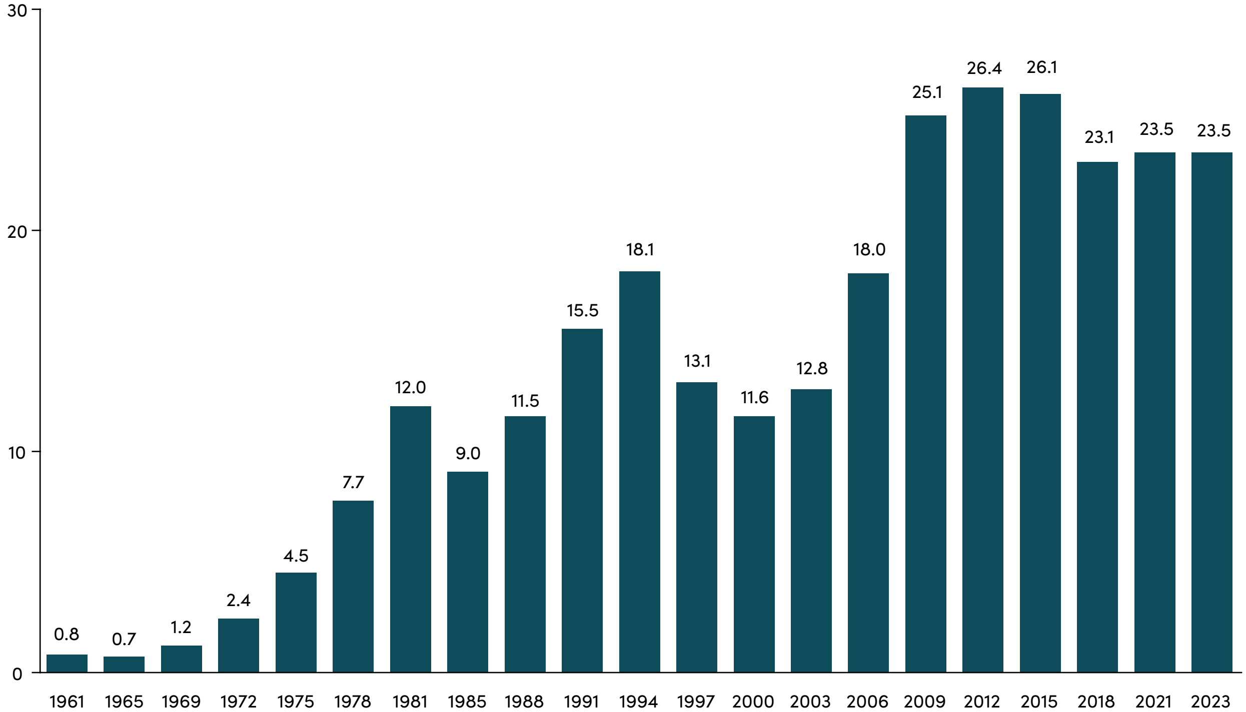
Falling donor contributions

IDA replenishment contributions have been consistently dropping over the last 10 years from their 2012 peak—despite the global recognition of the importance of supporting low-income countries confront the challenges. This is true across all categories of donors, including the G7, the G20 and OECD. The last replenishment, IDA20, was accelerated taking effect this financial year (2023 on the chart) meaning that on an annualized basis, donor contributions did increase. However, our analysis focused on replenishments as the basis for comparison, as this is more comparable historically and helps address data limitations (Figure 4).

In absolute terms, the contributions of the UK fell the furthest, from $4.2 billion to $2 billion between 2012 and 2023, a 50 percent drop. They were followed by Spain, which fell from just $1.1 billion to 350 million, or 67 percent less. The US dropped third most, from $4.1 billion in 2012 to $3.5 billion in 2023, a 15% drop. Excluding countries whose contributions fell to zero, 14 other donors saw declines of over 10 percent, among them G7 members Italy, Germany, Australia, and Canada. The only G7 that didn't decline was France, which increased its contributions by $20 million, or 1 percent.

