Accelerating Progress of Low-Income Countries Towards the SDGs: Balancing Realism and Ambition in a Post-COVID-19 World

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Abstract

The world is in the throes of a health, economic, and social crisis due to the COVID-19 pandemic. Slower global growth has significantly worsened the economic prospects for all countries, including the poorest ones. Low-income countries (LICs) are also finding it more difficult to service their external debt as well as to access private capital—concessional and non-concessional. Aid flows, which had stalled even before the crisis, are showing little sign of recovering as donor countries confront their own economic reckoning. Policymakers in LICs see difficulties in initiating and sustaining ambitious policy reforms, which had already been flagging in the relatively good times that preceded the crisis. This less-than-propitious context makes it critical that all development partners balance realism and ambition in looking for ways to sustain the progress of LICs towards the Sustainable Development Goals in the decade that lies ahead. Achieving such a balance will require a mix of short- and longer-term actions, and a spirit of global partnership that is much deeper and wider than has been in evidence recently.

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Introduction

The world is now a third of the way towards the deadline for attainment of the Sustainable Development Goals (SDGs). Announced in 2015 as the successors to the Millennium Development Goals (MDGs), these goals represent the most ambitious global attempt at spurring broad-based development. The 17 goals represent an expansive view of development, covering a range of areas from income poverty and hunger to human development and environmental sustainability. With 169 targets and 230 indicators, the SDGs also embody a commitment to tracking and measuring development outcomes.

Before the COVID-19 pandemic upended the global economy earlier this year, the dominant narrative about progress towards the achievement of the SDGs particularly in the poorest countries of the world was that lack of adequate financing was the main barrier to their achievement. This narrative is founded on translating the goals mechanically into estimates of fiscal "needs." With these needs-based assessments as the backdrop, the focus is then on how low income countries in particular would mobilize the necessary financing, whether for their needed infrastructure investments or for the delivery of health and education services.[1]

In this context, this paper has three aims. First, it takes stock of the key determinants of the progress of low income countries (LICs) towards the SDGs before the COVID-19 pandemic hit.[2] In doing so, it highlights the need to look systematically at *both* the availability of financing to help these countries move towards the goals *and* the adequacy of the countries' policy and institutional frameworks so that all available financing is well utilized. The difficulties that LICs were facing in mobilizing financing on the required scale even before the pandemic are noted. In addition, it is highlighted that the (average) quality of recipient countries' policies and institutions, which matter for how financing is used and therefore for the achievement of the SDGs, had stagnated or deteriorated even before the pandemic began. Second, the paper delineates the ways in which the pandemic has made it much more difficult for LICs to achieve the SDGs. In doing so, it looks at the adverse impact of the pandemic both on sources of financing available to LICs as well as on the economic performance and reform prospects of LICs. Finally, the paper identifies the most promising options available to LICs and their development partners to accelerate progress towards attainment of the SDGs once the global economy begins its recovery from the effects of the COVID-19 pandemic. In doing so, it stresses the need for coordinated actions on the parts of all actors, which strike a balance between short- and long-term priorities. It also underscores the need for the countries and the global community to take a broader view of prospects for the SDGs beyond the availability of financing.

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[1] This approach is used, for example, in Sachs et. al. (2019).

[2] In keeping with other work, the characterization of LICs in this paper is quite broad since different institutions, including the UN, the World Bank, the IMF and the OECD DAC, vary in the coverage of this group. For this reason, the paper specifies which characterization is being used at various points.

Determinants of the Prospects for Achieving the SDGs: The Situation pre-COVID

In looking at the prospects for countries to reach the SDGs, the predominant focus has been on the need for adequate concessional financing, particularly for LICs. Before turning to what the prospects for such financing flows were before the COVID-19 pandemic hit, the role of financing in helping countries reach the SDGs is discussed.

Progress towards the SDGs Depends Both on Financing and on Good Policies and Robust Institutions

There is no doubt that countries, especially poor ones, will require to spend substantially larger sums of money if they are to make rapid progress towards the SDGs. The goals are ambitious relative to where countries are today, and so will require significantly larger *public* outlays. This recognition, in turn, has spawned an industry of estimates of the financing needs for attainment of the SDGs, much of which builds from sectoral assessments. For instance, the incremental *annual* costs in 2030 of reaching the SDGs in five sectors—education, health, roads, electricity, and water and sanitation—have recently been estimated at US$ 0.5 trillion (or about 15 percentage points of GDP) for 49 low income and developing countries.[3]

However, even before the advent of the SDGs, when it was the MDGs that were the topic of discussion, it was recognized that additional financing *alone* was not going to secure progress towards those ambitious development goals. Rather what was needed was a combination of additional financing and policy and institutional reforms at the country level to ensure these resources are well deployed and used so as to yield better development outcomes. As one analysis in the early 2000s concluded, "To accelerate progress in human development, economic growth is of course necessary. But it is not enough. Scaling up will require both a substantial increase in external resources and more effective use of all resources, internal and external. As resources become more productive, the argument for additional resources is more persuasive. And external resources can provide strong support for changes in practice and policy to bring more effective use. In this sense the two are complementary."[4]

[3] Gaspar et al. (2019).

