

INTERNATIONAL FINANCE FACILITY
CAFOD RESPONSE
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Introduction

Now, nearly five years after the Millennium Declaration, and 10 years away from the 2015 target date for the achievement of the Millennium Development Goals (MDGs), it is widely acknowledged that many countries will fail to reach them. Donor countries have not made, and are not making, sufficient resources available to make the MDGs attainable. The International Finance Facility (IFF), advocated by the Chancellor of the Exchequer, Gordon Brown, and supported by a wide international coalition, is an imaginative response to this situation.

Raising the money

The IFF is a scheme to raise funds for development by selling on international capital markets bonds secured against long-term commitments by donor governments. The IFF is not a development agency which would actually spend the money it raises. This, the money raised, would be passed by the IFF to development agencies and institutions, such as the World Bank, specialised UN agencies and development ministries, including DFID. The IFF “front loads” aid spending in the years leading up to 2015 by borrowing from future aid budgets.

High level conditions

IFF bonds, unlike Treasury bonds, would not count as government borrowing because there would be an element of risk attached to them in the form of one or more “high level conditions”. Currently the high level condition most commonly mentioned in connection with the IFF is a country falling into prolonged arrears with the IMF. If this condition were breached donor governments would not have to pay back bondholders for that proportion of IFF funds that were allocated to the country that was in arrears. The only countries currently in arrears with the IMF are Iraq, Liberia, Somalia, Sudan and Zimbabwe. This shows that countries fall into arrears as a consequence of the failure of politics rather than simple economic mismanagement and that donors are therefore unlikely to be able to affect the likelihood of default. It should be noted in passing that the high level condition also exists to protect taxpayers who are ultimately responsible for ensuring that bonds are redeemed. The credibility of arguments for greater development assistance rests not only on the need for aid, which is undisputed, but on evidence that it is well used and effectively contributes to development and poverty eradication.

Will the IFF count towards 0.7%?

This has yet to be clarified by the Development Assistance Committee of the OECD which determines what is and what is not “development assistance”. It is clear, however, that disbursements by the IFF in the years running up to 2015 and repayments to IFF by donor governments, largely after 2015, should not be double counted and that both sets of flows should be shown transparently so that if the original sums that are raised are counted as development assistance then their repayment will not also count as development assistance.

Spreading the risk

If the IFF were backed by all the G7 governments¹ it could raise an additional \$50 billion a year for development. This is the sum called for by the UN Conference on Financing for Development held in Monterrey, Mexico in March 2002, which agreed that development assistance had to be doubled from \$50 billion to \$100 billion a year if the MDGs were to be achieved in most countries of the world. The IFF needs a number of backers if it is to spread risk among donors and if bond-holders are to feel confident that there is sufficiently robust backing for their investment. For this reason in order to get off

¹ Canada; France; Germany; Italy; Japan; United Kingdom; United States. The G8 includes Russia which, for the time being at least, is not a major aid donor and is outside the development assistance reporting system of the OECD. The meeting in Gleneagles on 6-8 July will be a G8 meeting but only the G7 governments will take part in the great aid debate.

the ground the IFF needs a minimum of three or four major donors to participate. At present the UK is the only country absolutely certain to participate. Both France and Italy have voiced support but this has yet to be translated into solid commitment to the scheme. An IFF backed by these three participants would raise much less than half the \$50 billion that is still set by the UK as its target.² At the G7 finance ministers' meeting on 3rd February the German finance minister, Hans Eichel, expressed guarded support for the IFF, saying that it should be run as a pilot scheme, possibly backed by a tax on aircraft fuel.

The case for the IFF

As the table below shows, there would be no need for the IFF if the world's major donors were today achieving the UN target of dedicating 0.7% of national income (GNI) to development assistance. The IFF, in fact, is a frank recognition that, owing to lack of political will on the part of most donor governments, aid budgets are not going to provide resources on the scale needed to achieve the MDGs ahead of 2015. One of the compelling arguments in favour of the IFF is political in nature: it is the only proposal on the current G7 agenda, with some support from currently three G7 governments.

