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International financial system and development

Report of the Secretary-General

Summary

The present report was prepared pursuant to General Assembly resolution 78/136, entitled "International financial system and development". The report provides an overview of current and emerging challenges for the international financial system in providing long-term financing for sustainable development in the context of a rapidly growing financing gap. Against a backdrop of escalating global risks, the report calls for urgent action to rapidly accelerate the pace and scale of reforms in the international financial system and architecture and to increase investments in the Sustainable Development Goals at an unprecedented scale. Priority actions to achieve those aims include a strengthening of the global financial safety net; bold measures to scale up multilateral development bank finance, including early consideration of replenishments and capital increases, efforts to raise new capital and the rechannelling of special drawing rights; the strengthening of debt crisis prevention and establishment of a more effective debt crisis resolution mechanism; efforts to advance progress on the regulatory agenda to create financial markets that are accessible, stable and sustainable; and efforts to enhance the voice and representation of developing countries in global economic governance. The report points to the Summit of the Future, to be held in September 2024, and the Fourth International Conference on Financing for Development, to be held in June 2025, as important venues for discussions on such reform.

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I. Introduction

1. Reform of the international financial system continues to be a top policy priority as tight global financial conditions, geopolitical uncertainty and the lingering economic effects of the pandemic weigh on the outlook for financing for development for countries worldwide. The existing international financial architecture has been unable to support the mobilization of stable, long-term financing at scale for the investments needed to combat the climate crisis and achieve the Sustainable Development Goals. It is plagued by deeply rooted inequities, inconsistencies, gaps and inefficiencies. Despite the progress made in some areas in the aftermath of recent crises, reform of the global financial system and international financial architecture remains an unfinished task.

2. Developing countries, particularly the poorest countries, suffer disproportionately from the failure of the international financial system to deliver adequate, stable and affordable long-term financing to support sustainable development. As the financing gap for the Goals continues to expand, there is a need to transform the system, including through a shift from short-term, volatile financial flows to investment oriented towards the long term; from a misalignment with climate and sustainability objectives towards sustainable finance and investment; and from boom and bust cycles, a lack of access to affordable long-term finance and investment, and repeat cycles of debt crises and distress towards a stable, resilient and inclusive international financial system.

3. Recently, the uneven recovery from the coronavirus disease (COVID-19) pandemic and adverse global economic trends, such as tight monetary conditions, have exacerbated developing countries' financing challenges. Over the past five years, many developing countries have experienced declines in capital inflows, as well as continued volatility. High interest rates and higher costs of capital also have a negative impact on capital-intensive investments in the energy transition. These trends have posed challenges for policy at all levels. The global financial safety net continues to be severely stretched, and access to it is uneven. At the same time, the ability of countries to invest in the Goals is being severely curtailed by high levels of sovereign debt, which is increasingly mediated by the market.

4. Underlying factors behind these challenges include insufficient alignment of the international financial architecture with sustainable development and shortcomings in global economic governance. Despite the commitments set forth in the financing for development outcomes, very limited progress has been made towards enhancing the voice and representation of developing countries in global economic governance.

5. Financial regulators also face acute policy challenges, as they are tasked with preserving financial sector stability and, increasingly, with considering sustainability implications, amid volatile financial market conditions.

6. The Fourth International Conference on Financing for Development, to be held in 2025, provides a unique opportunity for the international community to address these and other shortcomings in the international financial system and strengthen the system's ability to weather crises and support climate action and the achievement of the Goals. As global financing efforts stand at a crossroads, Conference participants will seek a viable path forward for reform of the international financial architecture, building on the ongoing discussions in multiple forums, such as the United Nations, the Boards of the World Bank and the International Monetary Fund (IMF), informal country groupings such as the Group of 20 and the Group of 7, and country-led initiatives, such as the Bridgetown Initiative for the Reform of the Global Financial Architecture and the Paris Pact for People and the Planet. The present report contains specific proposals for reform, building on the proposals made by the Secretary-

General for a Sustainable Development Goal stimulus and reforms to the international financial architecture.[1]

II. Trends in capital flows

7. Developing countries have experienced numerous surges and reversals of capital flows over the past two decades. After a period of high inflows amid low global interest rates, in 2019 many developing countries, in particular the least developed countries, began to experience a decline in external financing inflows, a trend that worsened with the onset of the pandemic. By the second half of 2022, net financial flows to developing countries had turned negative.[2]

8. Sovereign debt flows mirrored that trend: the net flow of external public sector debt from private creditors to developing countries turned negative in 2022, and developing countries with the poorest credit ratings essentially lost access to international bond markets. Multilateral institutions played a critical role in preventing a net outflow of public sector debt from the least developed countries and middle-income countries in 2022, counteracting the net outflows to bondholders.

9. Since early 2024, there has been a resurgence in sovereign bond sales for some developing countries, driven by expectations of interest rate cuts in major developed economies. Bond issuance by developing countries amounted to a record $45.5 billion in the first quarter of 2024, but the distribution is highly skewed towards a few countries, and borrowing costs, while lower than in late 2023, remain elevated, especially for countries with non-investment-grade ratings. This uneven and costly market access poses challenges for debt sustainability and public spending.

10. At the same time, growth in foreign direct investment (FDI) has been less robust in recent years, with FDI flows to developing countries falling by 7 per cent in 2023, to $867 billion.[3] This decline follows a prolonged period of slow growth in investment. The global financial crisis of 2008 and 2009 has proved to be an inflection point: for the past 15 years, FDI flows have no longer been keeping pace with gross domestic product (GDP) growth and global trade. The deceleration in FDI is particularly evident in the manufacturing sector, which has posted negative growth in the post-pandemic period as asset-light forms of investment have become more important in a digitalizing global economy. FDI patterns have also been affected by geopolitical considerations, as trends such as "nearshoring" and "friendshoring" have emerged.

