FINANCING THE SUSTAINABLE DEVELOPMENT GOALS: THE CRITICAL ROLE OF RISK AND RESILIENCE

Earthquakes, cyclones, droughts, conflicts, Ebola, economic crises and commodity price shocks. Shocks and stresses strain countries and communities, and set back development. For the Financing for Development (FfD) agenda, this issue is critical. Volatility is the world's new normal.

- 17 Ambitious Development Goals
- Every sector of Life and Living
- Volatility rising

This is not financial business as usual.

This document is part of an ongoing project by UNDP and the Government of Switzerland to highlight the critical need to appreciate the role that shocks and stresses play in development, and the role of risk and resilience considerations in all forms of finance – public and private, national and international – play in achieving long-lasting sustainability.

As part of this work a technical workshop on the 28th May 2015 in New York City. At this event close to 20 external experts joined a UNDP team to consider the latest Addis outcome document (1). This document builds on the results of that workshop to present a set of messages to Financing for Development (FfD) decision-makers. It should be noted that it does not represent an official opinion of either UNDP or the Government of Switzerland, nor the expert representatives who have contributed to its development.

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KEY MESSAGES: Overarching

Shocks and Stresses are Inherent to Development

The development process is inherently complex and non-linear, and shocks and stresses are part and parcel of its progress. Development needs to be rethought where investments in risk and resilience are part of the process. This rethink demands a financial articulation.

Successful Development is Not 'Business as Usual':

The current draft of the FFD Action Agenda document implies that, in our ever-more complex and inter-connected world, and the very ambitious nature of sustainable development goals currently being discussed, a different model of financing than was reached in the Monterey Consensus on Financing for Development is needed (2). That model said little about the need to target the financing of risk and resilience. Yet, we live in a volatile world, one where shocks and stresses are the new norm, and becoming more frequent and more severe. The human costs are high. Climate change is arguably the most important long-term stressor on development. There are human and financial implications of this new reality.

The Cost of Crisis Needs to be Articulated:

The cost of crises, the cost of inaction, needs to be articulated by the Action Agenda. There needs to be more discussion on the seemingly intractable rise of humanitarian spending (which has now reached close more than US$24 billion a year, three times more than a decade earlier (3)), the challenge countries face in mobilizing funds during crises and shocks, or the costs of failing to transition out of crises situations. In 2007 the cost of conflict in Africa was estimated to be at least US$284 billion, representing an average annual loss of 15% of Gross Domestic Product (4). Similarly, some consideration is needed on consequential financial requirements arising from crisis, such as displacement (which has reached record levels this year at 59.5 million people, with average displaced time being 17 years (5)) or the impact of conflict across a border to a neighboring state. (Tanzania, for example, loses 0.7% of its annual GDP for each neighbor in conflict (6)). And more can be done to articulate the financial implications of 20 years of disasters (7) claiming 1.35 million lives and reaching up to US$3 trillion (8) in financial losses, or that some small island developing states lose the equivalent of 300% of GDP in a single disaster.

Development must be risk-informed in order for it to be sustainable:

Achieving sustainable development will be impossible unless nations and communities are resilient, able to anticipate, shape and adapt to the many shocks and challenges they face. Firstly, if development investments need to be risk-informed in order to be sustainable, each investment can add or reduce risk. Yet many investments do not have as their first motive the reduction of risk.

Secondly, investments now in prevention and preparedness for all hazards, natural to man-made, public health or energy, will minimize risk and future costs. And finally, crucial for the future, an understanding and articulation of risk, by stripping away the 'unknown' to incentivise growth. 'Risk-pricing' (the extra investment needed to ensure risk-informed development) is therefore essential for ensuring we have development plans able to face the challenges of shocks and crises. The price of risk needs to be factored into all development costs and investments.

