



ECLAC

COVID-19
RESPONSE

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Financing for development in the era of COVID-19 and beyond

Priorities of Latin America and the Caribbean in relation to the financing for development global policy agenda



Introduction¹

- In 2020, the Latin American and Caribbean region faced the worst crisis on historical record and the sharpest economic contraction (-7.7% and -20%, respectively, in GDP and investment growth for 2020) within the developing world.² The available data also show that the contraction of investment relative to that of GDP was greater in Latin America and the Caribbean than in other developing regions.³
- The pandemic has magnified the structural and institutional gaps of Latin America and the Caribbean.⁴ The crisis has severely impacted productive structures, resulting in the closure of more than 2.7 million firms, and the labour market, as the number of jobless persons has escalated to 44.1 million.
- Significant firm closures and employment losses, jointly with the fact that the more vulnerable segments of the population have borne the brunt of the crisis, have pushed up poverty levels from 185.5 to 209 million people (from 30.3% to 33.7% of the total population). Meanwhile, extreme poverty will increase by 8 million, to 78 million people. Also, the sharp contraction of investment will constrain future capital accumulation and the capacity of the region's economies to generate growth and employment. The region's economic and social development is likely to be set back for at least a decade. By the end of 2020, the level of per capita GDP was equal to that of 2010.⁵

¹ Unless otherwise indicated, the cut-off date for the information used to prepare this report is 1 February 2021.

² See ECLAC (2020a). The estimate of the contraction in investment and the comparison between Latin America and the Caribbean and other developing regions is based on IMF (2020a and 2021c).

³ This implies that the investment cycle in Latin America and the Caribbean displays a greater sensitivity to GDP fluctuations than any other region in the developing world (see ECLAC, 2017).

⁴ Structural gaps refer to structural obstacles that hold back sustained, equitable and inclusive growth for Latin America and the Caribbean. ECLAC has identified 12 gaps in terms of inequality and poverty, indebtedness, investment and saving, productivity and innovation, infrastructure, education, health, taxation, gender and the environment. See ECLAC (2012).

⁵ ECLAC (2020a).

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- The effects of the pandemic and the policies implemented in response have increased the liquidity needs of the countries of the region to confront the emergency phase. At the same time, these factors have led to rising debt levels (Latin America and the Caribbean is the most indebted region of the developing world), which may jeopardize the recovery and countries' capacity to build forward better.
- The predicament of Latin America and the Caribbean reflects the long-standing situation of middle-income countries whose position in the international cooperation system in terms of level of social and economic development is gauged on the basis of per capita GDP.⁶ Middle-income countries are often characterized by high levels of inequality and share some of the same vulnerabilities as low-income countries, while at the same time they are unable to create the broad-based capabilities at the firm and social level to undergo a process of structural change towards innovation and more knowledge-intensive production, and to drive convergence with more advanced economies.⁷
- Within the current context of the pandemic, a financing for development agenda faces two interrelated challenges. In the short run, it must support the expansion of public health expenditures and pay special attention to vulnerable groups, including to low-income segments and to older persons.⁸ In addition, short-term financing for development policies are also required to offset the detrimental effects of containment policies (based on social distancing and self-isolation) on economic activity and on the productive fabric (productive structure) and employment.
- This involves sustaining the consumption of individuals and families requiring exceptional transitory income support measures, such as a temporary basic income guaranteed by the State. These must have the widest possible reach, as broad strata of the population in the region are very vulnerable to falling into poverty, often owing to unstable incomes and informal jobs.
- In the medium and long run, as policy priorities shift from addressing the urgency to building forward better, a financing for development agenda must support a countercyclical policy stance aimed at increasing employment and sustaining adequate growth. Within this context, expanding public capital expenditures and outlays on productive transformation and greening the economy are key to ignite the recovery efforts.
- This report proposes a set of policy actions to address both challenges and then focusses on potential initiatives to build forward better.
- A first policy action consists in confronting the short-term challenge through the expansion and redistribution of liquidity from developed to developing countries through Special Drawing Rights (SDRs). Redistribution of liquidity can also be implemented through the establishment of multilateral funds such as the Fund Against COVID-19 Economics (FACE) proposed by the Government of Costa Rica. A second policy action focuses on strengthening regional cooperation by improving the lending and response capacity of regional, subregional and national development banks and other regional institutions.⁹
- Access to increased finance must be complemented by a third policy action to reform the international debt architecture. This would include the creation of a multilateral debt restructuring mechanism and the establishment of a multilateral credit rating agency. The Debt Service Suspension Initiative (DSSI) of the Group of Twenty (G20) must also be widened in scope, to include all relevant stakeholders (i.e. the private sector and multilateral institutions) and vulnerable middle-income countries, and must be extended beyond 2021.
- Strategies to confront the debt issue must avoid a one-size-fits-all approach. Like other developing regions, Latin America and the Caribbean is heterogeneous in terms of its economic and social structures. Different realities (in terms of size, productive base and vulnerabilities) will require careful choice and calibration of policies and instruments tailored to the specificities and needs of a particular subregion or country.

⁶ ECLAC has argued that the evaluation of countries' developmental needs and the organization and allocation of international cooperation should be guided by the structural gap approach. This approach is based on the analysis of a set of structural gaps whose relevance can differ according to the specificities of any given country. See ECLAC (2012).

⁷ This is known as the middle-income trap. See Paus (2014) and Alonso and Ocampo (2020).

⁸ This also includes households lacking interconnection. A significant part of the vulnerable are in the informal sector.

⁹ See Ocampo (2020) for a critical analysis of international financial cooperation during COVID-19.

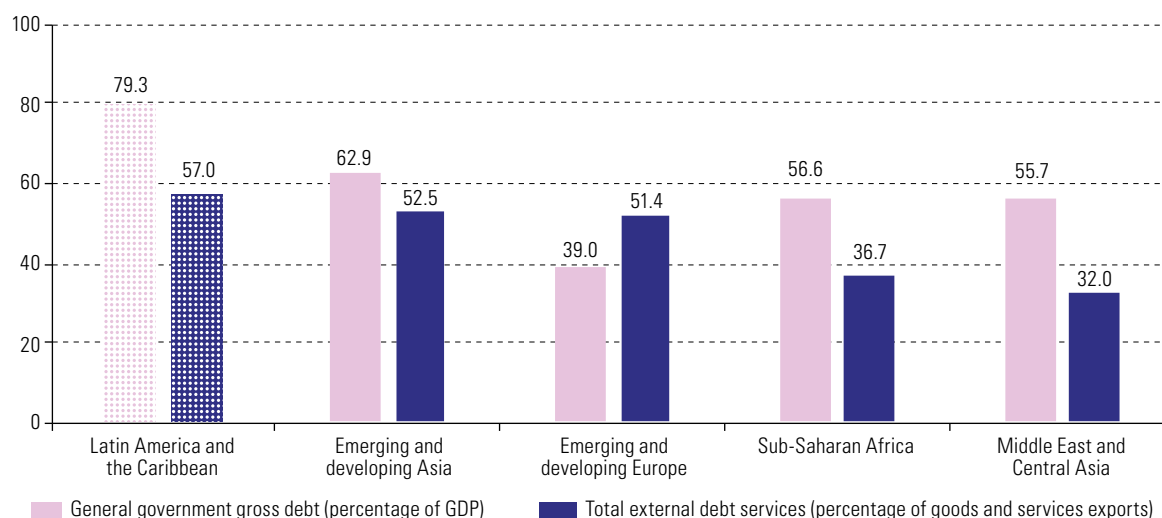
- A fourth policy action consists of establishing the common usage of different innovative instruments to improve countries' debt repayment capacity and avoid debt distress. Innovative instruments link countries' repayment capacity to their exposures and vulnerability to natural disasters (such as the case of hurricane clauses) or to the ups and downs of the business cycle (such as income-linked bonds or state-contingent bonds).
- As a fifth policy action, increased access to liquidity and debt reduction must be intertwined with medium- and long-run development objectives and thus with initiatives to build forward better. In this sense, the current crisis should also be seized not only as an opportunity to rethink the financing for development agenda of middle-income countries, but also as an occasion to reach wide social and political consensus to implement ambitious reforms in order to engage in a sustainable and egalitarian building back process. Building forward better means placing equality and environmental sustainability at the centre of the recovery phase.

A. The economic and social impact of COVID-19 will significantly widen the region's financing gap

- Government response to the emergency, focused on public health and social spending measures, in combination with the drastic fall in tax revenues, has increased fiscal deficits and exacerbated debt burdens, especially in the smaller economies, including in Caribbean small island developing States (SIDS). The latest available data show that government expenditures in Latin America rose from 15.2% in January–September 2019 to 18.1% of GDP in the same period in 2020, mainly reflecting an increase in current transfers.¹⁰ In the case of the Caribbean, government expenditure rose from 12.8% to 14.8% of GDP for the same period.
- Without exception, all countries have experienced a deterioration in their fiscal situation and an increase in the general government debt levels.¹¹ As things stand, the debt of the general government at the regional level is expected to rise from 68.9% in 2019 to 79.3% of GDP in 2020, making Latin America and the Caribbean the most indebted region in the developing world and the region with the highest external debt service relative to exports of goods and services (57%) (see figure 1).¹²

Figure 1 | Developing regions: selected debt indicators, 2020

(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), World Economic Outlook Database, October 2020 [online] <https://www.imf.org/en/Publications/WEO/weo-database/2020/October>.