III. A global financial safety net and monetary system under duress

11. Despite some progress in recent years, the coverage of the global financial safety net remains highly uneven, and the safety net has been stretched by the recent confluence of shocks and crises. Developing countries are particularly affected by uneven access. Providing greater access to mechanisms that can support countries in times of crisis is an urgent policy priority in a context of rising systemic risks and vulnerabilities in the global economy, which contributes to financial instability. The

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[1] See "Our Common Agenda policy brief 6: reforms to the international financial architecture" (A/77/CRP.1/Add.5); see also United Nations, "United Nations Secretary-General's SDG stimulus to deliver Agenda 2030", February 2023.

[2] *Financing for Sustainable Development Report 2024: Financing for Development at a Crossroads* (United Nations publication, 2024).

[3] *World Investment Report 2024: Investment Facilitation and Digital Government* (United Nations publication, 2024).

Fourth International Conference on Financing for Development will provide a platform to galvanize action towards a strengthened and more equitable global financial safety net.

12. The global financial safety net is a set of institutions and mechanisms aimed at providing financial protection against crises and helping to mitigate their impact. The safety net is intended to provide countries with insurance against crises in the form of short-term liquidity finance when shocks hit. It comprises four main layers of resources: the international reserves held by each country; bilateral currency swap arrangements between central banks; regional financing arrangements through which countries can pool resources to increase financing in a crisis; and financing from IMF.

13. The gross reserves held by countries are by far the largest component of the global financial safety net. Since 2000, the total stock of international reserve holdings has increased more than sixfold, reaching $14 trillion at year-end 2022. Over the same period, emerging markets added $5 trillion to their reserves, and low-income economies accumulated more than $4 trillion. Broken down by region, 43 per cent of reserves are held by countries in East Asia, while 22 per cent are held by European countries. African countries hold just 3 per cent of total reserves.

14. Between 2000 and 2022, the amount of external resources available through the other safety net layers grew nearly 16-fold, to around $3.5 trillion. The global network of swap lines expanded dramatically in response to the world financial and economic crisis of 2008 and the COVID-19 pandemic, to a total of $1.6 trillion. Nevertheless, very few developing countries have access to such facilities.

15. Regional financing arrangements have so far played a limited role in the global financial safety net. Developing economies have access to five such arrangements, which had a combined lending power of $360 billion in 2022, a mere fraction of that of the bilateral currency swaps. Requirements for some of these facilities explicitly include the existence of a programme with IMF to gain access to larger volumes of liquidity. Use of these arrangements has been marginal.

16. IMF is designed to be at the centre of the global financial safety net and has issued around $270 billion in total disbursements since 2020. Since 2008, IMF has approved an average of 17 new programmes each year, half of which focus on providing concessional financing to developing countries. In September 2022, IMF established a temporary Food Shock Window under its emergency financing instruments to support countries facing urgent balance of payment needs related to the global food crisis.

17. In December 2023, the IMF Board of Governors approved its sixteenth general review of quotas, raising IMF member quotas by 50 per cent. Once implemented, it will bring the total quotas of IMF, which are permanent resources, to 715.7 billion in special drawing rights (SDRs) ($960 billion). In March 2023, the IMF Executive Board agreed to temporarily increase the limits on members' annual and cumulative access to the General Resources Account – to 200 per cent and 600 per cent of quota, respectively – for a period of 12 months, which has since been extended to year-end 2024. In December 2023, the IMF Executive Board agreed to temporarily increase the limits on access to concessional funds through the Poverty Reduction and Growth Trust – to 200 per cent and 600 per cent of quota, respectively – to match the increase in the limits on access to non-concessional funds until year-end 2024.

18. Alongside the increase in lending, more countries have been paying IMF surcharges, which add extra costs for precisely those countries that face the most severe balance of payment challenges. In all, 23 countries have paid surcharges in 2024; in the 2023 fiscal year, IMF collected almost $2 billion in surcharges. In early 2024, IMF agreed to conduct a review of its surcharges policy following calls by the

Secretary-General and many other actors to lower or remove them altogether so as to free up resources for borrowing countries that have large needs for investments in the Goals.

19. SDRs, an international reserve asset created by IMF in 1969 to supplement its member countries' official reserves, were successfully allocated twice in crisis situations in the past 20 years. The quota-based allocation of SDRs, in proportion to countries' quota shares at IMF, means that developing countries received around one third of the $650 billion worth of SDRs allocated in August 2021 in response to the COVID-19 pandemic.

20. Following the allocation of SDRs in 2021, some IMF members with sufficient reserves and strong external positions agreed to voluntarily rechannel SDRs to countries in need. Countries have pledged to rechannel over $100 billion in unused SDRs, mainly to the Poverty Reduction and Growth Trust and the Resilience and Sustainability Trust. Given that a large portion of SDRs on central bank balance sheets in developed countries remains unused (around $500 billion in total), there have been calls for additional rechannelling of SDRs, including calls for developed countries to rechannel 50 per cent of their remaining unused SDRs.

21. While efforts to rechannel unused SDRs have so far been focused on the Poverty Reduction and Growth Trust and Resilience and Sustainability Trust at IMF, several multilateral development banks, which are prescribed holders of SDRs, have also explored modalities to rechannel SDRs. The African Development Bank, jointly with the Inter-American Development Bank, has put forward an innovative proposal for a mechanism that would allow countries to rechannel their SDRs to the two banks, which would then leverage those SDRs as hybrid capital to provide long-term financing for development and climate projects. The instrument would require a minimum of five contributors and would have a multiplier effect, leveraging SDRs by up to five times while enabling them to maintain their status as reserve assets. On 15 May 2024, the IMF Executive Board approved the rechannelling of SDRs to multilateral development banks through the purchase of this type of hybrid capital instrument, albeit with an initial cap of SDR 15 billion (approximately $20 billion). The decision represents an important and innovative step towards expanding finance for sustainable development, in line with the Sustainable Development Goal stimulus proposed by the Secretary-General, and could unlock up to $100 billion in financing for developing countries.