[4] World Bank (2003).

This view that progress towards development goals requires a mix of adequate financing and policy effort by countries to use that financing well does not, however, permeate the more recent literature on the SDGs, which has tended to focus predominantly on the need for additional financing.[5] Hence discussions of the progress of developing countries, especially LICs, towards the SDGs are dominated by considerations of how much financing is available and how the (large) additional financing flows are to be generated. Yet, it is critical that attention also be paid to the policy and institutional frameworks of recipient countries so that aspects such as the quality and composition of their public spending programs, and of the efficacy of their growth strategies also receive the attention they deserve, given their influence on the pace of development progress.

Headwinds to Progress towards the SDGs Pre-COVID

Even before COVID-19 hit, a number of factors were already slowing the progress of countries, especially LICs, towards the SDGs. The major sources of external financing for the SDGs—official development assistance (ODA), private capital flows and blended finance, and increased borrowing—were stagnant. Efforts to increase domestic resource mobilization appeared to have stalled. And despite progress in pursuing reforms in the early-2000s, the quality of low income countries' policy and institutional environments had stagnated or deteriorated, especially following the Global Financial Crisis (GFC), raising questions about the efficacy of additional financing flows alone in promoting better development outcomes.

Stagnating aid flows

ODA flows to LICs in 2019 were about US$27 billion. This level was almost unchanged in real terms from 2018, which in turn was about 6 percent lower than in 2017.[6] Taking a longer-term view, net ODA (which includes flows to developing countries at all income levels) has doubled in real terms since 2000. However, much of that increase occurred between 2000 and 2010, following on commitments made by donors at the Monterrey Conference on Financing for Development in 2002 and at Gleneagles in 2005. ODA peaked in 2016 before falling in 2017 and 2018. ODA is now about 0.30 percent of the GNI of DAC members, a far cry from the optimism of the early 2000s that it would soon reach the 0.7 percent of GNI target.

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[5] This is not to imply that these analyses ignore the need for policy and institutional reforms in low-income countries to underpin progress towards the SDGs. Rather, the issue is one of emphasis. These analyses tend to focus on deriving and refining estimates of the additional spending needs and on their financing rather than on how such flows might interact with better policies to result in better development outcomes.

[6] http://www.oecd.org/dac/financing-sustainable-development/development-finance-data/ODA-2019-detailed-summary.pdf. This definition of LICs follows the World Bank's income classification categories as laid out in https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups

Negligible private capital flows

The trends of recent flows of private development finance are even bleaker. Far from confirming a transition that would help fulfil the "billions to trillions" vision articulated in 2015, the share of flows of private development finance to LICs has actually been falling. Development finance institutions (DFIs)—bilateral and multilateral—which it was hoped would be the major vehicle in promoting such flows, still operate mostly in middle-income countries. In 2017–18, the 28 DFIs that report to the OECD DAC mobilized US$ 48.4 billion in private finance, but only five percent of this amount flowed to least developed countries (LDCs—as defined by the UN) and other LICs, compared to almost 10 percent in 2012–15. Of blended finance commitments by DFIs in 2018, which totaled US$ 3.5 billion in 2018, only about 11 percent went to LICs. And LICs account for only about a fifth of DFI concessional commitments—about the same as upper middle-income countries and a third the share flowing to lower middle income countries. There are also relatively few transactions with private participation in infrastructure in LICs. And foreign direct investment in most of these countries has been falling while private portfolio flows have been negligible.[7]

Growing debt distress

A debt crisis was already on the horizon for many low-income countries even before the dislocation caused by the pandemic. At end-2019, half of all low-income economies (LIEs) and 44 percent of low income developing countries (LIDCs) were either in debt distress or at high risk of external debt distress.[8] The current buildup in debt began after the Heavily Indebted Poor Country (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) in the early-2000s helped clear the debt overhang of the 1990s for most LICs. It was facilitated by the improved access of many LICs to international capital markets following HIPC and MDRI as well as the search for yield as investors looked beyond advanced economies where returns have remained relatively low following the GFC. An indicator of the pressures that increased debt placed on public spending in many LICs can be seen in the pace of increase of their debt service payments. Between 2011 and 2019, average public external debt service rose in 61 low- and lower middle income countries from 5.5 percent of government revenue to 12.4 percent. And in 15 of these countries, public external debt service payments in 2019 exceeded 18 percent of revenues.[9]

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[7] For details and analysis of each of these flows as well as the characterization of LICs, see Lee and Cardenas (2020).

[8] IMF (2020a). Low income economies (LIEs) are defined here as countries that are eligible for concessional financing from the World Bank, i.e., IDA-eligible countries, through the IDA18 period (FY18–20), including Bolivia, Sri Lanka and Vietnam, which graduated from IDA at end FY2017 but are receiving transitional support on an exceptional basis during the IDA18 period. Low Income Developing Countries (LIDCs) include all Poverty Reduction and Growth Trust (PRGT)-eligible countries, and so excludes (relative to LIEs) high-income small states and some countries that have graduated from the PRGT.