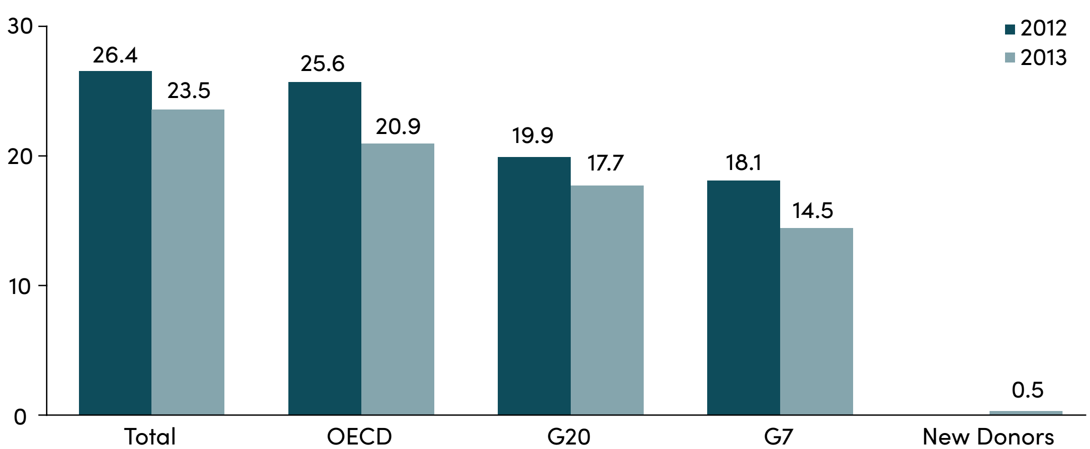
21 https://www.cgdev.org/blog/should-mdbs-be-leading-adoption-debt-pause-clauses
22 https://unctad.org/news/global-economy-gets-covid-19-shot-us-stimulus-pre-existing-conditions-worsen

FIGURE 4. IDA replenishment donor contributions (USD billions)



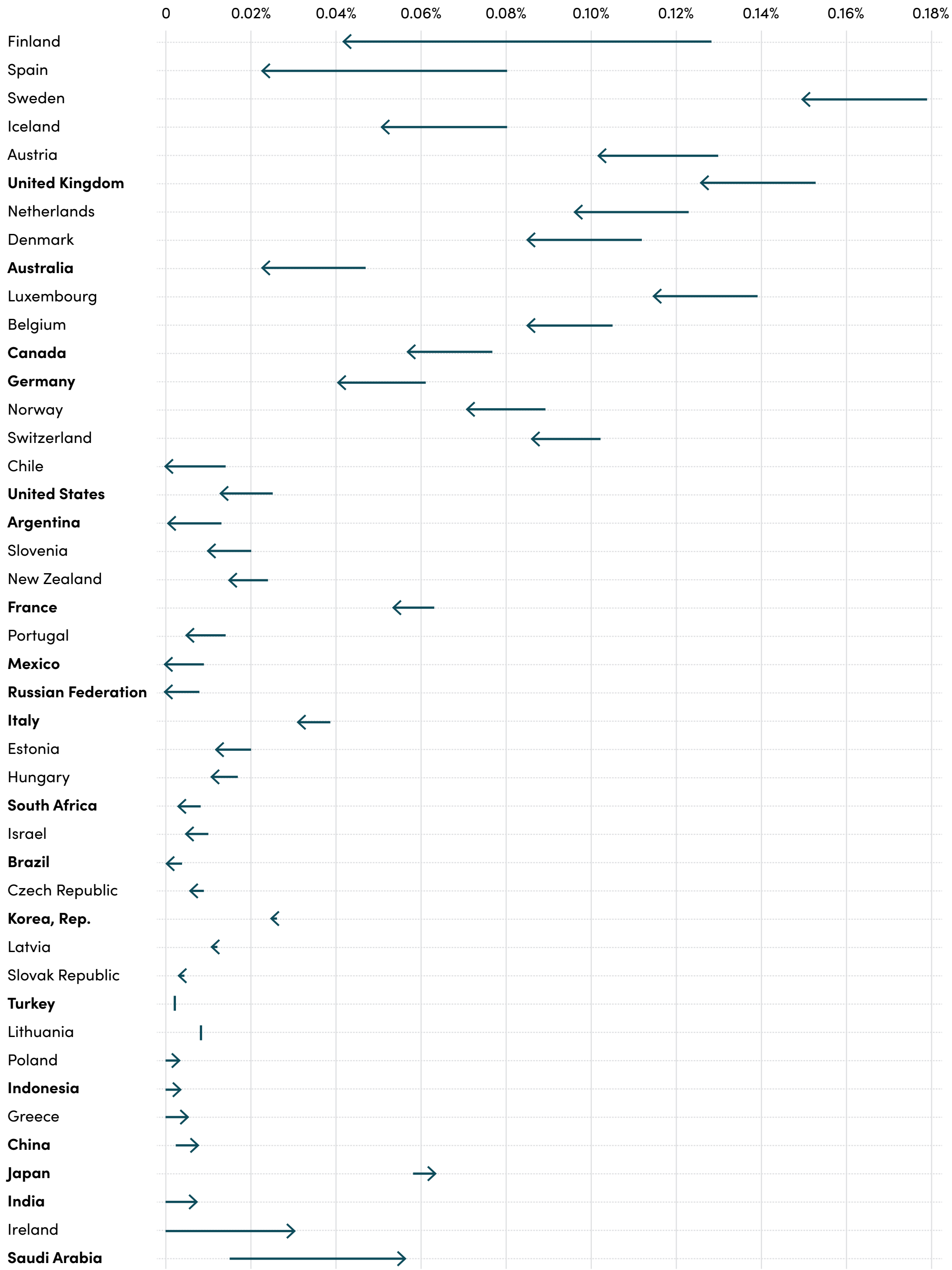
Source: Scott Morris, Oxford Review of Economic Policy
Note: Year corresponds to start of effective period.