22. After the onset of the full-scale financial crisis in 2008, it took 11 months to approve the issuance of SDRs; after the onset of the pandemic in 2020, it took 17 months. To combat crises more effectively, there should be greater automaticity in consideration of SDR issuance. Agreeing to triggers that automatically generate a recommendation on SDR issuance when conditions are met could help to prevent political delays. If SDRs are to play a larger role in buffering external adjustment or providing a flexible source of financing to bolster IMF lending capacity, the Articles of Agreement of the International Monetary Fund will need to be revised, but the IMF Executive Board could, on its own, agree to triggers that would automatically generate a recommendation for SDR issuance.

23. With the expected increase in systemic risks and the growing frequency and intensity of crises, including those related to climate change, there is a clear need to further strengthen the global financial safety net so that it provides adequate financing to all in need. At the upcoming Fourth International Conference on Financing for Development, Member States will have an opportunity to consider how to achieve this. Potential solutions could include measures to revamp the role of SDRs, for example by making SDR issuance more automated as a countercyclical measure or in response to shocks, or by basing allocations on need (or developing ex ante

agreements through which unused SDRs could be swiftly reallocated to countries in need, allowing for opt-out clauses), as well as efforts to make IMF lending more flexible, by placing fewer conditionalities and limits on access, eliminating surcharges, and basing borrowing limits on need rather than on quota multiples.

IV. A dearth of long-term development financing

24. Long-term financing, from both public and private sources, continues to be insufficient to meet rising financing needs. Faced with challenging financing conditions and limited options for long-term financing on financial markets, many developing countries have become increasingly reliant on official sources of financing.

25. Multilateral development banks are a key source of affordable, long-term finance for developing countries. They also play a countercyclical role in economic downturns and crises. They are an effective way to mobilize private savings for public investment and can also act as a bridge between public and private capital, including through mechanisms such as blended finance, when those mechanisms are well aligned with national priorities and focused on Sustainable Development Goal impact and when risk and returns are shared fairly between public and private actors.

26. In the Addis Ababa Action Agenda of the Third International Conference on Financing for Development, Member States recognized the role that multilateral development banks play in supporting the mobilization of financial resources in support of sustainable development, providing both concessional and non-concessional, stable, long-term development finance by leveraging contributions and capital and by mobilizing resources from capital markets. In the Addis Ababa Action Agenda, Member States called upon multilateral development banks to: (a) make optimal use of their resources and balance sheets in support of the 2030 Agenda for Sustainable Development and (b) establish a process to examine their role, scale and functioning to enable them to adapt and be fully responsive to the sustainable development agenda. Multilateral development banks have responded to these calls and have gradually stepped up their lending and alignment with the Goals and climate action. Recent crises have, however, made the need for reform even more urgent and prompted a new wave of related discussions.

27. Lending by multilateral development banks has increased significantly over the past two decades, from $30 billion in 2000 to $96 billion in 2022; concessional funding, however, has decreased. Multilateral development banks have accelerated their efforts to scale up and enhance their contributions in response to recent crises. In 2022, the Group of 20, as part of its independent review of the capital adequacy frameworks of the multilateral development banks, laid out proposals for multilateral development banks to optimize the use of their resources and balance sheets. In the Sustainable Development Goal stimulus, a call is made for a scaling up of long-term financing by $500 billion annually, primarily through multilateral development banks. The reports of the independent expert group on multilateral development bank reforms established by the Group of 20 have included many of the recommendations set out in the Sustainable Development Goal stimulus as well as a specific call for multilateral development banks to triple their annual lending to bring it to a total of almost $400 billion by 2030. In initiatives such as the Bridgetown Initiative and the Paris Pact for People and the Planet, attention has also been drawn to the potential of public development banks, in particular multilateral development banks, in expanding lending to meet the investment needs for sustainable development.

28. In response to these and other calls, multilateral development banks are implementing or considering reform measures aimed at increasing lending capacity,

improving lending terms to enhance debt sustainability and better aligning their operations with the Goals. Specific reform efforts aimed at enhancing financial capacity include capital management reforms, guarantee programmes and the issuance of hybrid capital. World Bank shareholders recently agreed to a reform package aimed at boosting lending capacity, including through the creation of a portfolio guarantee mechanism, a raising of the limits on bilateral guarantees, the launch of a hybrid capital instrument (including by channelling SDRs), and a lowering of the minimum loan-to-equity ratio for the International Bank for Reconstruction and Development. These reforms could yield a total of $300 billion–$400 billion of additional lending capacity over the next decade.

29. While significant in scale, these reforms still fall short of the ambitions laid out in the Sustainable Development Goal stimulus and by the independent expert group on multilateral development bank reforms of the Group of 20. They are also insufficient to meet financing needs and close financing gaps for the Goals and climate action. Therefore, additional action is urgently needed; proposals for such action are focused on several priority areas, notably the timely consideration of general capital increases, the implementation of recommendations from capital adequacy framework reviews and a rechannelling of SDRs.