[9] Jones (2020).

Stalling reforms

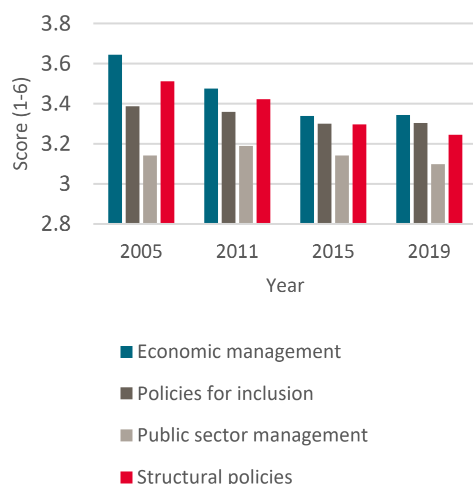
Apart from the availability of adequate and affordable financing, the pace of progress towards the SDGs is mediated also by the quality of policies and institutions in recipient countries. Sound policies and robust institutions help ensure that financing—external and domestic—is deployed in ways that support higher growth and better service delivery thereby facilitating progress towards the SDGs. Looking broadly at the policy environment in LICs, both within Sub-Saharan Africa (SSA) as well as in other regions, the data indicate that, after improvements in the period leading up to the GFC, there has been some deterioration in recent years.

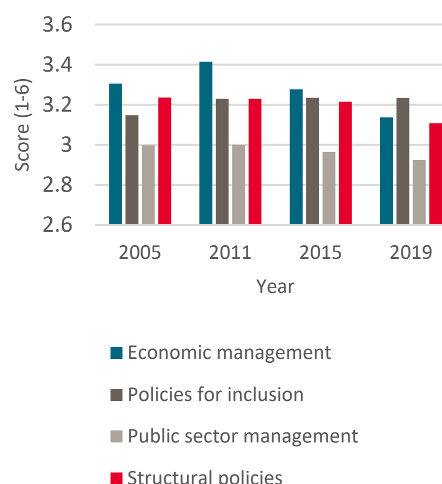
A comprehensive measure of the evolution of the policy and institutional framework in low-income countries is provided by the World Bank's Country Policy and Institutional Assessment (CPIA).[10] While there are some differences in the trends in average CPIA scores between LICs in Sub-Saharan Africa and those elsewhere, they point generally to the worsening of the policy and institutional environment on most dimensions since 2011 (Figures 1 and 2).

For low-income countries outside Sub-Saharan Africa (non-SSA LICs) as well as SSA LICs, this decline in the (average) quality of policies and institutions after 2011 was evident in all categories, especially for economic management, structural policies and public sector management (Figures 1 and 2). For non-SSA LICs, the decline after 2011 extended to the quality of policies for inclusion (Figure 1).

The CPIA also includes disaggregated ratings for three aspects of the quality of countries' fiscal policies that are especially important in determining the pace of progress towards the SDGs—efficiency of revenue mobilization; quality of budgetary and financial management; and equity of public resource use.

[10] The CPIA rates countries annually in 16 areas grouped into four clusters: (i) economic management; (ii) structural policies; (iii) policies for social inclusion and equity; and (iv) public sector management and institutions. In each area, countries are scored (on a scale of 1–6) on the basis of World Bank staffs' expert assessments of the quality of policies and institutions. In what follows, low income countries are those that are eligible for assistance from IDA, but excludes fragile states.





Source: World Bank, World Development Indicators.

Of these three areas, the efficiency of domestic revenue mobilization is especially significant because it shows the extent to which countries can match external financing with their own resources to sustain progress towards development goals. While low income countries have improved their performance in this regard since the early-2000s, with their average tax to GDP ratio rising from about 10 percent in 2000 to around 14 percent in 2018 (and to about 15 percent for SSA LICs), these improvements appear to have stalled at this relatively modest level.[11] This recent stagnation in the efficiency of revenue mobilization in LICs, both in SSA and elsewhere, is confirmed by the trends in the corresponding CPIA scores (Figures 3 and 4). Moreover, the buoyancy of the tax systems in most of these countries appears relatively low. For instance, estimates by Gupta and Liu (2020) for 44 countries in Sub-Saharan Africa (SSA) suggest that long-term buoyancy is only slightly higher than one.

A similar pattern of deterioration after 2011 is evident for LICs in both SSA and in other developing regions also for the quality of budgetary and financial management policies and for policies aimed at equity of public resource use (Figures 3 and 4). Even more concerning is that among these three measures of fiscal policy, the average quality of budgetary and financial management, which is critical for service delivery, is the lowest for LICs in SSA and elsewhere.