FIGURE 5. IDA donor contributions, by donor category (USD billions)



Source: World Bank

FIGURE 6. IDA donor contributions / GNI (OECD + G20)



Source: World Bank
Note: Arrow indicates direction of change from 2012 to 2021; bolded countries are G20 members. Colombia and Costa Rica did not contribute, and so are not pictured. IDA Replenishment Contributions (USD) / Current GNI (USD).

Particularly troubling is that IDA contributions have declined even as donor economies have grown significantly. In GNI terms the picture is bleaker. Following the pledge of developed countries to contribute 0.7 percent of GNI for development,[23] in 2021, no country contributed more than 0.16 percent of GNI to IDA.[24] Sweden, UK, Luxembourg, Austria, and the Netherlands lead the pack in GNI terms, but even they have dropped precipitously since 2012. France, Japan, and Germany sit at less than 0.07 and the US at 0.03 percent of GNI. Overall, though 12 existing (non-new) donors registered increases in absolute terms between 2012 and 2021, only 7 saw increases in GNI terms. Of these, only one was a G7 country—Japan, and its positive trend could potentially reverse when its 2023 contribution, which was lower than it was in 2012, can be compared to 2023 GNI.[25]

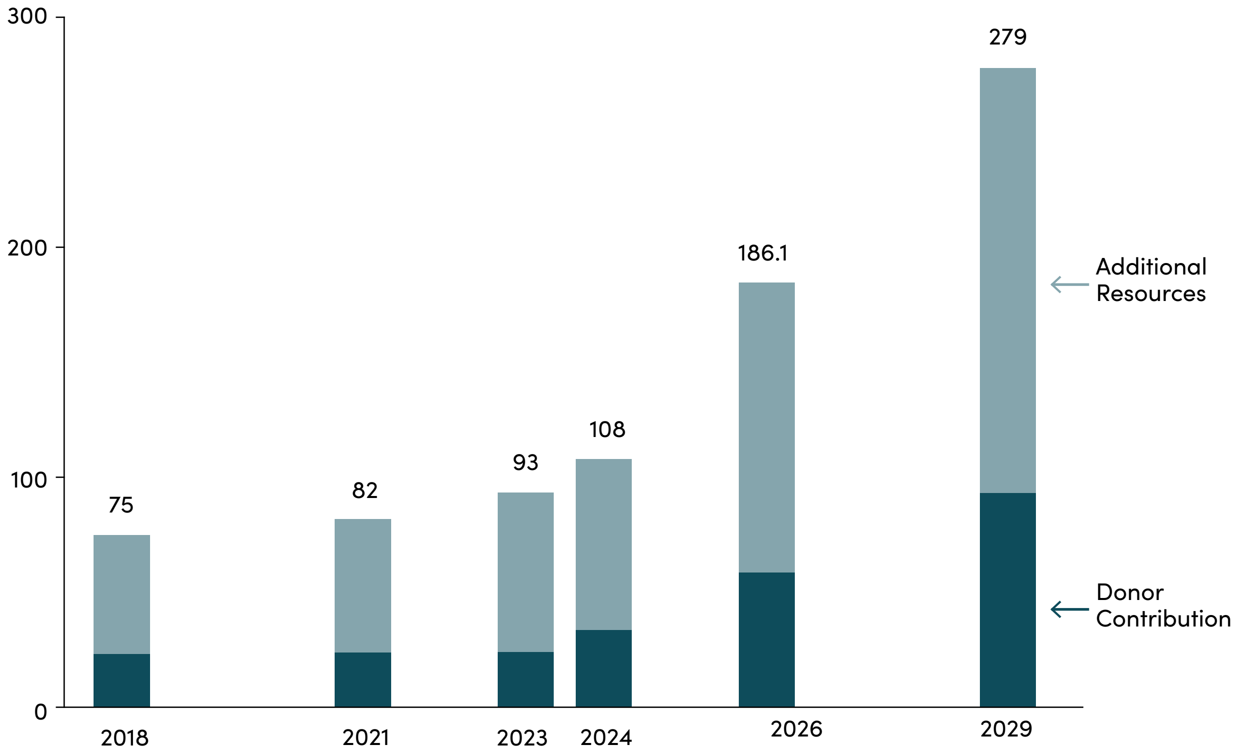
Over the years IDA has seen an increase in new donors contributing a total of nearly $500 million between 2012 and 2023. The donors with the biggest increases in absolute terms over that period were China, Saudi Arabia, and Korea, all relatively younger donors. Maintaining this momentum by continuing to recruit and encourage new donors is crucial for IDA's long-term growth. However, IDA will need to address the governance challenges that could result. Moreover, while the contributions of new and young donors such as China and Saudi Arabia are welcome and significant, as shown is Figure 5 above, they are far from enough to make up for the drop of the traditional donors.