30. New capital should be raised through ambitious replenishments of concessional windows and general and selective capital increases. Discussions on general capital increases should be initiated immediately, so that they can be completed before the end of 2026. An ambitious replenishment of the International Development Association should ensure that it has a financing capacity of at least $120 billion. There is also a need to fast-track the implementation of the remaining recommendations from the review of the capital adequacy frameworks of the multilateral development banks, including recommendations on appropriately valuing callable capital and adjusting leverage ratios.

31. Multilateral development banks can leverage rechannelled SDRs by borrowing against them on international capital markets, which is similar to an infusion of new capital, as discussed above. Building on the proposal by the African Development Bank and the Inter-American Development Bank, all major multilateral development banks should urgently consider setting up such mechanisms.

32. Looking beyond financing capacity and the goal of having bigger banks, efforts are also under way to ensure that increases in the quantity of resources of multilateral development banks are accompanied by strong policy and institutional frameworks that have sustainable development impact at their core, and such efforts need to be stepped up. To that end, multilateral development banks should strengthen their efforts aimed at measuring and reporting the Goal-related impact of their operations and investments at both the corporate and the project levels and aligning internal incentives accordingly.

33. There is also room to galvanize more cooperation among multilateral development banks so that they work as a system in service of development and climate impact, which would help to reduce risk on individual banks and enable a better targeting of resources on the basis of the institutions' respective comparative advantages. Greater use of co-financing and other risk-sharing mechanisms can reduce risks on the balance sheets of individual multilateral development banks and better leverage the balance sheet of the system as a whole. On the margins of the 2023 annual meeting of the International Monetary Fund and the World Bank Group, the heads of 10 multilateral development banks issued a joint statement agreeing to strengthen collaboration in five areas: scaling up financing capacity; boosting joint action on climate; enhancing country-level collaboration; strengthening co-financing; and catalysing private sector engagement. The World Bank has also announced the

launch of a co-financing platform for multilateral development banks, aimed at facilitating coordination across global and regional priorities.

34. Multilateral development banks should also step up their cooperation with other public development banks, including national development banks. Public development banks are an important tool for mobilizing financing and ensuring that expenditures and investments are aligned with sustainable development. The accumulated assets of public development banks totalled around $23 trillion in 2021. Led by the Finance in Common Summit, coordination between public development banks has grown enormously since the agreement on the Addis Ababa Action Agenda. Building on this progress, the entire system of public development banks, including multilateral development banks, could work together more closely. Given their local knowledge, national development banks could help to address bottlenecks in project pipelines, project generation and investment policy and planning, in collaboration with regional and multilateral development banks. Other options include measures to strengthen capacity-building and information-sharing and scale up co-financing, where feasible.

35. Blended finance has yet to deliver on expectations and must be rethought and refocused to prioritize sustainable development impact over project bankability. To that end, a process could be established within the United Nations for reviewing the development outcomes of blended finance to date and using the findings and lessons learned to develop a framework for scaling up blended finance with a focus on development impact rather than quantity or degree of leverage. At the Fourth International Conference on Financing for Development, these and other proposals geared towards addressing the dearth of long-term development financing could be explored.

V. Sovereign debt challenges

36. The recent tightening in global financing conditions has dramatically exacerbated the debt challenges faced by developing countries. Debt levels and vulnerabilities had been rising even before the pandemic, but now half of the least developed countries and other low-income countries are at high risk of or in debt distress owing to the multiple shocks that have occurred since 2020. Many more developing countries are facing debt service burdens that significantly impede their ability to invest in the Goals and climate action. The high costs of debt servicing and refinancing and the increasingly complex landscape of debt instruments and creditors have also made it more challenging to address debt crises speedily and effectively when they do arise.

37. Many developing countries, particularly the least developed countries and other low-income countries, benefited from strong economic growth and debt relief under the Heavily Indebted Poor Countries Initiative and Multilateral Debt Relief Initiative in the late 1990s and early 2000s, and their external debt-to-GDP ratios dropped significantly. In the past 10 to 15 years, many of those countries then embarked on ambitious, externally financed infrastructure drives. As a result, the stock of external public debt in nominal United States dollar terms has doubled since 2010 in the least developed countries and other low-income countries. In parallel, the share of sovereign debt held by commercial creditors rose rapidly. Consequently, countries were much more vulnerable to the change in global financing conditions in 2022, which has led to liquidity and refinancing challenges, rapidly rising debt service burdens and a growing number of defaults.

38. The median debt service burden for the least developed countries stood at 12 per cent of government revenue in 2023, the highest level since 2000. Debt service

burdens now consume over a fifth of tax revenue in 25 developing countries. Over the period 2020–2022, 46 countries spent more on debt interest than on public health, 12 more than in the period 2010–2012. A total of 15 countries had debt interest payments that exceeded public education expenditures, 3 more than in the period 2010–2012. In addition, 24 countries spent more on debt interest than on public investment in the period 2019–2021, 9 more than in the period 2010–2012.

39. Since 2022, net debt inflows to developing countries as a whole would have turned negative if not for debt financing by multilateral institutions. In 2024 and 2025, debt service burdens will remain elevated as a result of high refinancing costs combined with high external debt repayments, partly owing to the end of the Debt Service Suspension Initiative. In the least developed countries, for example, external debt service will hover around $40 billion annually between 2024 and 2025, up from $26 billion in 2021.

40. Borrowing is critical for financing investments in sustainable development, but too many countries encumbered by severe debt challenges lack the capacity to do so. Lack of borrowing capacity not only endangers their achievement of the Goals and clean energy transitions but also prevents them from investing and growing out of their debt overhangs.

