The Risks of Private Capital Mobilization Proposals in Paragraphs 33 and 34 of the FfD4 Zero Draft to Ensuring High Quality Net Flows

By:

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The Zero Draft: Outcome Document of the Fourth International Conference on Financing for Development was published on January 17, 2025. This draft will go through a series of negotiations in the coming weeks in preparation for the Fourth International Conference on Financing for Development in Seville Spain from June 30th to 3rd July 2025.

My comments focus on Chapter II on Domestic and Financial Private Business and Finance. I will focus on the proposals relating to domestic financial sector, enabling environments and access to financing in paragraphs 31, 33 and 34 of the Zero Draft. My overall comment is that these proposals are a wish list for foreign investors and further that these proposals not proven avenues of raising good quality financings.

The proposals included paragraph 34 of the zero draft are expanding long term bond and insurance markets as well as equity markets, building secondary markets in para 34(a), as well as establishing comprehensive risk management and insurance markets for small holder farmers in paragraph 34(d).

These proposals sit quite oddly with over 25 years of failed efforts to develop insurance markets to protect the poor against risks. Notwithstanding many efforts to promote agricultural insurance markets, these markets have instead exposed the poorest to new risks and costs such as hauling them into utopian visions of uplift while saddling the poor with credit. These options therefore fail to resolve the crisis they are ostensibly designed to address. These proposals do not also deal with the reason the poor have no access to finance, which is ‘ low and unpredictable incomes’ - not the lack of risk or insurance markets. These Zero Draft proposals are therefore more aligned with the profit motives of the industries promoting them than in addressing why poor people have low and unpredictable incomes as well as austerity.

Further investment vehicles like green, social sustainability and sustainability linked bonds in Para 34(c) have never been shown to be efficacious. While ostensibly designed to provide finance, these instruments are debt creating and compounding vehicles. There is no single example where these instruments have resolved financing for the climate crisis or the debt crisis. These instruments are merely garden-variety bonds, like the Eurobonds that many heavily indebted countries have accumulated in the last decade or so. The new-fangled bonds proposed in the Zero Draft therefore come at the same commercial terms including high interest rates and short maturity periods like Eurobonds even while they are labeled with terms such as sustainability, food security. Governments like them because they come without the policy conditionalities of the Bretton Woods institutions and as such governments have discretion on how they would use them. Governments overwhelming tend to use them on non-productive short term expenditures or to repay maturing bonds. From this perspective, the legions of climate finance firms promoting these green, social sustainability and sustainability linked bonds are perhaps the new vultures sauntering over heavily indebted poor countries. tThe FfD4

Zero Draft embraces these investment vehicles options lock, stock, and barrel without any allusion to their limits and risks.

Further, these new instruments (including climate bonds, green, blue and sustainability linked bonds) are problematically monetizing the ecosystems' resources of the Global South including forests and farmland. These ecosystems are being opened foreign investors without any barriers. The Zero Draft entrenches this trend of availing these resources to profit-making and extractive initiatives couched as avenues to raise private capital. Another consequence of this problematic embrace of private capital as a source of finance is that it effectively displaces the historical ecological responsibility of the Global North countries most responsible for the climate crisis. This is inconsistent with what countries of the Global South have been seeking in multilateral climate justice negotiations under the auspices of the United Nations Framework Convention on Climate Change (the Paris Agreement). In negotiations under the Paris Agreement countries of the Global South have sought the countries of the Global North that contributed most to the climate crisis to contribute towards addressing the climate crisis. Given the strong preference of countries of the Global North to private capital, rather than themselves as a source of such funding two unfortunate consequences follow. First, the countries least responsible for the climate crisis will bear the brunt of the climate crisis for which these instruments are ostensibly designed to address, and second these countries will increase their unsustainable levels of sovereign debt by subscribing to these instruments. In addition, these new bond instruments effectively offload the costs and risks of the business model of the global finance industry to indebted and climate vulnerable governments and particularly to their citizens. In other words, when things go wrong as they do when there is a default on these instruments, it is the borrower countries who will bear all the consequences.

While Paras 34 and 33 speak of developing a transparent, stable and predictable investment climate at the national level, this commitment sits in strong juxtaposition with the reality that all these garden variety bond, and therefore debt creating instruments tagged with terms such as sustainability and green are negotiated in absolute secrecy. The public that pays in the principal and interest on these bonds does not know who provides the financial and legal and other advisory services, how much is paid for these advisory services and how much such transaction costs add to the total indebtedness of borrower countries. Further, the public never gets to learn the listing frees, the credit worthiness assessment fees, third party ESG verification fees. All these amounts that go towards reducing the net proceeds of the issuance of these instruments.

Para 31 of the Zero Draft on international financial flows (IFFs) refers to effective implementation of the recommendations of the Financial Action Task Force (FATF) and Para 34(i) refers to supporting correspondent bank relationships. Yet, the Zero Draft is silent on another key inhibitor of finance flows in light of the reference to the FATF and correspondent bank relationships. The silence is on the regime of unilateral and sometimes multilateral sanctions which work pervasively with the FATF regime's designation of Global South countries as high risk. FATF and unilateral sanctions regimes kick Global South countries off from the global financial markets. This in turn debilitates their ability to access finances because these regimes act to suspend correspondent bank relationships or to close financial market access to them entirely. The suspension of correspondent bank relationships for countries under sanctions means that they cannot receive inflows of finances. The same is true of countries that come under scrutiny of the FATF regime.

The proposals in the paragraphs that I have reviewed above are inconsistent with the need for ensuring that developing countries have access to high quality net flows that will meet help them make the kind of transformative investments for their peoples and their climate needs. These proposals should therefore be carefully vetted and entirely removed from the FfD4 Draft and replaced with proposals that would provide high quality net flows to developing countries.

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