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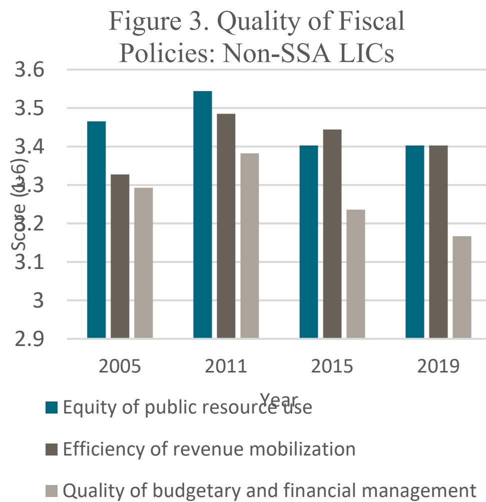
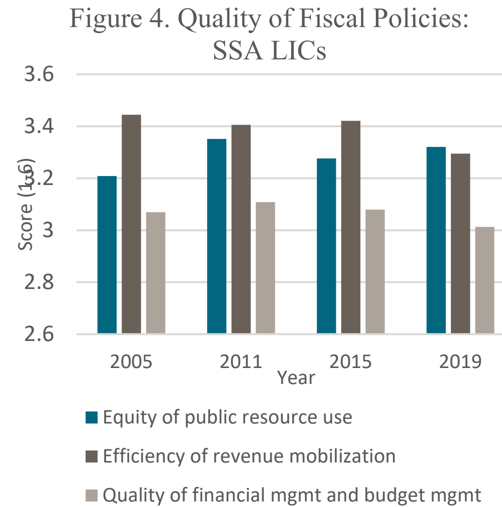
[11] Mullins et. al. (2020). As noted there, an important reason for this increase in LICs' tax ratios has been their adoption of the Value Added Tax (VAT). This grouping of LICs reflects the country classification used by the IMF's Fiscal Monitor (https://www.imf.org/external/datamapper/datasets/FM) and its composition differs from and is larger than that based on the World Bank's income classification cited in footnote 6.





Source: World Bank, World Development Indicators

The Impacts of COVID-19 on Progress towards the SDGs

The pandemic and its continuing impacts on the global economy threaten to slow, and even reverse the progress that most LICs have made towards the SDGs. There are several reasons for this pessimism. These include: the poor prospects for global growth in the short term and uncertainty regarding the timing and robustness of the ensuing recovery; the likelihood that the fiscal situation of most countries will worsen as revenues slump and pressures on public spending increase; the likely worsening of most of their external debt situations as export prices and volumes fall even as their borrowing needs increase; their difficulties in raising domestic revenues, and more broadly of initiating and sustaining growth-oriented reforms in an unfavorable economic environment; and the reversal of the modest inflows of private capital into their economies pre-pandemic.

First, the global economy will shrink in 2020 for the first time in a decade. And it is expected at best to see only a slow and patchy recovery in the medium term. According to the latest IMF projections, the global economy will shrink by about 4.4 percent in 2020, followed by a rebound of about 5.2 percent in 2021, although the latter estimate is highly uncertain depending very much on global progress in controlling the pandemic.[12] While LIDCs are expected to see a smaller contraction (-1.2 percent on average), their performance will vary considerably across countries and regions, with the economies of Sub-Saharan Africa expected to shrink by about 3 percent in 2020. Commodity exporters will also be hit harder than others with commodity prices expected to continue to be low.

[12] IMF (2020b).

Second, the severe economic downturn that is affecting most LICs means that their fiscal challenges have worsened and will likely continue to do so. The pandemic has forced many of them into damaging lockdowns, depressing output and revenues. At the same time, pressures to raise spending have also increased. Health-related expenditures will continue to rise as they deal with the effects of the virus. And social spending to mitigate the effects of the economic downturn on those most affected has risen. Revenues have come under pressure both in commodity-exporting countries that have seen commodity prices fall as well as in other LICs where revenues are tied more directly to domestic activity. The result is that fiscal deficits have widened. In 2020, Ghana's fiscal deficit, for instance, will rise by almost 7 percentage points relative to 2019, while those in Rwanda, Cote d'Ivoire, Burkina Faso and Malawi will rise by about 3 percentage points.[13]

Third, the severe economic contraction and the resulting budgetary pressures will have knock-on effects on the debt sustainability of most LICs even where countries were not at risk of debt distress before the pandemic. As growth slows and there is greater need for additional spending, it will be more difficult for many countries to keep up with their scheduled debt service payments. Although the IMF is providing grant-based debt service relief for an initial period of six months to the 29 poorest LICs with outstanding credit through its Catastrophe Containment Relief Trust, most LICs have also borrowed from bilateral and commercial lenders. While the Debt Service Suspension Initiative (DSSI) of the G-20 was intended to address debt service to official bilateral lenders, it is limited in scope and its current design has proven relatively unappealing for many LICs.

Fourth, private capital flows are turning away from developing countries, and especially from LICs. Despite the historically low returns in advanced economies, private capital is turning back towards safety, as is characteristic in turbulent times. Even LICs that were able to access capital markets in the past have found it difficult to do so in recent months as sovereign bond spreads have remained high.