41. In order to support solvent countries that are burdened by heavy debt service, systematic measures are necessary to facilitate investment in sustainable development. For countries with a significant share of official debt, such measures could include debt rescheduling by official creditors on net-present-value-neutral terms, for example through the Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative, with predefined terms and triggers to accelerate progress. There is also growing agreement on the need to help debtor countries engage with commercial creditors on voluntary rescheduling and to scale up financial support, for example through sweeteners[4] (along with seniority for voluntary exchanges), debt buy-backs or standardized debt-for-Sustainable Development Goal swaps, which can be structured and priced to help ensure comparability of treatment when relevant. To deliver such support swiftly and at scale, at the Fourth International Conference on Financing for Development, consideration could be given to establishing an institutional home for the provision of such support, which could, for example, be a scaled-up version of an existing facility, such as the World Bank Debt Reduction Facility. Such a facility could also provide countries with legal, capacity and financial support.

42. To achieve faster and deeper debt restructuring for insolvent countries, the international community must address the challenges of creditor coordination and power imbalances between debtor countries and creditors. The Common Framework for Debt Treatments needs to be strengthened by speeding up the process, clarifying steps and timelines, introducing debt service suspension during negotiations and expanding coordinated debt treatments for highly indebted countries that are currently ineligible under the framework. To enhance comparability of treatment of commercial creditors, the use of enforcement provisions, such as claw-back and most-favoured creditor clauses, should be further scaled up. At the same time, it should be noted that most-favoured creditor clauses put the onus of negotiating comparability of treatment on the debtor country, which may be ill-equipped to navigate complex restructurings involving several highly sophisticated creditors. The facility described in the preceding paragraph could also play a key role in this regard, providing legal and financial support to countries. In addition, IMF should continue to strengthen its

[4] Sweeteners are financial incentives that make bond exchanges more financially attractive for creditors.

policies on arrears and financing assurances to help to incentivize faster debt restructuring, building on recently adopted reforms of these policies.

43. Domestic legal approaches also have great potential to enhance debt crisis resolution, particularly if pursued in major financial jurisdictions. Discussions are currently under way on strengthening the enforceability of comparability of treatment provisions for commercial debt, and such reforms should be encouraged across jurisdictions to further enhance their impact. The Fourth International Conference on Financing for Development can also pave the way for further reform, such as an independent review of the sovereign debt architecture that contains recommendations, which could include consideration of a multilateral framework for sovereign debt workout.

44. While the debt crisis prevention agenda has been a focus of the international community, it is another area in which much work remains. In addition to progress across all action areas of the Addis Ababa Action Agenda, notably mobilization of domestic resources and international tax cooperation, increased grant and concessional financing and a supportive international economic environment, debt crisis prevention requires further efforts to enhance debt transparency, scale up capacity support for debt management and make the use of contingent debt instruments more systematic. The international community could also consider undertaking an effort to develop updated principles for responsible borrowing and lending that reflect the changing global debt landscape.

45. Discussions aimed at further improving debt sustainability assessment frameworks are also under way. IMF and the World Bank are in the process of reviewing their joint Debt Sustainability Framework for Low-Income Countries. An improved framework should account for both financing needs for the Goals and the impact of climate change from a longer-term perspective, as well as for impacts of investments towards the Goals and investments in resilience. Further consideration also needs to be given to the appropriate interest rate to use in such frameworks, which could help to better distinguish between liquidity and solvency issues.

VI. Achieving financial sector stability and sustainability

46. Financial sector regulation has been evolving in response to repeated instances of financial instability and the increasing complexity of the financial system. While the recent tightening of global financing conditions had raised fears of renewed bouts of instability and crises, banking systems and financial markets in major financial jurisdictions have largely avoided major crises and contagion, thanks in part to regulatory reform. While this situation has eased concerns about a systemic financial crisis, it may have contributed to the lack of urgency in addressing the severe impacts of reduced liquidity on conditions for access to finance in developing countries. At the same time, certain types of non-bank financial institutions are not subject to the same level of prudential requirements as banks. New digital financial instruments, including cryptoassets, present new risks.

47. International standards for banking regulation and supervision are set by the Basel Committee on Banking Supervision, based at the Bank for International Settlements. Post-2008 reforms to regulatory standards for banks, known as the Basel III reforms, were completed in 2018. In the period following the global financial crisis, the Addis Ababa Action Agenda, adopted in 2015, also included agreements to hasten reforms of financial market regulation, while underlining the need to enhance policy coherence and to take economic, social and environmental challenges into account.

48. While jurisdictions that are members of the Basel Committee on Banking Supervision continue to make progress in implementing the finalized Basel III reforms, risks are still present in the banking system. Work is still ongoing to close gaps in the operationalization of resolution plans for banks. Efforts to tackle the "too-big-to-fail" problem through increased regulation and supervision of the largest global systemically important banks have made progress, but domestic systemically important banks are not evenly covered, and information gaps persist. A string of bank failures and bank runs in March 2023, including the failure of one bank labelled as a global systemically important institution, resulted in the authorities in two developed jurisdictions using public money to underwrite the banking system. The earlier iteration of the Basel III reforms, which were implemented before the 2023 bank failures, are thought to have helped shield the global banking sector and the real economy from a wider spread of financial instability; at the same time, these crises underlined the importance of effective regulatory implementation and supervision.

49. Owing in part to the Basel III reforms, non-bank financial intermediation has taken on greater importance in financing the real economy. Non-bank financial intermediaries have grown to comprise almost half of global financial assets, despite a recent decline in their assets from $231 trillion in 2021 to $218 trillion at the end of 2022. This was the first notable decrease since 2009, and it is largely attributed to the impact of higher interest rates leading to valuation losses in mark to market asset portfolios, particularly in investment funds. These recent changes, however, are not expected to alter the long-term shift away from banks and towards non-bank financial intermediaries. Non-bank financial intermediaries pose new risks for financial stability, particularly with regard to illiquidity. Intermediaries such as money market funds and open-ended funds can experience instability in moments of market stress as a result of liquidity and currency mismatches, and this challenge has yet to be resolved.