Country	2003 Development Assistance (US \$ mill.)	Per cent of GNI	0.7% in 2003	Target date for achieving 0.7%
Canada	2,209	0.26	5,947	None set
France	7,337	0.41	12,526	2012
Germany	6,694	0.28	16,734	None set
Italy	2,393	0.16	10,469	None set
Japan	8,911	0.20	31,188	None set
UK	6,166	0.34	12,694	2013
US	15,791	0.14	78,954	None set
TOTAL	49,501		168,512	

There are other sources of development finance but, in the face of the immediacy and scale of the needs that they are supposed to address, they all present significant difficulties. Further debt reduction will not yield resources on the scale required by Monterrey and would in any case have to come largely from donors' budgets; aid budgets will not increase fast enough; the currency transaction tax, though acquiring some momentum, still has technical difficulties to overcome and is some time away from becoming a reality.

The UK also argues that the IFF could provide a steady flow of predictable resources that would allow developing country governments to plan the major, long-term investments in health, education and infrastructure that could put them on course to achieve the MDGs. Aid, in contrast, is subject to changes in donor governments, shifting donor preferences and budgetary constraints, and cannot be relied upon to support long-term expenditure and investment plans. The UK has put forward the principles that should guide the IFF's disbursements, namely, that resources raised by the IFF should be: invested in poverty reduction; not tied to contracts using suppliers from the donor country; provided in predictable multi-year programmes lasting at least three years; disbursed in grant form; disbursed to a wide range of recipients; targeted at low income countries.

The IFF proposal, therefore, acknowledges that:

- Current trends indicate that most of the international development commitments made by donor governments, in particular the MDGs, are not attainable within the time frames agreed.
- Current levels of aid, debt reduction, private investment and trade reforms (which are still a promise rather than a reality) will not provide sufficient resources to allow most developing countries to achieve the MDGs.
- Wealth redistribution at the global level requires effective and predictable financial flows from wealthy economies, primarily to the poorest countries.

² An IFF with UK, France and Italy would be about 30% of an IFF in which all potential donors participated. The US alone would account for about 30% and Germany 10%.

- If all donor governments were today achieving the UN 0.7% target, there would be no need for the IFF. The IFF is, in fact, an acknowledgement that, with a few honourable exceptions, most countries lack the political will to achieve the 0.7% target in the near or medium term.
- Promises are not enough. We need concrete and immediately feasible solutions that will enable Northern countries to fulfil their commitments.

The IFF is only part of the answer

Although the IFF offers the possibility of massive additional finance for development in the years leading up to 2015, it is not, and has not been presented as, a solution to world poverty. The IFF does not and should not replace other more radical, longer term and more far reaching proposals. In particular CAFOD believes that donor governments must make progress towards the following goals:

- Further debt cancellation, 100% debt cancellation in most cases – with debt sustainability assessed according to human development criteria, not merely debt-to-export ratios and other economic criteria;
- The establishment of a Fair and Transparent Arbitration Procedure to deal with unbearable debt burdens on the basis of shared responsibility and the rule of law;
- Fairer trade rules, in particular ending all forms of dumping, and allowing developing countries to support and protect crops essential for food security and sustainable rural development;
- At least 0.7% of GNI dedicated to development aid and improved aid quality;
- Implementation of global taxes to finance global public goods, such as the currency transactions tax or a tax on air travel.
- The abolition of tax havens and improved global tax coordination;
- A more democratic and equitable system of global governance, since power imbalances at the global level – apparent in the governing bodies of the IMF and World Bank and in the Security Council of the UN – are a major obstacle to development and global equity.