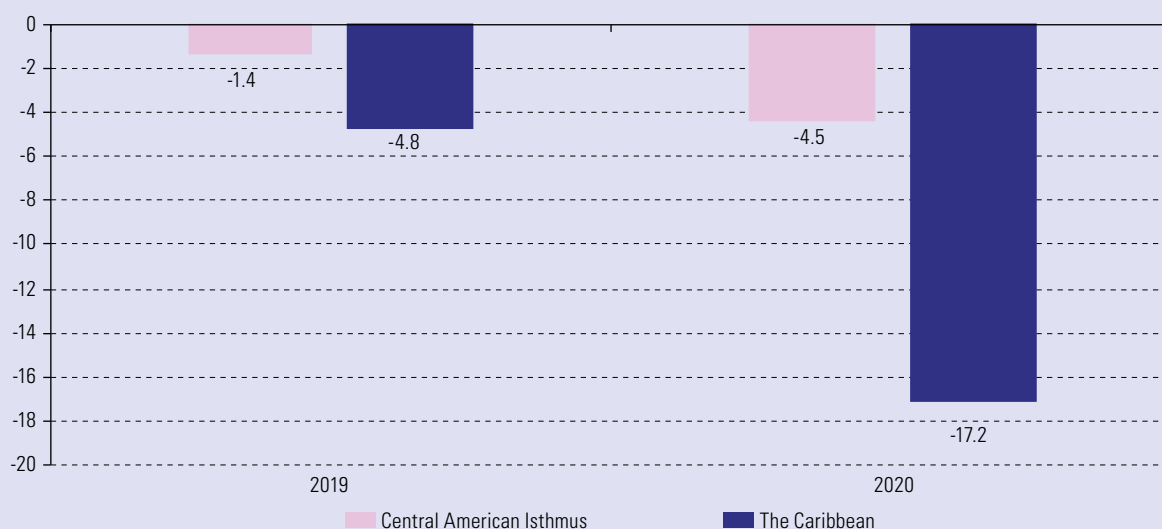
¹⁰ Current transfers explain 72% of the increase in government expenditures for Latin America. See ECLAC (2020a).

¹¹ The largest increases in the debt of the general government have been registered by Caribbean SIDS that also have some of the highest debt levels in the region. See IMF (2020a).

¹² It should be noted that the regional aggregates can hide significant disparities at the country level.

- The generalized increase in fiscal imbalances and indebtedness has given rise to greater liquidity needs across the countries of the region, in spite of their considerable heterogeneity in the fiscal situation and debt vulnerability.¹³ This places a major constraint on governments' responses to the coronavirus disease (COVID-19) pandemic and, in the medium term, it undermines their capacity to build forward better.
- The financing gap of the public sector is compounded by the need for balance-of-payments support required in particular by the region's smaller economies (Central America and Caribbean countries), as a result of the decline in exports —specifically in export services (tourism)— and supply chain interruptions. Between 2019 and 2020, the current account deficit widened from -1.4% to -4.5% of GDP in the case of the Central American Isthmus¹⁴ and from -4.8% to -17.2% of GDP in the case of the Caribbean (see figure 2).
- The region will also see a significant fall in foreign direct investment (FDI) (roughly between 45% and 55% between 2019 and 2020).¹⁵

Figure 2 | Central American Isthmus and the Caribbean: current account balance as percentage of GDP, 2019–2020
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), World Economic Outlook Database, October 2020 [online] <https://www.imf.org/en/Publications/WEQ/weo-database/2020/October>.

B. Closing the internal and external financing gap requires international financial institutions to scale up the availability of liquidity commensurate with the financing needs of Latin America and Caribbean countries

- Multilateral institutions have swiftly responded to the liquidity demands of developing countries, including those of Latin America and the Caribbean, with a series of important initiatives that share the same objectives: to mitigate the immediate impacts of the pandemic and provide finance for economic recovery. Given the unprecedented social and economic effects of the pandemic, these initiatives need to be scaled up to fully address countries' financing needs. The overall financing needs of developing countries have been estimated at US\$ 2.5 trillion, which exceeds the lending capacity of the International Monetary Fund (IMF).¹⁶

¹³ For 2019 general government debt ranges from 122% (Barbados) to 26% (Paraguay) of GDP. For 2020, general government debt ranges from 145% (Suriname) to 32% (Guatemala) of GDP. The data for 2019 exclude the Bolivarian Republic of Venezuela.

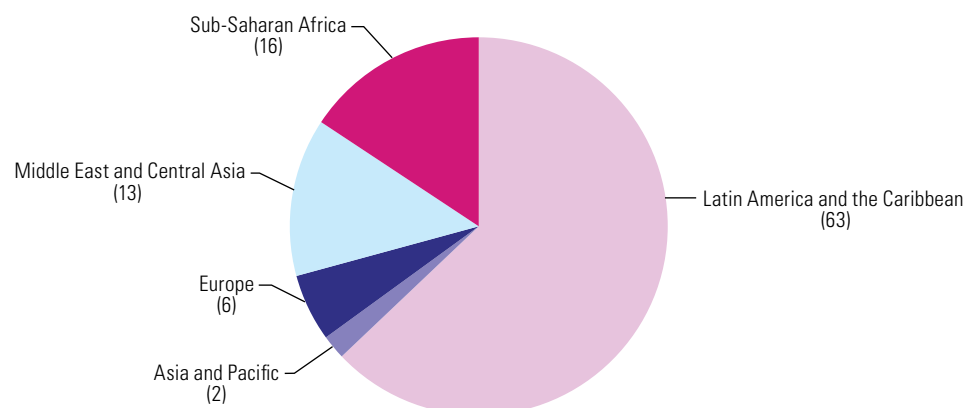
¹⁴ Data for the Central American Isthmus in this document include the Dominican Republic and Haiti.

¹⁵ The available evidence points to a contraction in FDI inflows of -45% in Central America and of -27% in the Caribbean for the second quarter of 2020 (ECLAC, 2020b).

¹⁶ The lending capacity of IMF is estimated to total US\$ 1 trillion. However, a more precise computation taking into account the Fund's lending commitments, as well as the unusable quota resources and the prudential balances, puts its lending capacity at roughly US\$ 800 billion. The US\$ 2.5 trillion figure was estimated in March 2020 and it is likely to have increased since then (IMF, 2020b).

- IMF has put at the disposal of 21 Latin American and Caribbean economies (8 Caribbean, 7 in the Central American Isthmus and 6 South American countries) the bulk of its COVID-19 emergency lending. As of January 2021, IMF had committed roughly US\$ 66.5 billion to Latin America and the Caribbean, representing 63% of its total disbursement to 85 developing economies (US\$ 106 billion) (see figure 3).¹⁷

Figure 3 | Distribution of International Monetary Fund emergency lending by developing region, January 2021
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), “COVID-19 Financial Assistance and Debt Service Relief”, 2021 [online] <https://www.imf.org/en/Topics/imf-and-covid19/COVID-Lending-Tracker>.

- Lending is provided through financial instruments with limited or no conditionality in order to improve the flexibility and response capacity of IMF to confront the effects of the pandemic. The streamlining of conditionality was also key feature of IMF lending during the global financial crisis (2008–2009).
- IMF financial instruments used by Latin American and Caribbean countries include mainly the Rapid Credit Facility (RCF), the Rapid Financing Instrument (RFI) (75% of the total) and, to a lesser extent, the Flexible Credit Line (FCL).¹⁸
- RCF is extended at a 0% interest rate with a grace period of 5.5 years and a maturity of 10 years. RFI charges interest rates below the market rate (the interest rate corresponding to SDR plus a fixed margin determined by the IMF Executive Board on an annual basis) with a payment period between 3.25 and 5 years.¹⁹ Finally, FCL is also granted at a similar cost and is renewable after one or two years. In the case of RCF and RFI, countries can borrow up to 100% of their IMF quota. In contrast, borrowing under FCL is not limited by a country’s quota and in fact there no cap on access to IMF resources.²⁰
- These financial instruments do not benefit all countries equally. Countries with strong economic fundamentals, including Chile, Colombia and Peru, can access finance with no quota limits (through FCL).²¹ However, this is not an option available to most countries, particularly Caribbean SIDS.
- Some of the Caribbean countries face recurrent fiscal and external imbalances owing in part to their small size and structural constraints and high exposure and vulnerability to natural hazards, which severely limits the possibility of achieving “track records in economic performance” as required by FLC.²² Available evidence for Caribbean SIDS shows that, prior to the pandemic, for the period 2015–2019, the combined current account deficit averaged -6.9% of GDP. In the

¹⁷ This does not include the funding provided through the Debt Service Relief from the Catastrophe Containment and Relief Trust (CCRT) amounting to US\$ 488.7 million. As of January 2021, IMF total lending commitments amounted to US\$ 267 billion (IMF, 2021a). Haiti is the only country in the Latin American and Caribbean region that, by virtue of being a low-income country, also qualifies for debt relief under the Catastrophe Containment and Relief Trust (CCRT). Between March and October 2020, Haiti was granted approval of US\$ 11.2 million under CCRT (IMF, 2021a).