50. Credit rating agencies support lending by improving market information, but inaccurate ratings can affect the cost of borrowing and the stability of the international financial system, as demonstrated during the 2008 global financial crisis. The crisis resulted in regulatory reforms to reduce the mechanistic reliance of financial regulation on ratings and address conflicts of interest, particularly in relation to structured finance and corporate ratings. Nevertheless, these reforms have not addressed the role played by rating agencies in the challenges faced by sovereigns in gaining access to long-term stable sovereign borrowing. Sovereign ratings are structured differently from corporate ratings in that analysts' judgments about political risks and "willingness to pay" play a much greater role. Perceptions of bias in such ratings, whether real or perceived, can impede market efficiency and affect countries' investment decisions, as some may forgo productive investments that would negatively affect a country's short-term fiscal position but improve medium-term growth prospects. Fear of ratings downgrades has also hindered some countries' participation in official debt relief programmes, in particular the Group of 20 Debt Service Suspension Initiative during the COVID-19 crisis in 2020–2021. To address these concerns, enhancements in the credit rating architecture are needed, particularly with a view to providing long-term oriented investors with long-term and model-based ratings that complement existing ratings and that incorporate long-term (climate and other) risks and positive impacts of investment.

Fintech and financial stability

51. One major new trend that is having an impact on financial intermediation is the rapid growth of new technologies used in the provision of financial services, or fintech. Fintech has greatly contributed to enhancing access to finance and was a major driver of the significant progress towards financial inclusion that has been

achieved since 2015. Fintech has the potential to contribute to financial stability by strengthening decentralization and diversification, deepening financial markets and improving efficiency and transparency in the delivery of financial services. If not well regulated, however, fintech could also incentivize riskier activities and exacerbate the cyclicality of financial markets.

52. Fintech has helped to expand access to financial services in developing countries.[5] Overall, account ownership grew by 30 percentage points between 2011 and 2021 in developing countries, reaching 71 per cent in 2021. Technological innovations have been a major driver of this trend; mobile money in particular has facilitated a vast expansion of low-cost and small-scale transactions.

53. Preliminary evidence also suggests that the use of fintech platforms for capital raising in advanced economies has played a role in improving financial stability, though this has not been the case in developing countries. Established financial institutions in countries with high regulatory quality and government effectiveness have benefited from increased competition from fintech firms. Well-designed regulations can establish a level playing field – one in which new fintech firms can succeed and incumbent financial institutions are protected from unfair competitive behaviours. At the same time, the reduced profit margins resulting from increased competition from fintech could create difficulties for established banks in building the capital buffer necessary to absorb losses and maintain solvency. If regulations are inadequate, reduced profit might incentivize banks to engage in riskier lending and investment activities, which would have implications for market stability.

54. Lending activities facilitated by fintech platforms may also involve greater financial risk due to market concentration and overreliance on data-driven algorithms in risk evaluations and credit-related decisions, which could lead to herd behaviour. Moreover, fintech can amplify market volatility because it significantly increases the speed and ease of moving money in response to financial market performance. Since artificial intelligence is used to automate risk assessments and credit approvals, which tend to fluctuate with economic cycles, it can expedite and reinforce the cyclical nature of financial conditions.

55. To mitigate the risks posed by fintech firms to market stability, it is essential to continuously evaluate and update the licensing framework for financial service providers, taking into consideration emerging entities with innovative business models. Moreover, capital, liquidity and operational risk management requirements need to be strengthened, so that the diverse risks associated with various fintech business models are adequately represented. Authorities should apply effective regulation, supervision and oversight in line with the principle of "same activity, same risk, same rules".

Incorporating sustainability into regulatory frameworks

56. In response to growing interest in sustainable investing from clients and increasing political momentum to align policy frameworks with sustainable development, sustainable finance has been increasingly embedded in regulatory and legislative frameworks. Countries are strengthening the role of the financial sector in advancing sustainable development. Several databases have emerged to record the progress made. As of July 2023, over 780 sustainable finance policy measures in 109 countries had been registered with the Green Finance Measures Database, a 70 per cent increase since 2015. Nonetheless, progress continues to be unevenly distributed, and scope for improvement remains significant.

[5] Serhan Cevik, "Promise (un)kept? Fintech and financial inclusion", IMF Working Paper, No. WP/24/131 (June 2024).

57. Taxonomies and disclosure legislation have been at the heart of legislative efforts; there are at least 30 taxonomies and 200 frameworks, standards and guidelines on sustainability and climate disclosures in place across 40 countries. By setting out clear and transparent criteria for sustainable economic activities, regulatory frameworks on sustainable finance can enable the development of a reliable and credible market for allocating capital to the sustainability transition.

58. The growing regionalization of sustainable finance legislation reveals disparities and fragmentation across jurisdictions, highlighting the need for global interoperability. Sustainable finance legislation is being tailored to regional priorities, as seen by the different taxonomies adopted in Europe, Latin America and the Asia-Pacific region, each reflecting the unique local contexts.

59. Regionalization is legitimate and important, but without effective coordination it risks causing fragmentation and high compliance burdens for investors, which would reverse the progress made on the consolidation of standards and could make investors underestimate the sustainability credentials of funds. At minimum, there is a need for global collaboration towards interoperability while simultaneously exploring the possibility of developing a global foundational framework that would leave room for regional adaptation. For example, all industry activities could be linked to the Goals in a global taxonomy, which would help regions to coordinate their own visions across regional taxonomies, building on ongoing efforts on harmonization and interoperability of regulations across jurisdictions.