These figures show that the G7 countries severely underperform on IDA.[26] Far from rising to the unprecedented crises facing the world today, they have failed to even match prior contribution levels. At a time when IDA needs more resources to help countries out of debt crises, relaunch growth, and deal with worsening climate shocks, it is receiving less support from donors—particularly the richest ones—than it did a decade ago. Donors' declining support for IDA sits within a larger trend of a growing share of ODA passing through bilateral agencies and specialized vertical funds and institutions.[27] While these new channels have contributed to an overall increase in aid flows in recent years, the fact that their share is increasing while IDA's is falling suggests that donors are leaving significant value on the table. Bilateral agencies and specialized vertical funds may cater to a particular political priority among donor countries, but they lack the combination of concessionality, breadth, and, crucially, the leverage offered by IDA.

In forthcoming replenishment cycles, IDA's deputies should be explicit in reminding donors about the institution's unique value proposition relative to more limited alternative ODA channels. Despite IDA's strong performance in recent years, current commitment levels are far below the enormous needs facing low-income countries. To reliably increase IDA contributions to the scale outlined in the

23 https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/the07odagnitarget-ahistory.htm
24 Our GNI analysis only goes to 2021 because 2023 GNI data has not yet been published.
25 This is very much an open question, since Japan's GNI per capita experienced a peak of $6.45 trillion in 2012, compared to $5.13 trillion in 2021 (current USD).
26 G7 members include Canada, France, Germany, Italy, Japan, the United Kingdom and the United States
27 https://www.brookings.edu/wp-content/uploads/2016/06/11_development_aid_kharas.pdf

FIGURE 7. IDA replenishment donor contributions—future case (USD billions)



Note: 2029 donor contribution projection obtained by tripling 2012 donor contributions in GNI terms, applied to 2021 GNI. For countries that did not contribute in 2012, whatever their maximum contribution in GNI terms was since 2012 was instead used. 2026 donor contributions represent the midpoint between 2023 and 2029. 2024 contributions maintain the same ratio of donor contributions to additional resources as in subsequent years.

Songwe et al. report, all donor countries must commit to tripling their IDA allocations up from their 2012 peak, which will give IDA a shot at tripling its overall replenishment packaged in 2029 to 279 billion.

A first and important point will be top up IDA20 so that it maintains its level of commitments in FY23–FY25 at $38 billion, as the world faces the continuous tightening of interest rates, the persistence of the war in Ukraine, and a sluggish recovery now projected for both China and the US and worries around financial stability.[28] Any one of these conditions would require extraordinary support, but combined and against the backdrop of a persistent climate crisis it is important that IDA continue to provide low-income countries with the liquidity, stability, and predictability they need to develop new resilient and sustainable growth agendas.

28 As the current IDA20 level, IDA could only commit $31 billion per year.

Long-term, it is now commonly agreed that an incremental approach to development has not delivered the outcomes expected and must be dramatically scaled up. The frequency and magnitude of the crisis also calls for acceleration on the development front to stay a foot ahead.

Though IDA has successfully generated consistent increases in its overall replenishment package since 2012, a growing share of this comes in the form of additional resources, including reflows on its loan portfolio, and, increasingly, market borrowing against its balance sheet.[29] However, while these flows will continue to make up a significant share of future IDA replenishments, in the face of even bigger challenges more donor resources will be needed. There is no scenario where IDA reaches the level of ambition described by Secretary Yellen without at least a tripling of donor contributions to complement IDA stretching its own balance sheet and working in concert with other partners to raise additional resources. In return, IDA countries must continue on the reform path. This would see all categories of donors collectively raising their contributions to $92.4 billion, which would give IDA a shot at a $279 overall replenishment.

Honoring pre-existing global aid commitments to the poorest countries is the key to tripling IDA. Though rich countries committed to spending 0.7 percent of their GNI on development in 1970, but very few have met this mark.[30] The development community needs to at least hold countries to account on their IDA contributions. Given the importance of IDA the G20 may want to consider having a target contribution for countries based on their GNI. For example, a target of 0.1 percent of GNI across IDA donors would more than deliver the $92.4 billion needed by 2029; a more ambitious .15 percent of GNI would deliver over $135 billion.[31]

To reach these goals, IDA needs a permanent and persistent global advocate. The G20 trio—including the past, current, and future country chairs—again could take the ownership of IDA and support its replenishment process every three years by setting the standard for contributions as a percentage of GNI and monitoring performance as part of their agenda.

Additional donor support can come in innovative ways beyond the traditional paid-in capital. For example, donors could also consider more guarantee capital which will allow IDA to raise more market financing against its balance sheet, as the Asian Development Bank (AsDB) plans to do in its recently launched IF-CAP initiative to drive up climate financing.[32] The African Development Bank (AfDB) is also innovating on its balance sheet and a joint collaboration between IDA and the AfDB would allow for more efficient allocation and use of resources. These innovations should be attractive to donor countries, who will have to set aside less cash than they would for a traditional capital infusion.