Finally, the economic environment in which LICs find themselves and that is likely to persist in the foreseeable future is one that is not seen to be supportive of sustained structural reform. With their economies contracting, businesses collapsing, job losses mounting and pressures on public spending rising, it will be difficult for even the most committed reformist governments in these countries to continue to sustain growth-oriented reforms, including adopting more efficient tax systems, as well as to improve the composition of public spending in ways that foster efficiency and equity.

In sum, the pandemic has already slowed, and will continue to be a drag on, the progress of LICs towards the SDGs because it weakens their growth prospects while making it more difficult for them to generate financing from the available sources. With only a decade between now and the deadline for reaching the SDGs, these impacts mean that even more

[13] Zeufack et. al. (2020).

difficult choices now face policymakers in these countries in their efforts to accelerate progress towards the SDGs.

The Most Promising Options for Sustaining Progress towards the SDGs

At this challenging time for countries across the world, sustaining progress towards the SDGs in LICs in particular will require a mix of actions, balanced between addressing short-term concerns and longer-term priorities. And to be effective, these actions will need to be coordinated across a range of actors—the countries, their donor partners, development finance institutions—bilateral and multilateral, and multilateral institutions. They will also need to balance the urgency of acting quickly in the midst of a crisis with recognizing the ambition inherent in the SDGs.

Addressing Short-Term Concerns

Addressing debt vulnerabilities

Among the most urgent actions needed from the global community in the short term are steps to address the debt service problems that most LICs are now confronting. Without concerted action now, it is likely that more LICs will find themselves in debt distress, which will cast a long and lingering shadow over their efforts to make faster development progress once this crisis ends.

The history of developing country debt crises is one of failing to marshal the will to address liquidity problems early enough or to recognize when these have already become solvency problems. This has meant that a prolonged crisis results and the adverse effects of the debt overhang on the debtor countries are magnified. With the pandemic, it has been recognized quickly that many LICs, especially those dependent on commodity exports or tourism revenues or those already debt burdened or that have been hit especially hard by infections, already face serious problems in servicing their external debt. Not surprisingly, the chorus has grown for these countries to benefit from debt standstills.[14]

The Debt Service Suspension Initiative (DSSI), which was announced by the G20 in April 2020, reflected the recognition by the global community of the seriousness of the debt vulnerabilities for 73 low- and lower middle-income countries. In response to debtor countries' requests, the DSSI enables the suspension of their debt service payments to

[14] See, for example, https://www.brookings.edu/blog/africa-in-focus/2020/04/18/covid-19-and-debt-standstill-for-africa-the-g-20s-action-is-an-important-first-step-that-must-be-complemented-scaled-up-and-broadened/; and https://www.project-syndicate.org/commentary/a-letter-to-g20-governments-by-erik-berglof-et-al-2020-04?barrier=accesspaylog

bilateral official creditors for a limited period.[15] This suspension is intended to ease the short-term financing constraints these countries face in the aftermath of the pandemic.

While the DSSI is a welcome first step in helping LICs deal with their debt vulnerabilities, it is only that. It will help address the immediate liquidity needs of the countries that choose to participate. In so doing, it provides each of them and their creditors the space to assess and address debt sustainability more systematically. However, whether this opportunity will be seized and acted upon in a way that helps ease the long-term debt vulnerabilities of LICs is still very much in doubt.

A major concern emerges from the hitherto limited participation of the eligible countries. As of October 2020, 46 out of 73 eligible countries had sought relief under the Initiative, which meant that more than a third of the countries that could have benefited from it have not yet chosen to take advantage of it.[16] This degree of non-participation highlights the concerns that many LICs have about its likely adverse impact on market access. Specifically, missed payments by countries to official creditors under DSSI can be viewed legally as cases of sovereign default under many bond and loan contracts, which now account for the bulk of long-term public and publicly-guaranteed debt held by private creditors.[17]

To address this, the recent six-month extension of the DSSI will need to be complemented by several modifications. Specifically, more objective standards are needed for determining when temporary suspensions are warranted so that countries do not fear the adverse consequences of suspending debt payments. In this regard, the template waiver letter that the International Institute of Finance (IIF) has formulated for use by countries to seek agreement from private creditors that suspension of debt service to official creditors will not be viewed as default on private debt contracts is a step in the right direction. Countries also will need to be assured of more financing from the IMF and the MDBs, including the World Bank, if they participate in DSSI. And to incentivize greater participation by private creditors in debt restructuring efforts, their involvement needs to be linked to such additional financing from the IMF and the MDBs. Finally, given the likely persistence of the pandemic, the Initiative itself needs to be extended further beyond April 2021.[18]

[15] This period was initially six months but has now been extended until April 2021 with the possibility of further extensions.

[16] As of end-August, World Bank estimates indicate that 43 countries had benefitted under DSSI with temporary debt service suspension from official bilateral creditors of about US$5 billion. This amount accounted for more than 75 percent of eligible official bilateral debt service under the DSSI in 2020. See Development Committee (2020).