60. As progress is uneven across regions, several challenges must be addressed to promote universal coverage. At present, most sustainable finance legislation is being adopted in developed economies. The successful implementation of sustainable finance legislation requires bolstering institutional capacities, legal frameworks and capital markets through enhanced capacity-building support and technical guidance. The Global Sustainable Finance Observatory informs capacity-building efforts on sustainability disclosure, taxonomies, carbon pricing, and sector- and product-specific measures. Stock exchanges can also play an important role in helping markets to navigate new environmental, social and governance requirements.

61. The number of stock exchanges that have guidance on environmental, social and governance disclosures; mandatory environmental, social and governance reporting; environmental, social and governance training; and related bond and equity offerings has increased in the past few years. Support from development cooperation providers is needed to build capacity in developing countries to gain access to sustainable finance, including through the use of innovative instruments, such as insurance and investment based on results, which mitigate risk and attract external resources aligned with the Goals without increasing debt distress. Strengthening the climate information architecture and aligning the practices and products of financial and information intermediaries can support the scaling up of blended finance for climate mitigation and adaptation in developing countries.

62. Legislative efforts should incentivize impact across asset classes in line with the 2030 Agenda and global climate goals, while being carefully crafted to avoid distortions. Only 14 per cent of impact investors have perceived progress in government support over the past decade. A global taxonomy in which global industry activities are linked to the Goals could be the first step towards improving identification of investments aligned with the Goals, but that taxonomy should be supported by policies containing financial incentives for such investments. Such policies include measures aimed at developing the supply of capital, such as through risk-sharing mechanisms, adjusted market costs, improved transaction efficiency or guarantees, as well as measures aimed at developing pipelines and the capacity of capital recipients.

63. To address current funding gaps, specific focus could be placed on channelling impact funds towards underfunded sectors, particularly those requiring private investment to complement public funds. New disclosure legislation should be aimed at facilitating the measurement of private sector impact and progress towards climate goals by adopting an impact or double materiality perspective. Countries accounting for nearly half of global GDP are adopting disclosure legislation, and many have already pledged to transpose International Sustainability Standards Board standards in their regulatory frameworks. Jurisdictions that are already contemplating the adoption of International Sustainability Standards Board standards can leverage current progress while integrating additional provisions for a double materiality vision.

64. Instead of imposing additional burdens on investors, a double materiality approach would align with the objective of preventing fragmentation across jurisdictions and reducing investor confusion. The double materiality approach also mitigates medium- to long-term transition risks for policymakers and investors. It will seamlessly align with transition-aligned legislation, which will progressively demand greater accountability from companies for their externalities and contributions to global climate goals.

65. Beyond policies focused on improving or widening the field, sustainable finance must be integrated into broader efforts to achieve sustainable transformations. In regulatory frameworks, consideration needs to be given to the roles of actors across the financial system, including pension funds, insurers and banks, so that financial flows can be aligned with sustainability objectives. Sustainable finance policy must be seen as part of a whole-of-government approach and a wider set of economic and financial policies that together create enabling conditions for sustainable transformations.

66. Sustainable finance policy reform has already moved from a siloed approach led by environmental ministries to a key consideration for financial policymakers. This move includes consideration of the interplay between sustainability and financial stability, for instance through climate transition plans. It also includes broader fiscal and regulatory policies to create sustainability-aligned incentives for real economy actors, as well as financial sector and macroeconomic policies that are supportive of sustainable transformations.

67. The Fourth International Conference on Financing for Development offers an ideal platform to advance action on and continue collaborating towards: (a) the interoperability of sustainable finance legislation across regions to prevent uneven progress and heavy compliance burdens, while accounting for regional and local specificities; (b) the adoption of mandatory national disclosure standards with a double materiality vision; (c) the development of frameworks and carefully crafted incentives for impact investing at scale, so as to align capital markets with real world impact; and (d) the development of a broader set of macroeconomic policies that create enabling conditions for sustainable transformations.

VII. Global economic governance and policy coherence

68. The international community's response to the series of recent crises and their fallout in the international financial system has been judged by many as inadequate. As a result, there has been a renewed focus on the governance and decision-making arrangements that guide international financial institutions in the execution of their mandates and on the lack of voice and representation of developing countries in these structures.

69. Member States have repeatedly committed to broadening and strengthening the voice and participation of developing countries in international economic decision-making, norm-setting and global economic governance, not least in the financing for development outcomes (most recently, the Addis Ababa Action Agenda). While countries in developing regions represent over 74 per cent of the membership of the General Assembly, which utilizes a one-member-one-vote system, their voting share in other international organizations remains far below that level. Developing country membership in other United Nations bodies fluctuates from year to year.

70. There has been no significant change in developing countries' voting rights in recent years at any international economic institution. Reforms agreed by the Board of Governors of the World Bank in October 2018 have been phased in over time as countries subscribe to their new capital shares, but developing countries continue to hold only 39 per cent of voting rights at the main lending arm of the World Bank, which is only a marginal increase compared with their share in 2000. At the International Finance Corporation, the private sector lending arm of the World Bank, developing countries have just over 32 per cent of the voting rights.

71. Two general reviews of quotas were completed at IMF in 2019 and 2023, without any change to the distribution of quotas, which help determine voting rights. Developing countries retain 37 per cent of the voting rights at IMF. An agreement was expected to be reached on a new quota formula in 2014 but is now not expected until 2025. At international organizations, the voting rights of countries in developing regions have remained steady, with large disparities across organizations.

72. The Addis Ababa Action Agenda also contained a commitment to the open, transparent, gender-balanced and merit-based selection of the heads of international financial institutions and to the enhanced diversity of staff. While two women have now served as head of IMF, the Managing Director of IMF has always hailed from Europe, and the President of the World Bank Group has always been a citizen of the same country.