29 https://www.cgdev.org/blog/road-better-world-bank-starts-commitment-ida
30 https://www.oecd.org/dac/financing-sustainable-development/ODA-2022-summary.pdf
31 Assuming GNI growth across donors.
32 https://www.cgdev.org/blog/if-cap-recap-asian-development-banks-big-climate-finance-bet

Innovations to meet outsized demand for IDA

IDA countries need more resources than IDA can deliver. This has led many to resort to the market for additional resources at very onerous rates. Even with a tripling of resources on the donor side, IDA itself will have to innovate to deliver a tripling of its overall replenishment package. There are several ways IDA could stretch its balance sheet and provide additional resources to countries, especially under the current high cost of capital environment.

One such way is further differentiation in pricing for different categories of IDA countries based on market access. In 2012 only 14 of IDA countries had access to markets. Today over 23 countries have crossed this hurdle. No IDA country is rated investment grade (Baa3 and above). Countries' reluctance to sign onto the DSSI until they were confident it would not affect their credit ratings illustrates the value country finance ministries ascribe to having access to market borrowing.[33]

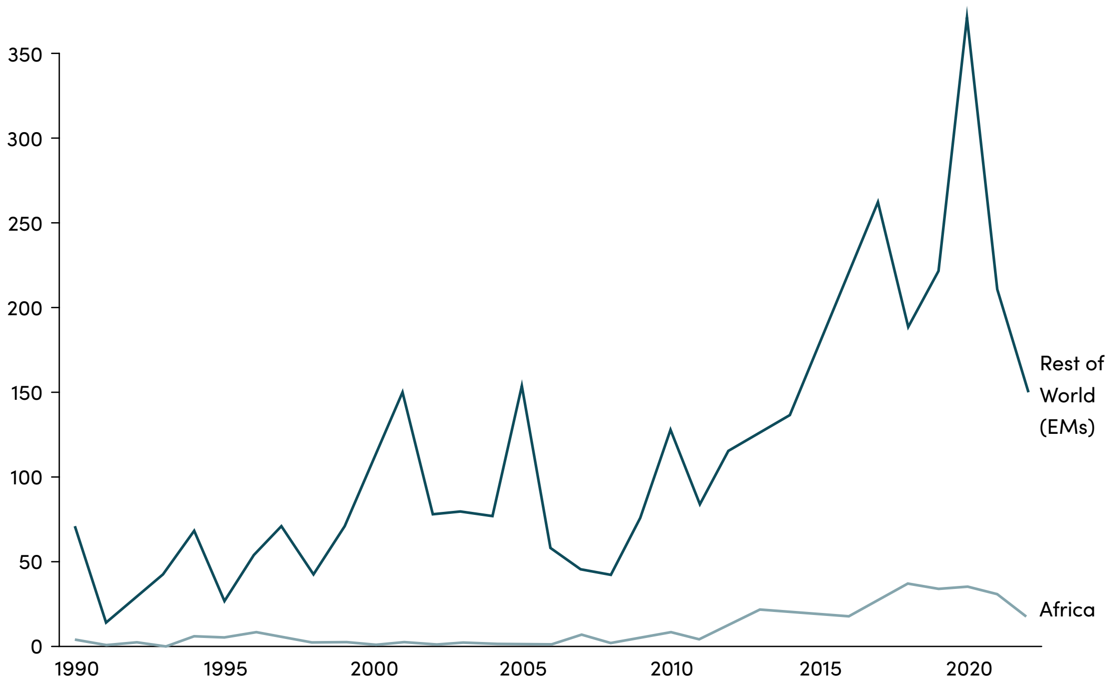
Many IDA countries gained this access in the growth years, when China drove a boom in commodity demand, and Africa was growing near 6 percent consistently for 8 years.[34] This was also a period of political opening up, which mean that leaders had to deliver for their citizens to get elected.

As growth accelerated, so did Eurobond issuances by IDA countries. For many countries, these translated into clear improvements in infrastructure outcomes, such as in Senegal and Ivory Coast, and Ghana, which saw transformational infrastructure projects like the upgrading of the Ghana's Tema port.[35] Access to electricity and the coverage of paved roads increased,[36] as did the number of health facilities and social safety net projects.[37]

By the middle of the 2020s many countries were raising twice or triple the annual IDA commitments through the market. However, this market access came at a steep cost. In case of Kenya in 2018, for example, while IDA concessional resources were offered at blend terms featuring a 5-year grace period, 30-year maturity, and 286 bps in combined interest and service charges, the cost of a 10-year Eurobond was nearly 800 bps, or over three times the cost of IDA.[38] The similar dynamic can be observed for Ghana, Senegal, Cameroon, Nigeria, and others, as shown in the Annex. Despite this premium, countries repeatedly tapped markets. A common attraction of the Eurobond is the speed at which countries can get the resources and the lower conditionality hurdles placed on the resources.[39]