¹⁸ Other financial instruments used on a much smaller scale include the Extended Fund Facility (EFF) by Barbados, Costa Rica and Ecuador; the Precautionary and Liquidity Line (PLL) by Panama; and the Stand-By Arrangement (SBA) and the Standby Credit Facility (SCF) by Honduras. In contrast to COVID-19 emergency financing instruments borrowing conditions under the EFF and SBA involve compliance with IMF conditionality.

¹⁹ The borrowing cost also includes a surcharge that varies according to the amount and the time that credit is outstanding.

²⁰ See IMF (2020c). As explained by IMF in the case of FCL “the need for resources is assessed on a case-by-case basis based on the member’s actual or potential balance of payments needs”. FCL was created in 2009 to increase “the flexibility in IMF lending and streamline its conditionality requirements” to enhance its response capacity to the global financial crisis (IMF, 2009).

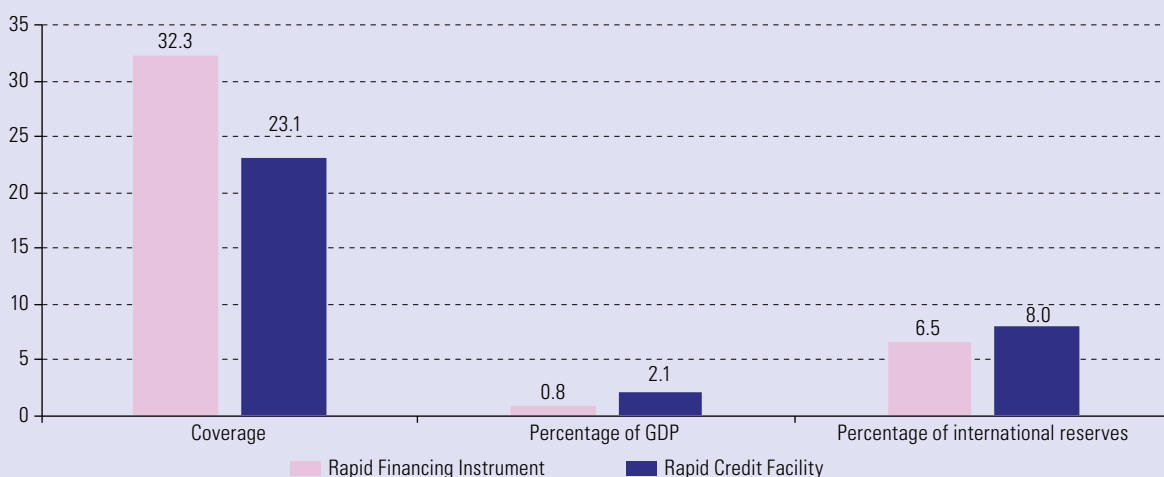
²¹ Mexico also has access to a flexible credit line (FCL). In the Mexican case, FCL was approved in November 2019 prior to the pandemic. The Mexico FCL amounts to roughly US\$ 61 billion (IMF, 2020d).

²² See IMF, 2020c.

case of the economies belonging to the Organisation of Eastern Caribbean States (OECS),²³ the external imbalance was much higher (-9.4% of GDP for the same period). These high external imbalances are associated with large indebtedness ratios in some cases.

- Available data from Latin American and Caribbean countries show that the finance provided under RFI and RCF covered on average only 32.3% and 23.1%, respectively, of countries' internal and external financing needs.²⁴ This is equivalent to 0.8% and 2.1% of GDP and between 6.5% and 8.0% of international reserves (see figure 4). Besides IMF emergency lending facilities, countries have three other alternatives to access funding: apply for an IMF standard programme with the associated conditionalities, request loans from multilateral development banks, or tap into the international bond market. The pecking order of these financing alternatives is not a settled issue. According to Standard & Poor's (2020, p. 4), multilateral development banks are lenders of last resort and should come into play "when access to commercial funding is restricted"

Figure 4 | Latin America and the Caribbean (selected economies): financing gap coverage provided by the Rapid Financing Instrument and the Rapid Credit Facility, 2020^a
(Percentages of GDP and of international reserves)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of information provided by the International Monetary Fund (IMF) and official data, 2020.

^a The figures are estimates based on a series of IMF reports on the countries of Latin America and the Caribbean that requested emergency funding through RFI or RCF during 2020, including the Bahamas, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Haiti, Jamaica, Panama, Paraguay, Plurinational State of Bolivia, Saint Lucia and Saint Vincent and the Grenadines.

C. First policy action: expand and redistribute liquidity from developed to developing countries

1. The most expedient, efficient and least costly manner to increase liquidity is a massive issuance of Special Drawing Rights (SDRs) and, in the short term, a voluntary reallocation of unused SDRs redirecting liquidity from developed to developing countries

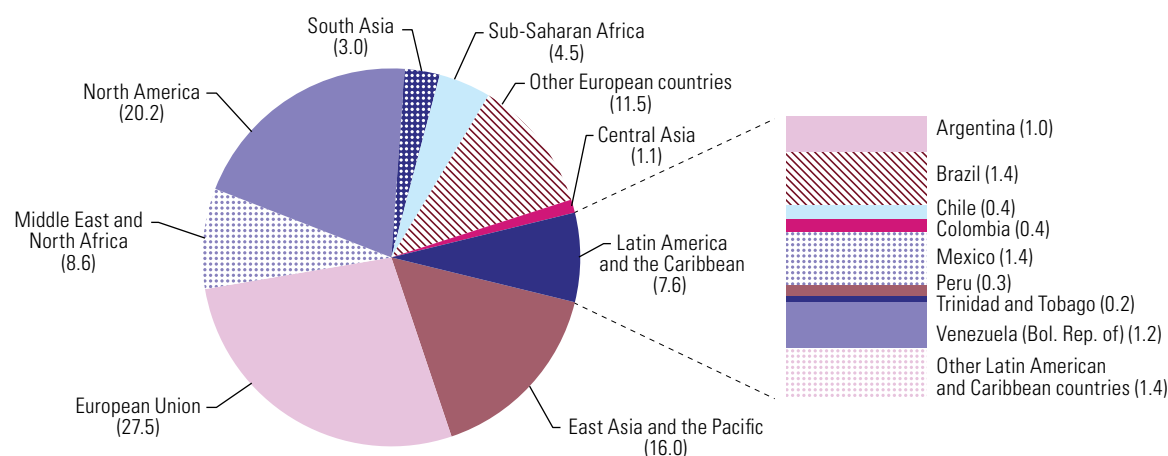
- Additional funding to cover the financing gap should be provided through the expansion of existing credit facilities, such as Special Drawing Rights (SDRs). These are an international reserve asset created by IMF to supplement its member countries' official reserves. SDRs are a potential claim on freely exchangeable currencies of IMF members. Allocations are made proportional to each member State's shareholding (quota) in IMF. As of the end of February 2021, cumulative allocations totalled 204.2 billion SDRs, equivalent to approximately US\$ 282.7 billion. This includes 182.6 billion SDRs allocated in 2009 as part of the measures to provide liquidity during the global financial crisis. In early March 2021, the G20 approved a new issuance of SDRs by IMF, the amount of which is yet to be determined.

²³ These include Antigua and Barbuda, Dominica, Grenada, Saint Kitts and Nevis, Saint Lucia and Saint Vincent and the Grenadines. The other Caribbean countries include Belize, Guyana, Jamaica, Suriname, the Bahamas and Trinidad and Tobago.

²⁴ Coverage refers to both domestic and external financing needs as estimated by the IMF when granting RFI or RCF.

- A new issue of SDRs would increase countries' liquidity without generating any additional debt.²⁵ Developing economies would be allocated about 40% of a new issue of SDRs and the rest would go to developed countries. Latin America and the Caribbean would receive roughly 7.6% of a new issue of SDRs (see figure 5).

Figure 5 | Allocation of International Monetary Fund Special Drawing Rights by region, December 2020
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), "IMF Members' Quotas and Voting Power, and IMF Board of Governors" 2020 [online] <https://www.imf.org/external/np/sec/memdir/members.aspx>.

- A hypothetical new issue and allocation of 500 billion SDRs would amount to US\$ 56 billion in additional international reserves for Latin American and Caribbean economies.²⁶
- South America, Mexico, the Central American Isthmus and the Caribbean would receive US\$ 36.7 billion, US\$ 13.2 billion, US\$ 3.6 billion and US\$ 2.5 billion, respectively (66%, 24%, 7% and 4% of the total, respectively). A new issue of SDRs would benefit some of the region's most indebted countries (including Argentina, Belize, Ecuador and Suriname) in terms of the contribution of SDRs to the build-up of international reserves (see table 1).