73. In a complex geopolitical landscape with increasing risks of fragmentation, system-wide coordination and policy coherence remain a challenge. All the financing for development outcomes have contained references to the importance of enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development. In the Addis Ababa Action Agenda, this understanding was expanded to include "all three dimensions of sustainable development".

74. The financing for development follow-up process has enhanced coordination among international institutions, including in the joint work undertaken by the Inter-agency Task Force on Financing for Development and participation in the annual forum on financing for development follow-up. However, other geopolitical pressures, including war and conflict, have complicated the work of international and intergovernmental bodies.

75. There are significant risks of the world fracturing into multiple rival geopolitical blocs with lower levels of trust and cooperation. This may have direct costs in reduced growth and trade, as well as indirect costs in reduced trust in multilateralism, weaker social contracts and an inability to address global challenges such as climate change. The Fourth International Conference on Financing for Development will provide a venue for directly addressing those risks and continuing to build policy coherence aimed at delivering on the 2030 Agenda.

Women's leadership in the economy

76. Despite advances in enhancing the leadership of women in the economy in recent years, progress continues to be uneven. In 2023, women held 25.8 per cent of board seats at large- and mid-cap companies included in a global index covering most of global investible equity. While that figure represented an increase in the representation of women on corporate boards compared with 2022, there were regional disparities: the participation of women on boards was significantly higher in developed markets (32.9 per cent) than in developing countries covered by the index (17.1 per cent).

77. Despite the upward trend overall, the growth rate of women directors has slowed, with a 1.3 per cent increase in 2023 versus 1.9 per cent in 2022. Notably, 41.2 per cent of the large- and mid-cap companies included in the index had achieved the goal for representation of women on boards within the financial industry (30 per cent) by October 2023, which reflects the progress made in advocating more equitable representation of women on boards. Nevertheless, challenges remain, particularly in emerging markets, where only 14.5 per cent of companies reach this benchmark and issues of high turnover among women directors highlight the need for better retention strategies.

78. A notable gender disparity also persists in established business ownership, defined as managing a business for over 42 months. Approximately 1 out of every 3 established business owners is a woman. Worldwide, women are more likely to be solopreneurs, i.e. persons who run a business without a partner or team: there are 1.47 women solopreneurs for every man. In terms of start-up activity, the ratio is 0.80 women for every man. Further efforts are needed to ensure the equitable representation of women in positions of leadership and the broader economy.

VIII. Conclusions

79. **Faced with cascading shocks and extremely challenging financing conditions, many developing countries are left with no choice but to reduce investments in the Goals and climate action at a critical moment for achievement of those agendas. The pace and scale of reforms in the international financial system and the architecture that governs it must be accelerated.**

80. **Achieving the Goals and the large-scale transitions needed to avoid catastrophic climate change will require investments at an unprecedented scale. Such an investment push will only be possible within a financial system that is fit for purpose; urgent reforms are needed to address the challenges of deteriorating public finances, fiscal constraints, debt, monetary and financial stability risks and the dearth of productive and sustainable investment.**

81. **Ambitious policy actions aimed at addressing the challenges of the international financial system are needed to achieve the objective of delivering $500 billion annually in additional long-term financing. The Summit of the Future, to be held in September 2024, and the Fourth International Conference on Financing for Development, to be held in June 2025, which is mandated to support the reform of the international financial infrastructure, are important venues for discussions on such reform.**

82. **In order to respond to challenges and rising risks in the global economy, the global financial safety net must be strengthened further and made more equitable in terms of access. Priority actions include rechannelling additional unused SDRs; introducing greater automaticity in triggering decisions on future SDR issuances and allocations based on need; and more flexible IMF lending.**

83. **Multilateral development banks play a central role in providing affordable, long-term finance and serve as a bridge between public and private capital. To scale up multilateral development bank finance, bolder and more urgent action is needed. Priority actions should include early consideration of replenishments and capital increases, measures to raise new capital by issuing hybrid capital instruments at scale and a rechannelling of unused SDRs through multilateral development banks. The focus of the Fourth International Conference on Financing for Development on architecture reform means that it will be an opportunity to strengthen the entire system of public development banks and to make better use of their complementary strengths to scale up the provision of financing aligned with country needs.**

84. **Against a backdrop of significant debt sustainability challenges in a growing number of developing countries across the globe, urgent action is needed across three priorities: (a) strengthening debt crisis prevention, including through debt management and transparency; (b) finding solutions that enable countries with severe fiscal constraints and debt overhangs to invest in the Goals; and (c) developing a more effective debt crisis resolution mechanism. The Fourth International Conference on Financing for Development provides an opportunity to agree on actions to bring down high borrowing costs and debt service burdens and address gaps in the debt restructuring architecture.**

85. **Implementation of the national financial regulations and international standards updated in the wake of the financial crisis of 2008 continues to be uneven, and certain risks remain outside the perimeter or scope of regulation. At the same time, climate-related risks are not being sufficiently addressed in financial regulatory norms, as quantification of such risks remains a challenge for regulators, supervisors and financial institutions alike. The Fourth International Conference on Financing for Development could serve as a platform for bringing together relevant stakeholders, including regulators, governments, international organizations, financial institutions, other private sector actors and civil society, to identify additional steps needed in the regulatory agenda to create financial markets that are accessible, stable and sustainable.**

86. **Despite repeated commitments to increasing the voice and representation of developing countries in global economic governance and some progress being made in this area, the pace and scale of reform has not been sufficient. The Fourth International Conference on Financing for Development, held in a context of widespread recognition of the need to strengthen the legitimacy of global governance arrangements, presents an opportunity to accelerate reform efforts.**