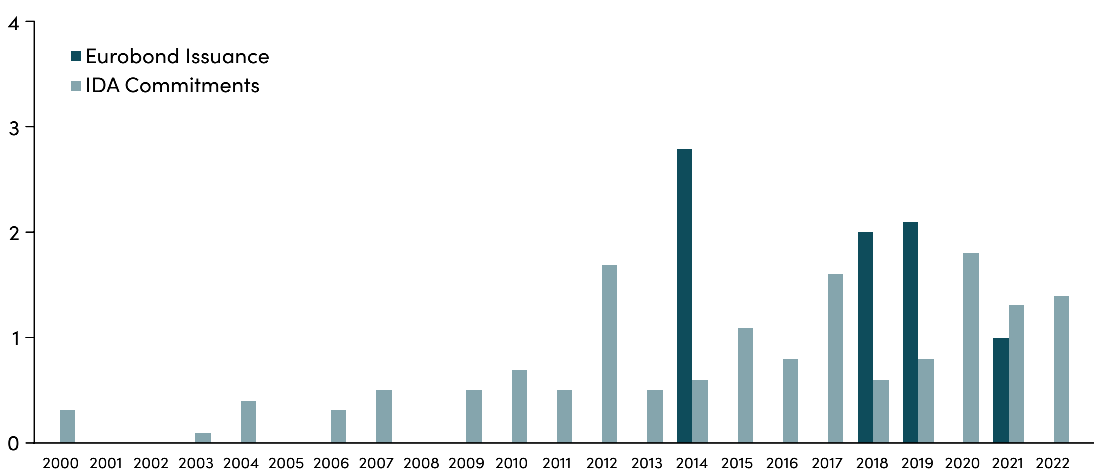
33 https://www.whitecase.com/insight-alert/g20-debt-service-suspension-initiative-reaction-key-market-participants
34 https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2021&locations=ZG&start=1995
35 https://aecom.com/projects/tema-port-expansion/
36 https://www.emerald.com/insight/content/doi/10.1108/OXAN-DB216786/full/html
37 https://www.presidence.sn/en/pse/results-and-perspectives
38 Bloomberg; https://thedocs.worldbank.org/en/doc/7cb32aa38021648e61669cd86d23e899-0410012018/original/ida_terms_effective_july_01_2018_updated_july_17_2018.pdf
39 https://www.imf.org/en/Publications/fandd/issues/2021/12/Africa-Hard-won-market-access

FIGURE 8. Eurobond issuance, Africa and other emerging markets (USD billions)



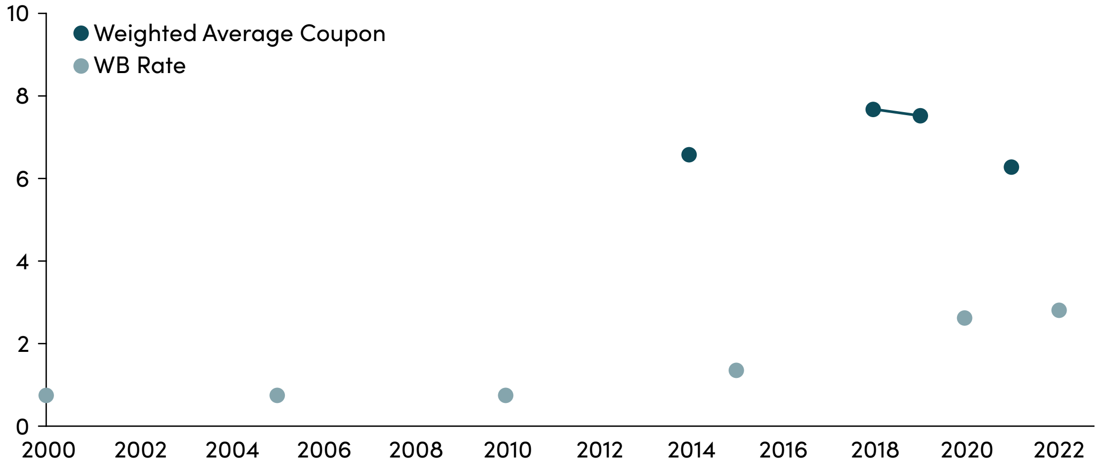
Source: Bloomberg

FIGURE 9. Kenya borrowing volume (USD billions)



Source: Bloomberg

FIGURE 10. Kenya borrowing costs



Source: World Bank, Bloomberg

While market access is important, what is clear is that market access at unsustainable rates is an accelerator of debt distress.[40] With grace periods, longer maturities, and significantly lower interest rates that what the market provides, IDA has room to raise rates for countries with solid macroeconomic and debt sustainability frameworks while still ensuring that its credits are significantly cheaper than market borrowing. Compared to market borrowing of the same volume, this would reduce debt sustainability risks in the long-term and free up fiscal space for development spending in the short and medium term. And with rates slightly higher for some borrowers, new credits will also generate greater reflows in the future, which IDA could then funnel back into its equity for expanded market borrowing. This process would supplement donor contributions, and ultimately result in a larger pot of resources for all IDA borrowers moving forward.