Table 1 | Latin America and the Caribbean (30 countries): allocation of a hypothetical issue of 500 billion Special Drawing Rights by subregion and country
(Percentages of gross international reserves at 2020 values)

The Caribbean		South America		Central American Isthmus	
Country		Country		Country	
Antigua and Barbuda	10.5	Argentina	12.0	Costa Rica	7.3
Bahamas	13.5	Bolivia (Plurinational State of)	6.1	Dominican Republic	6.8
Barbados	14.2	Brazil	4.7	El Salvador	10.8
Belize	21.3	Chile	6.9	Guatemala	3.7
Dominica	8.3	Colombia	5.4	Honduras	4.7
Grenada	6.8	Ecuador	31.4	Nicaragua	13.3
Guyana	44.4	Paraguay	3.2	Panama	7.4
Haiti	15.6	Peru	2.7		
Jamaica	15.5	Uruguay	4.0		
Saint Kitts and Nevis	5.5				
Saint Lucia	5.4				
Saint Vincent and the Grenadines	13.5				
Suriname	39.2				
Trinidad and Tobago	9.9				
Average	16.0		8.5		7.7
Median	13.5		5.4		7.3
Standard deviation	11.8		9.0		3.3

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), "IMF Members' Quotas and Voting Power, and IMF Board of Governors" 2020 [online] <https://www.imf.org/external/np/sec/memdir/members.aspx>.

²⁵ The interest rates charged for the use of SDRs are also very low, which benefits countries that have a high risk premium.

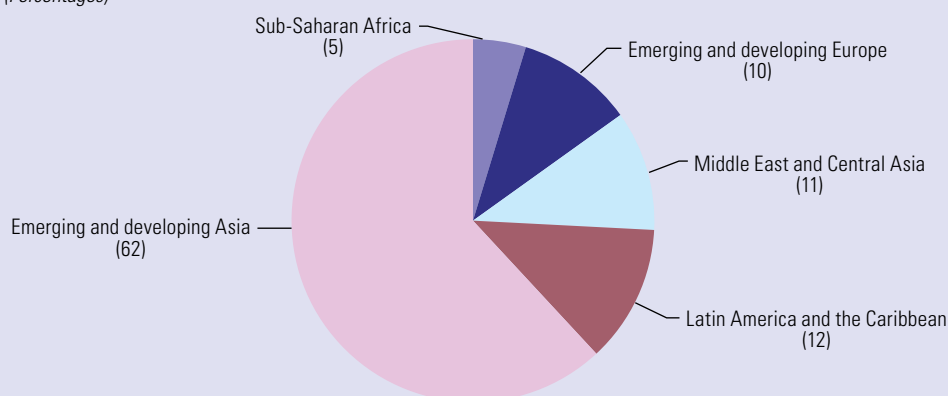
²⁶ The exchange rate between SDRs and the United States dollar was 1.433250 at 5 February 2021 (see IMF, 2021b).

- A new issue of SDRs requires the approval of 85% of the votes of IMF member countries and thus necessarily that of the United States, which holds 16.5% of the voting power of the Board of Governors of the IMF.²⁷
- Pending a new issue of SDRs, which has encountered political hurdles, liquidity could also be increased through a voluntary reallocation of existing unused SDRs (holdings of SDRs in excess of a country's allocation) from developed to developing countries. High-income countries hold approximately US\$ 190 billion in SDRs, which could be reallocated to developing countries.
- The reallocation of SDRs would require addressing important issues. While any country has the right to transfer its SDRs to another country voluntarily, the pooling of SDRs through the existing multilateral architecture would be a more effective way of dealing with the liquidity needs of developing countries, including those of Latin America and the Caribbean. In addition to set of high-income countries agreeing to give up their SDRs voluntarily, agreement would have to be reached on a reallocation mechanism. This could involve deciding which set of countries to benefit, and establishing the corresponding lending terms and criteria.
- At the regional level, it would be important to consider the creation of a new trust fund whereby countries with unused SDRs could voluntarily and/or temporarily commit part of their SDR holdings to strengthen the financial capacity of regional financial arrangements (RFAs) and other regional financial institutions (regional development banks). This proposed reallocation mechanism could apply both to newly issued SDRs and to previous allocations.

2. The creation of multilateral funds is another mechanism to redistribute liquidity from developed to developing economies

- Besides the reallocation of SDRs, liquidity funds financed by developed countries are a complementary policy option to reallocate liquidity from developed to developing countries. Liquidity funds can give a greater role to developing economies in the decision-making process regarding beneficiary countries, and also on the conditions under which liquidity is reallocated. One example of a multilateral fund is the proposed Fund to Alleviate COVID-19 Economics (FACE).
- FACE seeks to provide extraordinary financing to developing countries, including low- and middle-income countries, to mitigate the social and economic impact of the pandemic, including on households and productive sectors. FACE also envisions funding for economic recovery once the pandemic is overcome.
- The proposal is to finance this fund with resources from developed economies and channel them through multilateral development banks. The fund would consist of US\$ 516 billion (3% of GDP of low- and middle-income countries or 0.7% of developed countries' GDP) for concessional lending with a 50-year term, a 5-year grace period, and an interest rate of 0% or the current LIBOR²⁸ (0.7%). These concessional loans would be free of fiscal, monetary or structural conditionalities.²⁹
- If FACE were to distribute its funds to developing regions on the basis of the same criteria it uses to estimate the size of the fund (3% of the GDP of developing countries), Latin America and the Caribbean could receive up to 12% of FACE funds (US\$ 60 billion) which would be slightly below the funding currently provided by IMF (see figure 6).

Figure 6 | Hypothetical allocation of Fund to Alleviate COVID-19 Economics resources based on a criterion of 3% of the GDP of developing regions
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of International Monetary Fund (IMF), World Economic Outlook Database, 2021 [online] <http://www.imf.org/external/ns/cs.aspx?id=28>.

²⁷ With the approval of the United States Treasury, IMF can issue up to up to US\$ 649 billion in SDRs without requiring approval from the United States Congress.

²⁸ London Inter-bank Offered Rate.

²⁹ ECLAC/Permanent Mission of Costa Rica to the United (2020).

D. Second policy action: focus on strengthening regional cooperation by improving the lending and response capacity of regional/subregional and national financing institutions and strengthening their linkages to multilateral development banks

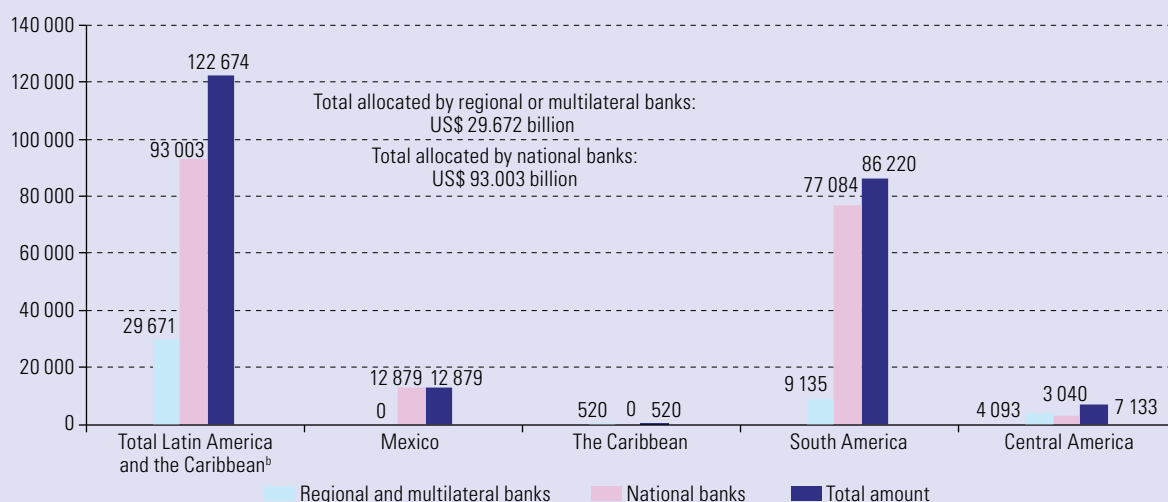
- The Inter-American Development Bank (IDB) and subregional development banks (the Development Bank of Latin America (CAF), the Central American Bank for Economic Integration (CABEI) and the Caribbean Development Bank (CDB)), have committed US\$ 8 billion and US\$ 12 billion, respectively, to fight the pandemic, which in total represents 0.5% and 1.9% of regional GDP and of exports of goods and services respectively.³⁰ These funds are targeted to finance emergency programmes, including health-related measures, as well as the provision of contingency credit lines. In the case of IDB, the expansion in lending to confront the effects of COVID-19 on the region in fact surpass those following the global financial crisis of 2008–2009.
- For their part, national development banks have committed the equivalent of US\$ 90 billion in financial support, which amply exceeds that provided by regional and subregional development banks (see figure 7). Moreover, national banks have supplied liquidity support through a variety of instruments, including guarantees, grants and refinancing schemes (see figure 8). The emergence of national development banks as key players in the provision of finance points to the need to foster greater cooperation and coordination between regional/subregional and national development banks.³¹
- The lending capacity of development banks can be increased through two different means: increased capitalization and greater flexibility in their lending criteria. CABEI increased its authorized capital by 40% (US\$ 2 billion) in April 2020, and IDB is considering the possibility of a capital increase that would enable annual lending to reach nearly US\$ 20 billion (Martin, 2021).
- IDB, as well as the World Bank, could also use its available capital more effectively by reducing its equity-to-loan ratios to a level commensurate to that of commercial banks. Multilateral development banks (MDBs) take a conservative approach to capital adequacy. The major MDBs have an equity-to-loan ratio of between about 20% and 60%, surpassing that of most commercial banks (10%–15%) (Humphrey, 2020).³² In other words, MDBs hold US\$ 2–US\$ 6 in equity for every US\$ 10 in outstanding loans, whereas commercial banks hold only US\$ 1–US\$ 1.50 per US\$ 10 in outstanding loans. The equity-to-loan ratios of the World Bank and IDB stand at 22.6% and 38.2%, respectively.
- Other institutions, such as the Latin American Reserve Fund (FLAR), are also an important component of the regional cooperation network. In response to the COVID-19 crisis, FLAR increased its lending potential to its member countries by 60%, to a total of US\$ 6.8 billion. FLAR also established an exceptional line of credit (up to 5 years with a 3-year grace period) for member countries to address balance-of-payments difficulties arising from COVID-19 (FLAR, 2020).