[17] For more discussion of this point as well as of the incentives of private creditors to free ride on the participation of official creditors in DSSI, see Lee (2020). For a broader critique of the DSSI by CSO groups, see EURODAD (2020).

[18] For recent recommendations from the IMF and World Bank on the changes needed in the design and scope of the DSSI, see Development Committee (2020).

Other challenges beyond the design and coverage of the DSSI will also need to be addressed if the debt vulnerabilities of LICs are to be resolved as the pandemic continues. While there is no substitute for case-by-case analysis of debt sustainability, the process of debt restructuring that will likely be necessary in many LICs will need to be expedited by finding ways to get two other significant groups of creditors to participate. These are private bondholders without collective action clauses, as well as official lenders from China and other non-OECD countries. Neither group is part of the Paris or London Clubs, and as a result has incentives to free ride on such initiatives as the DSSI as well as on additional concessional assistance from the IMF and the MDBs. Yet, the significance of these groups of lenders in LICs has grown in recent years following on the HIPC Initiative and MDRI, and no attempt to restructure debt in LICs will be able to achieve results without their participation. For instance, it has been estimated that debt service on official bilateral loans represent only about 44 percent of total debt service for DSSI-eligible countries in Sub-Saharan Africa. To this end, endorsement by G20 leaders at their recent summit in Riyadh of a "Common Framework for Debt Treatments beyond the DSSI" is a helpful step provided it is quickly translated into action.[19]

Maintaining levels of concessional funding

Bilateral donors and multilateral financial institutions need to find ways of sustaining concessional flows to LICs. Finding effective ways of easing the difficulties of LICs in servicing their external debt will help address the liquidity impacts of the pandemic. But it will not be enough to sustain their progress towards the SDGs. In particular, the health, economic and human costs of the pandemic will require that these countries increase public spending in a range of areas. These increases will mean that fiscal deficits will continue to rise and given the shallow domestic capital markets in these countries, the bulk of these will need to be financed externally. Increased aid flows will not only help finance progress towards the SDGs over the medium term. In the short term, they are a way of preventing recipient countries from avoiding the risk of debt distress. Although many bilateral donors are themselves facing domestic economic difficulties due to the pandemic, this is not the time for them to turn their backs on the budgetary constraints being faced by LICs and their inability to "do whatever it takes" to provide relief and support economic recovery.

Three priorities stand out in this regard. First, rich countries should at least maintain their ODA commitments in real terms in the short term. As noted before, real ODA flows have fallen in recent years both in levels and more significantly as shares of donor countries' incomes. So, keeping them constant in real terms despite a severe global recession should not be overly onerous, while helping to improve the economic outlook for recipient countries.

[19] See https://www.g20riyadhsummit.org/pressroom/g20-riyadh-summit-leaders.

Second, rich countries need to fulfil their commitments as shareholders of multilateral development banks (MDBs), including the World Bank and the regional development banks, so that these institutions can step in and provide financing to LICs at this time of exceptional need. The main reason that MDBs have chosen not to participate in DSSI is their reasonable concern that providing debt relief along these lines will affect their AAA ratings and therefore their ability to mobilize resources from capital markets, unless the costs of providing such relief are offset by contributions from their shareholders.[20] The World Bank, for instance, has chosen to proceed not by offering a debt standstill to its poorest borrowers (those that are eligible for International Development Association credits) but rather by trying to scale up its own commitments and disbursements. Although there are questions as to the extent to which the Bank has been able to scale up commitments, it is evident that its ability to expand its lending to LICs, especially in the form of quick-disbursing budget support (so-called Development Policy Loans) will be constrained going forward unless IDA resources can be topped up.[21]

Finally, more can be done even in the short term by bilateral and multilateral Development Finance Institutions to use concessional finance to catalyze larger private capital flows to LICs. The most promising approach would be a combination of: reforms of the ways in which DFIs operate, modifications in how they are financed, and changes in their allocation of concessional financing. Specifically, these options include: setting targets for commitments and concessional financing; and adapting their financial structures so as to allow them to take more risk, which is essential to operating in LICs.[22]

Continuing reforms to spur growth and improve service delivery

Despite the challenge for countries to sustain reforms at a less than propitious time with their economies shrinking or under pressure due to the pandemic, it will be critical that they keep up the momentum of reforms. Once the recovery from the current global slowdown begins, LICs need to be well positioned to be able to raise their growth rates and reduce poverty, not least to make up for the losses suffered during the current crisis. The potential for such a resumption in growth and improvements in public service delivery will depend mostly on whether countries can keep up the momentum for reform even during this challenging period. While the reform agenda itself will necessarily be country specific, four policy areas deserve particular attention.

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[20] See, for instance, http://pubdocs.worldbank.org/en/976541595021399817/DSSI-Explanatory-Note.pdf, for the view of World Bank management.