The Evidence is clear: investments in resilience reduce losses and deliver on development:

Investing in early response to drought in Kenya could save US$20 billion over 20 years. Flood management in Mexico reduced losses by three times more than the needed investment costed. Yet this is only half the picture, since the investment in risk-informed development and broad resilience has much wider impacts. Investments in water-supply protection in Bolivia not only delivered 14 times more value than the original investment, they also increased water supply, irrigated area and household income. Such investments therefore help countries avoid losses, protect development and deliver co-benefits, including the unlocking of growth potential by tackling 'background' risk.

What are the consequential financial requirements arising from crisis, such as displacement (which has reached record levels this year at 59.5 million people, with average displaced time being 17 years)

KEY MESSAGES: Financing Approaches

Aid Needs To Be Better Targeted:

Currently aid is highly concentrated, with 10 countries receiving 37% of official development assistance (ODA) and the top 20 getting 56%. The share allocated to the poorest and most vulnerable countries, such as least developed countries (LDCs) and small island states (SIDS), has come under pressure; in 2014 bilateral aid to least developed countries fell by 16% (9). In addition, aid shocks are still a common occurrence, especially in the most fragile countries. The 'kind' of aid finance also matters for risk and resilience. For example, humanitarian financing (which adds little to long-term sustained development) is a sizable component of ODA to conflict-affected countries. The money that is invested in supported countries to reduce their disaster risk is largely spent in middle-income countries that have both more capacity and financial ability; over 20 years 12 of the poorest countries received a combined US$34.9 million on disaster risk reduction but US$5.6 billion of largely disaster-related emergency aid, one for every 160 dollars (10). Similarly drought-affected sub-Saharan African countries receive very little financing for disaster risk reduction at all. There needs to be a rethink in the way in which the limited ODA available is spent, both where and on what.

Private Sector Investment is Essential to Deliver on Development:

Resilience is as much an issue for private as it is for public financing. This is important for a number of reasons. Firstly, it is clear that the ambitious post-2015 development agenda (11) cannot be achieved by public finance alone, whether international or domestic. Secondly there is private money available that is actively looking for investment opportunities, such as the US$7.8 trillion of assets the mutual and cooperative insurance sector holds (12). Thirdly, the fact that between 70% and 85% of all global investment comes from the private sector demands attention, if we wish all development, for example to be truly risk-informed. Incentives for the private sector to responsibly focus on sustainable development should be a focus for the FfD Action Agenda. Financing discussions should focus on how private sector investments can be adequately leveraged towards sustainable development. This should also include the barriers to investment such as over-regulation, weak financial structure/oversight and a high level of uncertainty (especially in developing contexts.) How do we build the capacities of countries to develop and manage high quality projects? And what role is there for FfD in that capacity building?

Insurance has a critical role to play:

The insurance sector can help countries and communities reduce risk, recovery from shocks and support a return to a development path. The mapping out of climate risks, creation of resilient supply chains and supporting better health are roles that the insurance sector can play in building resilience. Shocks can destroy asset/capital bases - insurance can help protect those assets. Systems of social and financial resilience are key to protecting asset/capital bases from erosion on the account of crises.

Social Protection delivers long-term community and family resilience:

Social protection is a key element of community and family resilience, and is critical to the reduction of risk (through reduced vulnerability). The Addis Action Agenda refers to social protection as one of the cross cutting areas for provision of basic services to those below the poverty line. In line with this idea, promoting the use of crisis-linked social protection is critical since this mechanism provides immediate access to financial resources to least resilient populations.

Investing in early response to drought in Kenya could save US$20 billion over 20 years.

KEY MESSAGES: Thematic

Make infrastructure investments deliver on resilience, not contribute to risk:

Effective, reliable infrastructure underpins economic activity, and a failure to adapt, increases the possibility of adverse economic impacts. Ensuring all investments are risk-informed is an opportunity to reduce, rather than lock-in risk. An estimated US$6 trillion a year is to be spent between now and 2030 on new infrastructure, such as for energy, roads, houses, schools, hospitals and other public services (13). This investment needs to not only be informed by risk 'considerations', but also support the actual reduction of existing risks. These investments should also support the transition to economies that deliver growth and contribute to a reduction in climate change at the same time.