³⁰ The Development Bank of Latin America (CAF), the Central American Bank for Economic Integration (CABEI) and the Caribbean Development Bank (CDB) committed US\$ 10 billion, US\$ 1.96 billion and US\$ 200 million, respectively, in 2020. These estimates are based on official information from the respective institutions and press clippings and on the basis of IMF (2021b). In response to the pandemic, the IDB Group committed a total of \$8.076 billion towards financing immediate public health needs, providing safety nets for vulnerable populations, promoting economic productivity and employment, and supporting the implementation of fiscal measures to help mitigate the economic effects of the pandemic.

³¹ Coordination is also required among multilateral development banks. Coordination of development banks would avoid duplication of tasks and scale-up the mobilization of private finance, increasing the efficiency of operations. See Bisogno and Fleiss (2020) on the benefits of coordination among multilateral development banks.

³² Equity includes paid-in capital and accumulated reserves. Loans include loans, guarantees, and equity investments made for development purposes.

Figure 7 | Latin America and the Caribbean (selected countries and groupings): amounts devoted by national and regional or multilateral development banks in COVID-19 response, to February 2021^a
(Billions of dollars)

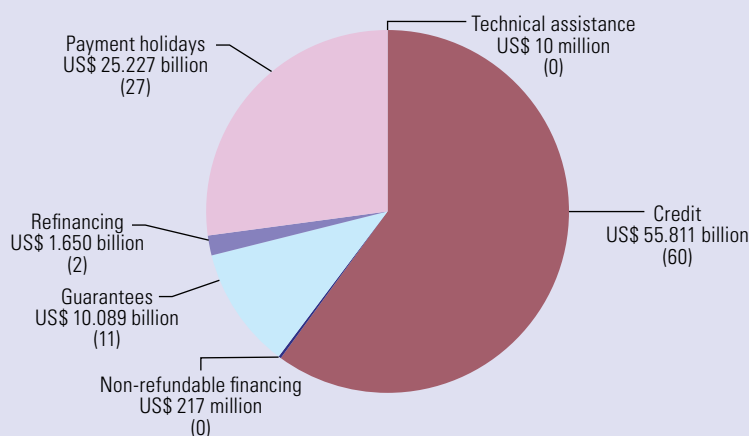


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information and press clippings.

^a Regional and multilateral banks: World Bank, Central American Bank for Economic Integration (CABEI), Inter-American Development Bank (IDB), CAF - Development Bank of Latin America, Caribbean Development Bank (CDB), International Monetary Fund (IMF) and FONPLATA Development Bank. National banking institutions: Agencia Financiera de Desarrollo de Paraguay (AFDP), Agência de Fomento do Estado do Amazonas (AFEAM), Agência do Fomento do Rio Grande do Norte SA (AGN), Agência de Fomento do Estado de Santa Catarina SA (BADESC), Agência Estadual de Fomento (AgeRio), Agência de Fomento do Estado do Tocantins, Agencia Nacional de Desarrollo (ANDE) (Uruguay), Associação Brasileira de Desenvolvimento (ABDE), Banco Agrario de Colombia, Banco Ciudad (Argentina and Panama), Banco da Amazônia, Banco de Brasília (BRB), Banco de Desarrollo Agropecuario (Panama), Banco de Desenvolvimento de Minas Gerais (BDMG), Banco de Desarrollo del Ecuador, Banco de Desenvolvimento do Estado do Espírito Santo (BANDES), Banco de la Pampa (BLP) (Argentina), Banco do Brasil (BB), Banco do Nordeste (BNB), Caixa Econômica Federal (CEF), Banco Estado (Chile), Banco Hondureño de la Producción y la Vivienda (BANHPROVI) (Honduras), Banco Nación (Argentina), Banco Nacional de Desenvolvimento Econômico e Social (BNDES), Banco Popular y de Desarrollo Comunal (Costa Rica), Banco Provincia (Argentina) Banco Regional de Desenvolvimento do Extremo Sul (BRDE), Banco de Comercio Exterior (Bancoldex) (Colombia), Financiera de Desarrollo Territorial (FINDETER) (Colombia), Banco Cooperativo do Brasil (BANCOOB), Banco Cooperativo Sicredi (Brazil), Cresol (Brazil), Bancor (Argentina), Banco de Desarrollo de El Salvador (BANDESAL), BanEcuador, Corporación Financiera Nacional (CFN) (Ecuador), Instituto Ecuatoriano de Seguridad Social (IESS), Banco de la Seguridad Social (BIESS) (Ecuador), Banco de Desarrollo del Ecuador (BDE), Corporación Nacional de Finanzas Populares y Solidarias (CONAFIPS) (Ecuador), Banco Nacional de Obras y Servicios Públicos (BANOBRAS) (Mexico), Nacional Financiera (NAFIN) (Mexico), Banco Nacional de Comercio Exterior (BANCOMEXT) (Mexico), Sociedad Hipotecaria Federal (Mexico), Banco do Estado do Pará (Banpará), Banco de Reservas de la República Dominicana (BANRESERVAS), Banco de Desarrollo Rural (BANRURAL) (Guatemala), Banco de Desarrollo Productivo de Bolivia (BDP), Banco BICE (Argentina), Banco Nacional de Bolivia (BNB), Banco Nacional de Fomento (BNF) (Paraguay), Banco de la República Oriental del Uruguay (BROU), Caja de Ahorros (Panama), Corporación Financiera de Desarrollo (COFIDE) (Peru), Corporación de Fomento de la Producción (CORFO) (Chile), Desenvolve - Agência de Fomento de Alagoas, Desenvolve - Agência de Fomento do Mato Grosso, Desenvolve - Agência de Fomento do São Paulo, Fondo para el Financiamiento del Sector Agropecuario (FINAGRO) (Colombia), Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero (FND) (Mexico), Fideicomiso Instituido en Relación con la Agricultura (FIRA) (Mexico), Fondo de Garantía para Pequeños Empresarios (FOGAPE) (Chile), Garantías Corfo para Inversión y Capital de Trabajo (FOGAIN) (Chile), Fondo de Garantías Buenos Aires (FOGABA), Banco Provincia (Argentina), GoiásFomento, Instituto Nacional de Desarrollo Agropecuario (INDAP) (Chile), Instituto Nacional de Fomento Cooperativo (INFOCOOP) (Costa Rica), Instituto para el Desarrollo de Antioquia (IDEA) (Costa Rica), Sistema de Banca para el Desarrollo (SBD) (Costa Rica), Sistema Nacional de Garantías para Empresas (SiGa) (Uruguay), Promotora de Comercio Exterior (Procomer) (Costa Rica), Instituto Nacional de Aprendizaje (INA) (Costa Rica), and Sociedad Hipotecaria Federal (SHF) (Mexico).

^b The total amount shown for Latin America and the Caribbean, in addition to the amounts individually received per country by national banking and regional/multilateral banking institution, includes US\$ 6.266 billion corresponding to joint regional multilateral and regional banking packages (IMF and CAF) and a further US\$ 9.677 billion corresponding to the updated amounts reported by IDB and CAF in February 2021, which are not disaggregated by country.

Figure 8 | Support provided by national development banks to confront the effects of COVID-19 by type of instrument, 2020
(Millions of dollars and percentages of the total)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

E. Third policy action: institutional reform of the multilateral debt architecture

1. The rise in debt is a major stumbling block to an effective response to the urgency of the pandemic and to a sustainable recovery

- Liquidity constraints faced by developing countries, including in those of Latin America and the Caribbean can, in the current circumstances, hamper countries' capacity to respond to the pandemic and build forward better. Within a low growth context, liquidity constraints may also, for some countries, turn into a solvency problem threatening both the private and public sectors.
- In the case of the private sector, lack of solvency can lead to increased delinquency, bankruptcies and financial sector losses that compromise financial stability. In the case of the public sector, solvency problems can lead to austerity policies that can aggravate the economic downturn and thus the accumulation of debt. Most Latin American and Caribbean economies have, in one way or another, committed themselves to fiscal consolidation.
- Given the importance of middle-income countries in the world economy, the absence of alternatives to address the debt problem can not only endanger the recovery but also compromise global financial stability. Middle-income countries represent 75% of the world's population, and roughly 30% of global aggregate demand. More importantly, middle-income countries account for 96% of developing country public debt (excluding China and India) (see table 2).