A differentiated loan pricing model has precedent—IBRD introduced one in 2018.[41] The details of implementation—which countries would see rate increases, and by how much—are delicate, and will require further analysis. In addition, ensuring sufficient demand for increased IDA credits in lieu of Eurobonds will require IDA to mimic the speed and efficiency of the Eurobond market, limiting excessive conditionality, and increasing the rate at which commitments are disbursed. This would mean generated quicker-disbursing development policy financing (DPF) type packages mirroring the efficiency and ease of Eurobond issuance for relatively richer IDA borrowers, while allowing for additional real grant resources to be directed to the conflict and fragile affected countries who need cheaper financing. Greater speed would also have added benefits—faster disbursements would help

40 https://www.un.org/osaa/sites/www.un.org.osaa/files/docs/2118580-osaa-eurobonds_policy_paper_web.pdf
41 https://www.devcommittee.org/sites/dc/files/download/Documents/2019-04/DC2019-0003-PIBRDIFC%20capital%20package%204-13.pdf

IDA's make a stronger contribution to crisis financing, by allowing its commitments to reach receipts more quickly in the wake of costly natural disasters.

Capacity building

As part of the contract between IDA and countries it will be important to help build the capacity of countries to prepare and implement country strategies, reforms, and projects and strengthen overall financial management in all relevant agencies. This is even more important as countries now need to use a sustainability and global public goods lens when making decisions.

While providing financing directly with greater speed and innovation, IDA could also provide market access-oriented technical assistance grants, working with bilateral donors, philanthropy, and other like-minded NGOs. Given its local and sectoral knowledge, debt sustainability analysis capabilities, and policy influence, the WBG is uniquely placed to work with the private sector to build capacity of countries in this domain. Knowledge products, country strategies, and platforms could complement project-specific risk mitigation for transformational infrastructure investments, including through guarantees, which would further improve countries' market attractiveness. These capacity-building activities could benefit public good challenges at the local, regional, and global level, including climate-aligned investments. However, building capacity across all these levels will require a revamped MDB system with substantive additional resources.

In many low-income countries, the private sector will not be the first mover. In these contexts, public sector entities will have to take a share of the risk in foundational, transformational projects and adopt the right financial instruments, policies, and regulatory framework to eventually attract private capital. It is through these projects that countries will adopt new transformational energy options, build more resilient societies, protect their human and natural capital, and lay the groundwork for self-sustaining investments.

As identified by Gardner and Henry in their 'twin hurdle model', regardless of the source of financing, projects undertaken must demonstrate a rate of return that exceeds the cost of resources, both domestic and foreign.[42] Too often, low income country projects exceed only the cost of domestic capital, with the cost of private foreign capital far higher than even a well-designed project could hope to return.[43] With more concessional resources available to countries from IDA, it is more likely that well designed projects with high development impact can clear both hurdles. Designing these projects requires capacity and knowledge of the de-risking tools available to make the project attractive to investors. Capacity building from IDA is critical for this.

42 https://www.lse.ac.uk/Events/Events-Assets/PDF/2021/02-ST/20210603-The-Global-Infrastructure-Gap.pdf
43 See Annex 1 for an illustration of high private foreign capital costs in SSA.

IDA lending can be a powerful tool for leveraging the private sector at scale to accelerate growth. But to do this effectively, IDA will have to make greater use of catalytic instruments which lower the cost of foreign private capital, including credit guarantees and other credit enhancement instruments. In some cases, IDA could even serve as an equity investor alongside a sovereign government. Many low-income countries are carrying and managing assets which could be off-loaded to the private sector; IDA could help countries with asset recycling deals which will free up capital and human resources for new development investments. IDA working with the IFC can provide support for these and other private capital market developments.