An approach that comprehensively and coherently addresses trade policies as well as finance, ultimately aiming at a fairer distribution of wealth, is necessary. Such an approach would acknowledge the following points:

1. Aid is necessary but is not enough. Any real progress towards global social and economic justice requires much more coherence, especially between Northern governments' finance and trade policies and development goals. The IFF addresses only the current shortfall in development assistance and the failure of most donors to achieve the UN 0.7% target.
2. Respect for recipient countries' policy space. As an NGO working with Southern partners, CAFOD is only too well aware of the harmful impact of some conditions (structural adjustment) attached by the World Bank and the IMF to loan rescheduling negotiations and to new loans. These conditions have undermined the ability of governments to create consensus and build ownership around national poverty reduction plans. The development agencies and institutions channelling IFF funds should work in partnership with developing country governments respecting the principle set out in 2002 by the G7 at Kananaskis in Canada: "No country genuinely committed to poverty reduction, good governance and economic reform will be denied the chance to achieve the Millennium Development Goals through lack of finance."
3. Donor coordination. Although the IFF will use only existing disbursement mechanisms and so will not create any new conditionality, the scale of the resources that the IFF could generate is likely to create difficulties and constraints for developing countries that already struggle to satisfy the multiple conditions and reporting requirements of donors. The IFF, in fact, is itself an argument for greater coordination among donors. One of the most attractive features of the IFF – of creating an aid-pool and a framework for multilateral negotiations on conditions – would be undermined if contributing donors could impose their own conditions on the money they contribute. At present, however, advocacy for the IFF focuses on the need for additional development finance. The UK

argues that the IFF's conditionality and governance can only be finalised by agreement among all its participant governments – and this is still not possible since the campaign to recruit donor governments to the IFF is still in full swing.³

4. Development will be a priority long after 2015. The MDGs and 2015 are only a first step towards the achievement of global economic justice and human dignity of all. Donor governments participating in the IFF will be repaying bondholders after 2015. At present it is foreseen that these payments will be deducted from future aid budgets. If donor governments do not increase aid between now and 2015, then the repayments to the IFF could significantly reduce existing aid flows after that date. The extent of the reduction of aid will depend on economic growth rates in industrialised economies and the commitment of donor governments at least to maintain aid budgets as a proportion of GNI. There is no way, apart from serious public political commitment, of ensuring that governments reach their 0.7% obligations – and this is not proof against contingencies and emergencies that may arise before 2015. This is a risk for development since extreme poverty and its attendant ills are likely to be the biggest challenge facing the world after 2015 – as they are now. After all, the first goal of the MDGs is to lift only half the extreme poor above the one-dollar-a-day level. Those who remain below this line will be the chronically poor who, by definition, will find it harder to rise above this very low level of poverty.

If the IFF is to be a durable part of global redistribution efforts, it should be accompanied by measurable targets and agreed timetables for all donors to reach and maintain the UN 0.7% target. The IFF's proponents, however, also argue that, if implemented, the IFF will by 2015 establish internationally a level of development assistance that will be hard to retreat from and will have generated real success stories that will increase public support for aid. This may be a reasonable prediction but, in the absence of firm commitments to increase aid, it is equally reasonable to ask where the resources that donor governments will need in order to repay to the IFF after 2015 will come from.

Conclusion

The IFF is a central element of the UK's G8 in 2005 strategy. G7 governments will have to make up their minds about the IFF before July. Civil society is also being asked to make up its mind and to decide whether the promise of massively increased predictable resources offered by the IFF outweighs doubts about conditionality, governance and the lack of guarantees regarding aid budgets after 2015.

CAFOD believes that the availability of resources is the first necessary step towards achieving the MDGs and for this reason the IFF should be supported. This support should not be uncritical. The UK Government, as the initiator of the proposal, should ensure that civil society has a role to play in the governance of the IFF and that its decision-making should be totally transparent.

CAFOD also believes that, if the IFF becomes a reality, it should not replace other measures on aid, trade and debt. Nevertheless, if implemented in full, the IFF could make a significant contribution to the achievement of the MDGs, the eradication of poverty and the building of a more just international economic system.

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³ For a joint DFID/Treasury view on conditionality see the consultation paper *Partnerships for poverty reduction: changing aid 'conditionality'*, available at <http://www.dfid.gov.uk/pubs/files/conditionalitychange.pdf> (Sept. 2004)