Table 2 | Country income groupings: external public and publicly guaranteed debt
(Millions of dollars and percentages of the total)

Grouping	Millions of dollars	Percentage
Low- and middle-income countries	2 923 874	100
Low-income countries	118 111	4.0
Lower-middle-income countries (excluding India)	1 021 506	34.9
Upper-middle-income countries (excluding China)	1 784 258	61.0
Middle-income countries (excluding China and India)	2 805 763	96.0

Source: World Bank, *International Debt Statistics* 2021, 2020 [online] <https://data.worldbank.org/products/ids>.

2. Existing initiatives to reduce debt, such as the Debt Service Suspension Initiative (DSSI), must be strengthened by increasing their scale, scope and time frame and including all the relevant stakeholders

- The Debt Service Suspension Initiative (DSSI) launched by the G20 in April 2020 consists of a temporary suspension of loan repayments (from March 2020 until June 2021) from official bilateral creditors. It applies only to the 76 countries that are eligible to receive assistance from the World Bank's International Development Association (IDA), and to all nations defined as least developed countries (LDCs) by the United Nations. As of November 2020, only 46 countries (28 in Sub-Saharan Africa, 8 in Asia and the Pacific, 7 in the Middle East, and 3 in Latin America and the Caribbean (Dominica, Grenada, and Saint Lucia)) had requested debt relief under DSSI.
- Besides focusing mainly on low-income countries and excluding most middle-income countries, DSSI does not include all relevant stakeholders. In fact, the private sector and multilateral institutions do not participate in the initiative.
- In 2020, official bilateral creditors accounted for roughly 44.4% of total debt service, which is a significant step forward. Still, the majority of debt service —25.5% and 30.1%, respectively— is owed to private lenders and multilaterals, which are not participating in the DSSI initiative. In the cases of Dominica, Grenada and Saint Lucia, multilateral and private creditors also account for the bulk of debt service (see table 3). Moreover, the savings resulting from participation in DSSI are small by any standard (0.70%, 0.72% and 0.27% of GDP for 2020 for Dominica, Grenada and Saint Lucia, respectively).

Table 3 | Dominica, Grenada, Saint Lucia and all countries worldwide participating in the Debt Service Suspension Initiative: debt service by creditor type, 2020
(Percentages of the total)

Type of creditor	All participating countries	Dominica	Grenada	Saint Lucia
Private lenders	25.5	18.0	25.0	1.0
Official multilateral	30.1	49.0	58.0	74.0
Official bilateral	44.4	25.0	17.0	25.0
Non-official	...	8.0	0.0	...

Source: World Bank, "COVID 19: Debt Service Suspension Initiative", 2020 [online] <https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative> and European Network on Debt and Development (EURODAD), *Shadow report on the limitations of the G20 Debt Service Suspension Initiative: Draining out the Titanic with a bucket?*, October 2020.

- The G20 Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative (DSSI) (November 2020) is an initiative that seeks to fill some of the gaps of DSSI such as the fuller inclusion of official creditors that are not part of the Paris Club (i.e. China). It also involves joint negotiations of official bilateral creditors with a given debtor country. Finally, it contemplates the possibility that the debtor country can request treatment from the private sector that is comparable to that provided by bilateral official creditors (G20, 2020).

3. Debt relief initiatives require changes in the international debt architecture

- An international sovereign-debt restructuring mechanism is needed to deal with obligations owed to private creditors. This is exemplified by the restructurings undertaken with private creditors in 2020 by Argentina, Ecuador and Suriname, which have led, in the absence of such a mechanism, to the adoption of harsh austerity measures.
- A sovereign restructuring mechanism goes hand in hand with the creation of a multilateral credit rating agency that can act as counterweight to the existing monopoly in credit ratings.³³ A multilateral credit rating agency could avoid conflict of interest between private and public interests.
- The existence of risk evaluation by private credit rating agencies implies transferring the regulatory authority from the government (which is normally entrusted with this task) to the private sector. This can create significant problems since credit rating agencies do not have a mandate to provide information or evaluate credit risk in the interests of public objectives, but rather to maximize profits and shareholder value (Gavras, 2012).
- Credit rating agencies are more than just opinion-makers—they have significant influence over market movements. As a result, they can affect not only the value of assets and of collaterals but also volatility and financial stability. This is especially the case during the COVID-19 crisis as private capital markets (bond markets) have become an important source of finance for developing countries, including those of Latin America and the Caribbean.³⁴ Seventeen Latin American and Caribbean countries have issued bonds between January and October 2020, worth US\$ 122 billion in total, which exceeds the amount issued for the entire year in 2019 (US\$ 118 billion).³⁵
- Changes in risk evaluation could avoid the wave of downgrades in credit ratings and in economic outlooks that has occurred since the start of the pandemic with their implications for Latin American and Caribbean economies.
- During 2020, 13 Latin American countries (Argentina, the Bahamas, Belize, Colombia, Costa Rica, Ecuador, Guatemala, Jamaica, Mexico, Nicaragua, the Plurinational State of Bolivia, Suriname and Trinidad and Tobago) witnessed credit downgrades. Ecuador, followed by Suriname and Argentina, registered the highest number of downgrades (eight, seven and four respectively) (ECLAC, 2020c).

³³ The "Big Three" credit rating agencies, Moody's, Standard & Poor's (S&P) and Fitch Ratings, control around 95% of credit ratings in the financial markets.

³⁴ However, as recent data indicate, international private markets can be highly volatile and may not be a reliable source of long-term financing.

³⁵ Historically, low interest rates in developed economies (as a result of expansionary monetary policies) have encouraged investors to buy developing market debt in search of higher profits. The evidence available for the period 2017–2019 shows that profitability during 2020 (i.e. during the pandemic) increased. Profitability is proxied by the difference between the rate of interest charged on debt issues in the international capital market and the rate of interest of risk-free 10-year United States Treasury bonds.

- During a systemic crisis such as COVID-19 and highly uncertain global conditions, the effectiveness and objectivity of ratings, including the timing of rating announcements, needs to be re-evaluated. Spending in response to the pandemic and increased indebtedness could trigger credit ratings revisions and downgrades, which could lead to capital outflows, increase the cost of capital and access to credit and worsen financial conditions. Downgrades tend to aggravate financial conditions when financing is much needed to fight the corrosive effects of a crisis.
- Debt reduction initiatives do not guarantee greater liquidity. This is why debt reduction should be complemented with liquidity injections, permanent capital controls (or capital account regulations) and proactive fiscal policy. Macprudential and capital account regulations are necessary not only to keep financial instability in check, but also for the effective implementation of expansionary monetary and fiscal policies in support of recovery.

4. Delineate a debt reduction strategy that avoids a one-size-fits-all approach, considering the heterogeneity of debt profiles and debt vulnerability in the region

- Dealing with the debt problem in Latin America and the Caribbean requires a strategy along three lines of action.
- First, all highly indebted economies should benefit from official debt relief or standstills, or both. High external public indebtedness is exemplified by the cases of Argentina (68% of GDP for the third quarter of 2020) and the majority of Caribbean SIDS, including in particular Barbados, Belize, Suriname and the Bahamas (117.4%, 114.2%, 95.3% and 74% of GDP for September 2020, respectively).
- Second, economies facing short-term debt profiles or a high debt service burden, or both, should also be entitled to some type of debt relief. Caribbean SIDS, along with Central American countries, face significant short-term debt service obligations. Debt service payments amount to 30% of government revenue on average for Caribbean countries and 2.8% of GDP for Central American countries.
- The case for debt relief in the Caribbean is strengthened by the fact that debt accumulation is driven by exogenous shocks (natural hazards) and structural features associated with their small size. The impacts of the COVID-19 pandemic will not only increase the debt burden but also lead to a reallocation of existing budgets.
- Finally, countries that have —by international standards— greater fiscal space and more solid fiscal or macroeconomic situations (for example, Chile, Colombia and Peru) can take advantage of the historically low levels of international long-term interest rates and the boost these have provided to the international bond market.
- Fiscal policy can also play an important role in improving the sustainability of public debt. In the short term, countries are financing emergency measures using a combination of budgetary adjustments, increases in public expenditure, tax relief measures and liquidity measures, including public credit guarantees. In the longer term, the reduction of illicit flows, including tax avoidance and tax evasion (6.1% of GDP —US\$ 325 billion— during 2018), coupled with progressive tax reforms to improve the collection of personal income taxes along with wealth taxes, could provide additional revenues and reduce income inequalities. Furthermore, taxing the digital economy, environmental taxes and corrective taxes targeting public health issues such as alcohol, tobacco and sugary or high-calorie beverages and food could diversify and strengthen tax revenue collection.