[21] See Duggan et. al. (2020) for an analysis of World Bank commitments and disbursements in response to COVID-19. Also see https://www.devex.com/news/world-bank-s-fund-for-poorest-countries-seeks-emergency-funding-to-avoid-a-cliff-98318 for a discussion of the need for additional funds to top up IDA ahead of its next replenishment cycle to address the crisis.

[22] See Lee and Cardenas (2020) for details of these proposals.

First, in most LICs, improving the business climate and deepening domestic capital markets remain priorities for spurring growth. Reforms in both areas will help promote inflows of private capital—domestic and foreign. Such reforms will obviously require to be customized to country contexts and will require commitment on the parts of country authorities and other stakeholders. It will also need support from external partners. DFIs can play a significant role in this regard. Through sectoral compacts with LIC governments that link support in the form of concessional funding to progress in implementing reforms, DFIs can help identify reforms and build support for them.

A second reform area of focus is to improve budgetary processes and outcomes. Cross-country ratings (Figures 3 and 4 above) show that budgetary and financial management processes and procedures in LICs remain a particular weakness and that their quality has deteriorated further in recent years. Coupled with concerns (also evident from these cross-country comparisons) in the equity of public resource use, such weaknesses mean that without considerable and sustained improvement, additional public spending, whether domestically or externally financed, will not improve growth and service delivery outcomes. In particular, large infusions of concessional external resources into these countries, even if available, would not by themselves catalyze faster progress towards the SDGs. These policy and institutional weaknesses need to be addressed even, and especially, during a crisis such as this one because it is important to ensure that any scaling up of public spending at this time will actually benefit the poor and vulnerable who need it the most rather than being captured by those better off. Oft-discussed and postponed reforms to social protection systems that would make them better targeted and more nimble are one example.

Third, efforts to upgrade debt management and improve debt transparency in LICs need sustained emphasis and support even as ways are found to ease their debt burdens. Better systems and processes for monitoring and managing debt will give countries greater credibility as they seek foreign capital and will help forestall the next debt crisis. While many LICs that benefited from debt relief under HIPC and MDRI have taken steps to improve their debt management systems, this form of institution building is a long haul and will require sustained effort and commitment.

A final area of focus is improving public investment management. Progress towards the SDGs will require that LICs implement a substantial scaling up of public investment. It is critical, therefore, that these investment projects be well selected and implemented. However, programs for public investment management in most LICs still have major gaps in how potential projects are screened, selected and financed. As with debt management, reforms in this area require time, analysis and commitment. And ensuring sustained external support to country-led efforts will be critical.

Focusing on Longer-Term Priorities

Undertaking fiscal consolidation

Once the pandemic eases and global conditions revert to normalcy, it will be necessary for LICs to design and implement appropriate strategies for fiscal consolidation. With the pandemic has come an expansion in fiscal deficits in most LICs. This widening of deficits has been essential to cope with the increased need for health and social protection spending in the wake of the pandemic, although when compared to the actions taken by their advanced economy counterparts have been far less dramatic. The strategies for consolidation will need to be carefully designed so as to not throttle growth while not burdening those who have suffered the largest losses of income as a result of the pandemic. They will also need to be supported by external partners.

The medium-term fiscal strategies of LICs will, therefore, need to incorporate well thought out revenue and expenditure components as well as include ambitious but realistic goals for external financing. Revenues will need to be raised efficiently and equitably over the medium term while public spending programs will need to be scrutinized to ensure that they are efficient and well targeted. Each of these is discussed below. From the standpoint of progress towards the SDGs, the role of donors in supporting the fiscal strategies of countries will be critical. Specifically, they will need to support the process of fiscal consolidation by ensuring that countries that have credible fiscal programs receive adequate financing so that they are not forced to consolidate too rapidly or in a haphazard fashion that could hinder their progress towards development goals.

Raising domestic revenues

It will be necessary to keep the focus on the longer-term goals of raising revenues efficiently and equitably once the recovery from COVID occurs.[23] Clearly, the midst of a severe crisis is not the time for countries, much less financially-strapped LICs to be looking to mobilize more domestic revenues. Nevertheless, this was a difficult area even pre-COVID—one in which many LICs and their partners have toiled for many years with not always a lot to show for it. A starting point, given that many LICs have introduced temporary fiscal measures to address the impacts of the pandemic, will be to reverse these sources of revenue losses as and when the crisis eases.

Beyond that, some lessons are clear from successful tax reforms. First, for reforms to work, it takes a mix of technical expertise, appreciation of the country context, and a good sense for the political economy. Second, there is a need both to take the long view and to involve multiple agencies and levels of government while linking DRM to the overall development strategy. Third, it is essential that the progress of reforms be monitored in terms of their

[23] See Mullins et. al. (2020) for a discussion of reform options aimed to raise domestic revenue mobilization in LICs.

revenue impacts as well as their effects on efficiency and equity. Finally, improving tax administration remains an ongoing and cross-cutting priority.