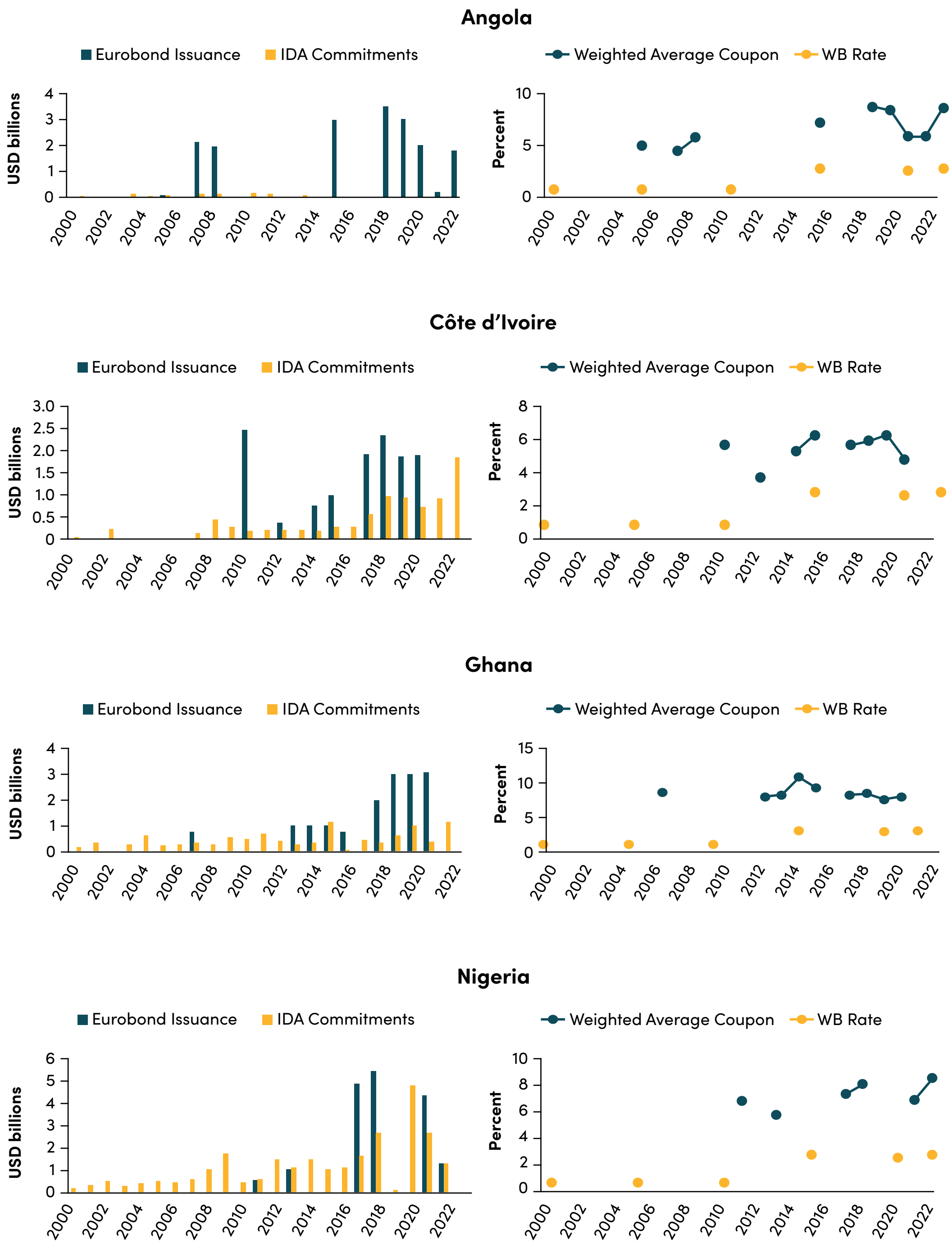
A social contract with the SDGs

The choice is clear. After declining for a decade, world hunger is on the rise. Approximately 50 percent of IDA borrowers are in, or at risk of, debt distress. Across the Global South, climate disasters are getting worse, destroying infrastructure, increasing conflict, and forcing people from their homes. In many countries, democracy is also under threat as leaders can no longer honor the social contract as the combination of high food prices, expensive health care, and lack of access to markets is eroding livelihoods. The challenges are compounding, and time is short.

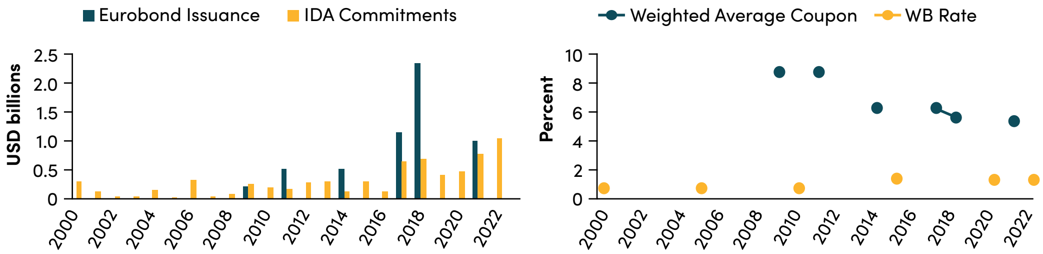
Building a new social contract between shareholders, countries, IDA, and the private sector is crucial for the success of any accelerated response to the development challenges at hand and the achievement of the SDGs. However, each must play their role of providing adequate and timely funding, adequate implementation support, and the right policy space for impact, speed, and scale respectively. Never have all these conditions been so aligned. All that is needed is action.

Annex

FIGURE A1. Market and IDA borrowing volume and cost of select African sovereigns (USD billions, percent), excluding bonds with tenor <5 years



Senegal



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