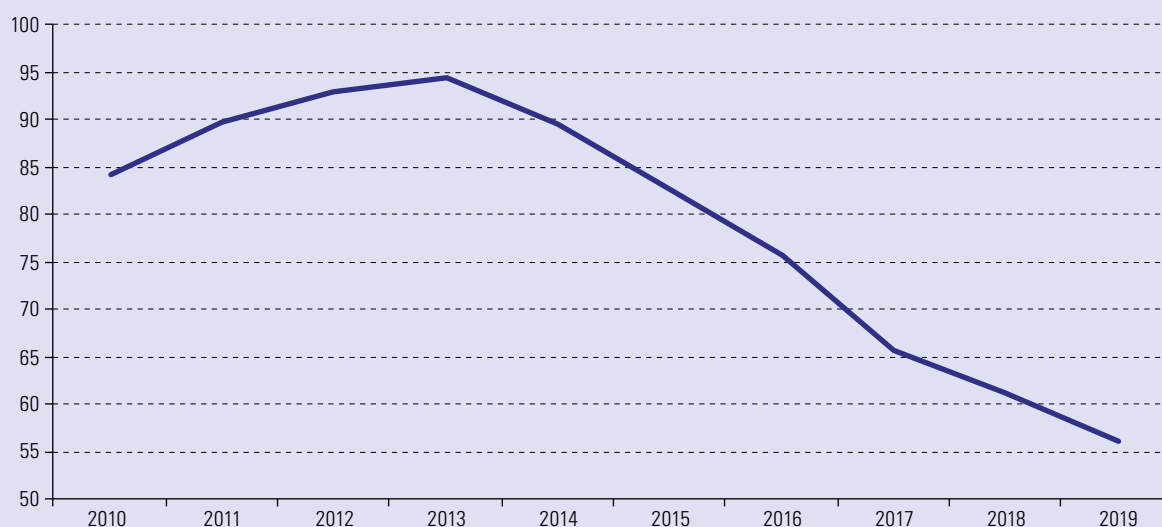
F. Fourth policy action: provide countries with a toolbox of innovative instruments to improve debt repayment capacity and avoid debt distress

1. Hurricane clauses should become a permanent feature of debt relief initiatives for countries, such as those of the Caribbean, which are recurrently exposed to natural hazards

- In the case of economies such as those of the Caribbean, the recurrent exposure to natural hazards and its devastating social and economic effects can worsen the financial situation and lead to debt distress. Hurricane clauses enable the deferral of principal and interest debt service payments or the possibility of fast-tracking debt restructuring operations, in the event of a hurricane (or other insured natural disaster).
- Important lessons for the successful application of hurricane clauses is provided by the experience of Grenada, where these were included as part of a comprehensive restructuring of the public debt which reduced the country's debt levels (see figure 9).³⁶

Figure 9 | Grenada: evolution of debt-to-GDP ratio, 2010–2019

(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information, 2020.

- Data and lessons learned show that the use of hurricane clauses must cover a significant amount of a country's debt and be of adequate duration in order to deliver the necessary fiscal space in the event of a natural disaster.
- The support and endorsement of multilateral lenders is also required to ensure successful implementation of the initiative as they can provide the necessary confidence and credibility for the private sector to engage. Finally, the experience of hurricane clauses implies the existence of economic and financial trade-offs that must be evaluated (Commonwealth Secretariat, 2016).
- By postponing debt service payments, a moratorium will lead to greater future disbursements due to the capitalization of interest payments. Countries must have the required repayment capacity to make ends meet, otherwise a moratorium simply postpones debt distress and default.

³⁶ Debt restructuring was undertaken in the period 2013–2015.

2. At a more general level, the experience with hurricane bonds underscores the need to link repayment capacity to the performance of the economy or the business cycle, as is the case with other innovative instruments worth exploring, such as income-linked bonds and state-contingent sovereign bonds

- **Income-linked bonds** are a countercyclical instrument that tie debt repayment to the capacity of a country to repay. The income-linked bond is an extension of the GDP-linked bond to developing economies that takes into account the importance of the external sector, including exports, imports and terms-of-trade, in determining a country's economic fluctuations. Income-linked bonds offer less risk and thus greater credibility for investors than GDP-linked bonds, since they include more exogenous elements making it harder to manipulate the numbers.³⁷
- This instrument reduces the burden of the debt when the economy is in a slow growth period, which is normally accompanied by reduced government revenue. In this way, an income-linked bond provides an insurance mechanism against fiscal liquidity crunches in bad times, thus reducing the probability of debt default and debt restructuring.³⁸
- **State-contingent convertible bonds** are another contingent debt instrument that allows payment standstill (either in interest or principal) or maturity extension when a certain indicator or indicators breach a given threshold. The objective of state-contingent bonds is to allow governments to deal with liquidity shortages and liquidity crises, and they can also help to avoid solvency crises. As in the case of income-linked bonds, they provide short-term breathing space, by addressing liquidity crises. Like GDP-linked bonds, they also improve burden-sharing of private sector creditors. Moreover, they reduce the size of official sector support.

G. Fifth policy action: make liquidity and debt reduction measures part of a financing for development strategy to build forward better

1. Confronting the emergency of the pandemic requires significant government expenditures

- Increased and improved access to finance and support for debt reduction initiatives are central to sustain demand and supply efforts to confront the ongoing urgency of the pandemic. These involve increased expenditure on health to contain the spread of the epidemic. Increased government expenditures are also required to offset the detrimental effects of containment policies (social distancing and quarantines) based on economic activity and on the productive fabric (productive structure) and employment. Moreover, as time is of the essence for intervention in this crisis, governments must provide rapid and urgent support to businesses and workers and promote the adequate functioning of labour-business relationships and of labour markets. Lack of adequate support could result in the permanent destruction of productive capacity and the deterioration of social conditions and labour institutionality, through higher levels of unemployment and informality. This could also potentially sow the seeds for future social conflicts.

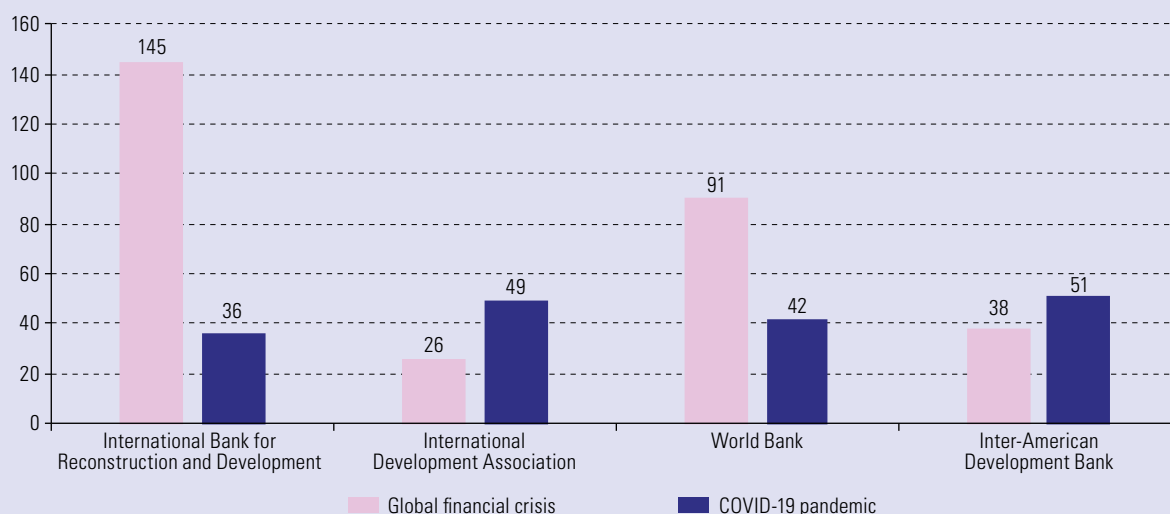
³⁷ Like any other financial instrument, a GDP-linked bond involves two parties: the issuer (in this case, the government) and the investor. Pros and cons of GDP-linked bonds should be viewed from both perspectives. The main benefits for the issuer include the reduction of default risk and reduction in credit spreads; reduction in servicing costs; increase in fiscal space; the mitigation of procyclicality; and risk sharing. The main benefit for the investor is that a GDP-linked bond provides a broader, more stable and less volatile source of income. The main caveats occur on the side of the investor; one refers to the incentive for public officials to manipulate data in order to show lower growth of GDP, which again could lead investors to increase the premium (as a reflection of the loss of confidence in government data). Other caveats on the use of GDP-linked bonds include the lack of liquidity, lack of markets to hedge GDP risk and difficulties in pricing, which can undermine their feasibility.

³⁸ The list of countries that have issued bonds with GDP-indexed features include Bulgaria (1994), Bosnia and Herzegovina (1997), Singapore (2011), Argentina (2005) and Greece (2012). The most recent experiment is that of Italy (Spence and Speciale, 2020). Most of the available empirical evidence on the performance of this instrument refers to developed countries. The evidence shows that the benefits of GDP-linked bonds in reducing default risk are larger for countries that have: (i) a lower credit rating; (ii) more volatile GDP (iii) a more constrained monetary policy (see Benford and others, 2016; and Barr, Bush and Pienkowski, 2014).