Improving the efficiency and targeting of public spending

Going forward, especially given the seriousness of the current crisis, there needs to be an emphasis on upgrading the quality of public spending, current and capital, over the medium term. The excessive focus on "financing the SDGs" has meant a relative lack of emphasis on how this financing should be used to ensure that countries do in fact make rapid progress towards the SDGs. An equal emphasis on how spending is used means looking for ways to enhance the efficiency of public expenditures in achieving tangible improvements in service delivery and on SDG-related development outcomes. It also means ensuring that public spending is well targeted at enhancing equity and improving distributional outcomes.

Deepening Partnerships and Strengthening Coordination

The agenda outlined here is an ambitious one, especially in the midst of a severe crisis. Nevertheless, it is achievable. Low income countries can make substantial progress towards the SDGs in the coming decade. But it will require global coordination and partnership on a scale both deeper and wider than is evident today. Specifically, actions will be required on the parts of low-income countries themselves; of the donor countries that support them; of International Financial Institutions; and of bilateral and multilateral Development Finance Institutions.

Why are coordination and partnership so important? The challenges that confront LICs in pursuit of the SDGs are complex. Whether the task is one of providing debt relief, of controlling the pandemic and stimulating global growth thereafter, or of helping improve service delivery outcomes, these challenges cannot be addressed through unilateral action by a single group. Rather, it will require action on the parts of multiple actors. For instance, speedy and effective debt relief requires that all creditors have the incentives to participate while the debtor countries undertake the needed reforms to reorient their policies and institutions to promote inclusive growth. Raising domestic revenues will require that advanced and emerging market economies work with LICs in strengthening the international tax framework so as to reduce opportunities for base erosion and profit shifting. Improving service delivery means that LICs will need to address bottlenecks and constraints that result in the diversion of public spending from its desired goals and recipients or render it ineffective.

Moreover, actions will need to be coordinated. Any effort at debt relief that does not include non-Paris Club creditors or private lenders will not be as effective as one that succeeds in drawing them in. Dealing effectively with the pandemic and reviving global growth will require simultaneous and phased actions by both rich and developing countries in ensuring, for instance, that vaccines when available are accessible to all and in keeping their markets open to goods and services from other trading partners. Efforts to raise revenues or to

improve the quality of public spending in LICs will be facilitated when external partners collaborate with the countries themselves and with each other around common platforms and assessment tools, such as the Tax Administration Diagnostic Assessment Tool (TADAT) and the Public Expenditure and Financial Accountability (PEFA) program, rather than duplicate their efforts.

Fortunately, there is a history of effective partnership and coordination among development partners that dates back to the Monterrey Consensus of 2003. In this spirit, the key actions required of various partners at this juncture are:

- Low income countries will need to continue implementing economic reforms and planning for recovery even while ensuring that the impacts of the pandemic are addressed.
- Donors will need to raise aid flows over time, and ensure that the debt vulnerabilities and fiscal constraints of LICs are addressed in a timely and comprehensive manner.
- International Financial Institutions will need to find ways of increasing concessional lending and engaging collectively on supporting reforms and building capacity in LICs.
- Development Finance Institutions will need to adapt their ways of working to channel more concessional resources to LICs so as to catalyze private capital into activities that accelerate progress towards the SDGs.

Conclusions

It would be easy to be disheartened at this juncture about the prospects for sustaining progress towards the SDGs especially in low income countries. Rich and poor countries are suffering through a global pandemic of almost-unprecedented proportions and an accompanying recession that will not ease until the pandemic is halted. Even in the relatively good times that preceded this crisis, progress towards the SDGs in the poorest countries in the world had been halting on many fronts and the optimism of 2015 had been replaced by concern that many of these countries would miss many goals by 2030.

Before COVID-19, there were two reasons for concern about the determinants of progress of low income countries towards the SDGs. First, external financing for the goals was stagnant, despite optimistic statements and upbeat commitments. ODA flows had barely budged, private capital flows to LICs, especially on concessional terms, were negligible, and although more countries had been able to access capital markets, a large proportion of these were either in debt distress or at high risk of falling into it. Second, and as important, the quality of policies and institutions in LICs, which determines how well they are able to utilize external financing and generate domestic resources, was stagnating or deteriorating in key dimensions, including those governing the effectiveness of public spending, after having improved through much of the first decade of the 2000s.

These challenges have now been magnified by the onset and resurgence of COVID-19. Slower global growth, with its attendant impact on trade flows and commodity prices, has significantly worsened the economic prospects for LICs. It has also deepened their difficulties in servicing external debt while making it much harder for them to access private capital—concessional and non-concessional. Donor countries are much more focused on supporting livelihoods and lives within their own borders than with stepping up assistance elsewhere. And the open-ended nature of this crisis means that policymakers in LICs view this as being a less than propitious time to initiate and sustain ambitious policy reforms.

Nevertheless, while being realistic about the context, this is also the time to combine urgency in addressing the crisis with ambition in accelerating the progress of LICs towards the SDGs. In identifying and implementing the most promising options, it will be necessary to find a mix of short- and longer-term actions that help find this balance. And if these efforts are to be successful over the coming decade, coordinated actions will be required on the parts of *all* development partners.

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