Make Climate Central to Discussions:

Climate change needs to play a central role in all our global development discussions. A changing climate is arguably the largest single global risk to sustainable development, there exists a significant investment from the international community in climate-related financing mechanisms, and both mitigation and adaptation can help deliver on sustainable development. The essential inter-related benefit of adaptation financing in both reducing the impact of climate change and supporting long-term development, is especially important for low-income countries and SIDS. The cost of adapting to climate change in developing countries alone is estimated to be at least US$70 billion per year through to 2050 (14).

Focus on Building out of Crisis:

Humanitarian financing is at an all-time high. Protracted crises last decades. Transition out of crisis appears impossible. At the same time there is much that can be done with sustained, predictable finance. Firstly, in those contexts of crisis and post-crisis, financing can increase the resilience of communities and countries (including those that may be 'hosting') through investments in social safety nets and multi-year planning cycles. Secondly, and more importantly, financing in protracted crises can tackle the underlying reasons for humanitarian need through realistic investments in peace, security, governance and long-term development. The financing discussions should articulate how fragile and conflict-affected states need particular financial solutions; without such tailored investment, close to 20 countries (and their populations) will not have sustainable development.

Enhance Macro-Economic Stability:

The impact of both internal and external shocks and stresses over the last ten years has proven the need for significant investments in macro-economic stability. On the one hand there is a need to enhance the debt management capacities of countries. Debt financing is not necessarily a negative, with it meeting urgent needs, maintaining fiscal stability, and creating new opportunities for risk-informed development; but it can also increase the risk of debt crises in the future. Access to the right kinds of finance is key to both mobilizing resources for resilience. Tools such as GDP-linked bonds and counter-cyclical loans are important innovations in financial instruments that can help reduce macroeconomic risk, and should be expanded post-2015.

Over 20 years, 12 of the poorest countries of the world received just US$1 on disaster risk reduction for every US$160 spent in those countries on disaster response

KEY MESSAGES: Operational

Build Capacity and Leadership:

The development of national capacity and national leadership is central to delivering on risk and resilience, and needs a much more prominent place within our future financing of sustainable development. Specific references that need to be emphasized include investments in human and institutional capacity, specifically capacity that enables countries to adequately govern risk (which includes investments in supporting institutions such as those responsible for financing and planning). This capacity should be extended to ensure the effective management and leverage of financial sources of all kinds towards ensuring development remains risk-informed.

Develop and use practical tools for risk-informed development:

Investments in resilience should focus on a set of measures to ensure that all investments in sustainable development consider the risks posed to development through shocks and stress. This includes significant investments in the better management and usage of the many assessments for risk already undertaken. It should include the financing of comprehensive risk assessments, such as social and political dynamics, drivers of risk, cross-border dynamics etc. These shared tools should then be used much more systematically to 'screen' investments in sustainable development for both the risk to that development (from issues such as conflict, disaster, climate) and the way in which that investment can impact on future development (and those same issues.).

Tailor the Channel of Delivery to the Task:

Both the international system and national governments should invest in innovative ways of delivering aid and social protection. For example, using cash rather than food and non-food items in crisis situations, will promote choice and empowerment, and help deliver resilience through stimulating local economies and markets. Technology must play its part, with mobile and internet technology increasingly being used to finance of social protection and emergency aid, especially in hard-to-reach areas.

FOLLOW UP

The messages presented here are designed to not only inform discussions on Financing for Development, but rather for the post-2015 development agenda in general, building political momentum and consensus around the need to change the current approaches to shocks. This work will therefore continue beyond the FfD Conference, to the SDGs, COP and beyond to the World Humanitarian Summit in 2016.

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References

1. For a full list of those who attended the workshop please contact Jan Kellett at UNDP, jan.kellett@undp.org