2. The policies to confront the economic and social effects of COVID-19 must link the short-term (emergency) phase to the long run

- How we think about the short run will determine to a large extent what the medium and long run will look like. Both must be integrated in order to reshape the development model towards productive transformation with sustainability and equality. To this end, recovery efforts must target resilience-building.
- Multilateral, regional or subregional, and national development banks can play a key role in spearheading recovery efforts through increased capitalization and more flexible lending standards, as mentioned earlier. The World Bank should, in addition, balance credit provided to middle-income economies, including those of Latin America and the Caribbean, and low-income countries more evenly.
- The World Bank has responded to the pandemic with a major package totalling US\$ 160 billion, centred on health; protecting the poor and the vulnerable; ensuring sustainable business growth and jobs; strengthening policies and institutions; and promoting investment for rebuilding better. However, Latin America and the Caribbean is expected to receive only 2.8% (US\$ 4.5 billion) of this total.
- The available evidence indicates that the World Bank has focused its efforts mainly on low-income countries. The increased lending provided to low-income countries through the International Development Association (IDA) to confront the effects of the pandemic surpassed that granted during the global financial crisis (a rise of 26% between 2008 and 2009, compared with 49% between 2019 and 2020). Conversely, the credit provided to middle-income countries through the International Bank for Reconstruction and Development (IBRD) rose by much more during the global financial crisis than in the current context (see figure 10).

Figure 10 | World Bank (including the International Bank for Reconstruction and Development and the International Development Association) and Inter-American Development Bank: growth in credit provided during the global financial crisis (2008–2009) and during the COVID-19 pandemic (Percentages)



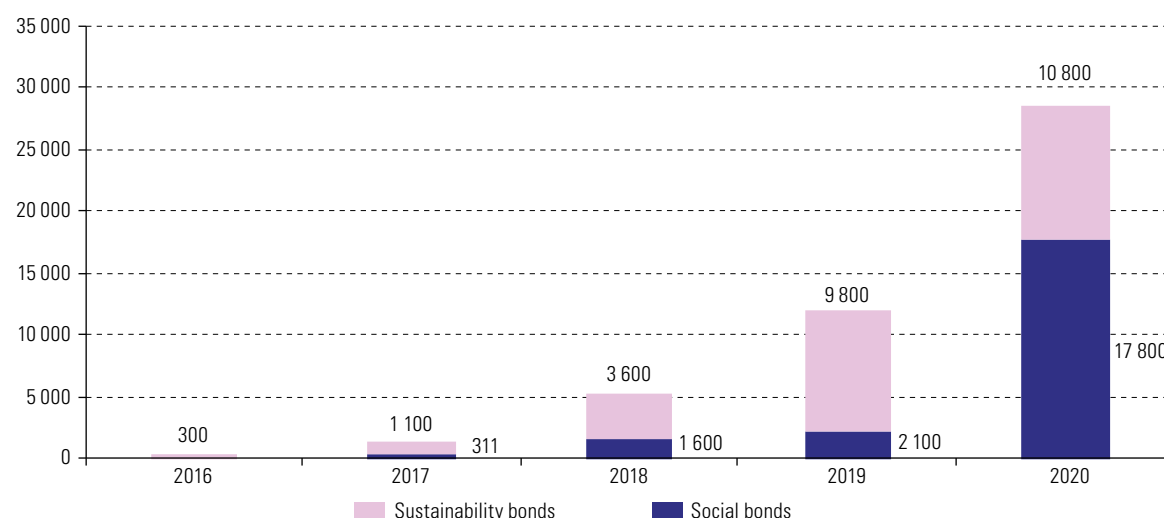
Source: C. Humphrey and A. Prizzon, "Scaling up multilateral bank finance for the Covid-19 recovery", *ODI Insight*, 18 November 2020 [online] <https://www.odi.org/blogs/17570-scaling-multilateral-bank-finance-covid-19-recovery#review-of-mdbs>.

- Development banks can also contribute to the recovery by shifting their lending priorities from the immediate response to the crisis, as emergency needs are met, towards medium- and longer-term development goals. Increased financing should be accompanied by changes in the composition of lending portfolios.
- Mandates of development banks should require channelling a significant percentage of portfolio loans to green investment and climate-change-related projects. Articulating a coherent strategy for the development banking system towards green finance requires the support of multilateral development banks towards subregional and national development banks in order to access low-cost funding, long-term capital, and technical capacity to access funds and design projects.

- The international community can support building back better by removing barriers to environmental technology access, fostering innovations through the expansion of compulsory licensing practices in developing countries, enhancing enforcement of competition law; and putting forth a new global development declaration (along the lines of the Doha Declaration) for intellectual property rights and climate change. It is also important to develop a voluntary environmental patent pool and enforce climate finance commitments to help developing countries, as envisaged in the Paris Agreement. In the same vein, the creation of employment and job programmes can be linked to the development of the green economy.
- Greater focus on the green economy can be linked to emergency job programmes based on ecosystems restoration and stimulus to use nature-based solutions (NBS) through the protection, restoration or management of natural forests and wetlands in watersheds to maintain a protective barrier for coastal communities against flooding; the creation of a major programme to pay for the unemployed or vulnerable communities to restore landscapes; and urban revegetation as well as urban agriculture and nature-based tourism. In the same vein, Official Development Assistance (ODA) flows—which should be provided on the basis of criteria other than per capita GDP—should be allocated in the main (at least in 50% of the total) towards the transformation of the productive matrix (renewable energy) and the accumulation of human capital (education).³⁹
- Building a more environmentally sustainable development model with improved social benefits can be facilitated by the growing interests of private financial markets in social and sustainable bonds issued in emerging market economies.⁴⁰ Available data from 2016 to 2020 show that social bond issuances have increased from US\$ 0 to US\$ 17 billion and sustainable bond issuances from US\$ 300 million to US\$ 10.9 billion (see figure 11). Within the Latin American and Caribbean region, Chile and Mexico are two of the countries that have taken advantage of the existing investor sentiment to issue sustainability-linked bonds.⁴¹

Figure 11 | Social and sustainable bond issues in emerging market economies, 2016–2020

(Millions of dollars)



Source: D.C. Mutua, “Chile Sells Biggest Latin American Sovereign Sustainability Bond”, Bloomberg, 20 January 2021 [online] <https://www.bloomberg.com/news/articles/2021-01-20/chile-sells-biggest-latin-american-sovereign-sustainability-bond>.

³⁹ The available evidence for countries in Latin America and the Caribbean that have graduated from ODA, including Barbados, Chile, Trinidad and Tobago and Uruguay, show that in the years preceding the graduation process the bulk of ODA flows were channelled towards education and renewable energy (ECLAC, 2020d).

⁴⁰ Social bonds are bond issues for projects designed to have a positive social impact. Examples include affordable housing, affordable infrastructure and community development. Sustainability bonds are bond issues to finance new and existing projects designed to have a positive environmental impact. Examples include projects connected to renewable energy, clean transport, energy efficiency, water/waste management and green buildings. They also include the financing of health-related projects (Mutua, 2021).

⁴¹ In 2020 The Federal Government of Mexico issued a seven-year sovereign SDG bond for US\$ 890 million. The bond prioritizes vulnerable populations and includes a governance criterion linked to the involvement of a United Nations organization. For its part, Chile has issued the biggest sustainability bond by a Latin American government in foreign debt markets. The issue includes sustainability bonds for US\$ 1.5 billion and €1.65 billion (US\$ 2 billion) in European markets to fund green and social projects.

3. At the subregional level, resilience-building can be implemented through initiatives such as the Caribbean Resilience Fund

- The Caribbean Resilience Fund (CRF) will function to attract large-scale, low-cost finance to address investment in green sectors, debt reduction through debt-for-climate-adaptation swaps, and support investment in resilience-building projects.
- It would use its funds to finance green industrial policy initiatives, infrastructure, and resilience-building in general, which in Caribbean SIDS, as in other parts of the Latin American and Caribbean region, should be a crucial component for recovery efforts and an opportunity for diversification and job creation. Apart from attracting concessional and other sources of financing, CRF would be financed through a debt reduction representing 12.2% of total public debt of the Caribbean SIDS, amounting to only US\$ 7 billion.

H. The current crisis should be seized as an opportunity to reach wide social and political consensus to implement ambitious reforms in order to engage in a sustainable and egalitarian building forward process

- Building forward better means putting equality and environmental sustainability at the centre of the recovery phase.
- This includes high quality universal public services—including education, health, transport and environmental services—and widening access to them, thereby increasing the population's sense of belonging and reducing the gaps in well-being, which have driven social and political unrest in many countries, already prior to the pandemic.
- Confronting and overcoming the effects of the pandemic in its different dimensions does not depend on its financial requirements, which are modest by any standard, especially in comparison with the scale of the stimulus packages introduced in developed economies, which benefit from comparatively lower borrowing costs and larger fiscal space.⁴² It resides in part in the recognition that the only way to respond to the urgency and the medium- and long-term challenges of a systemic crisis, such as COVID-19, is through collective action and solidarity.
- Collective action requires external multilateral cooperation, including the expansion and redistribution of liquidity, and a reform of the multilateral debt architecture, allowing countries to address their financial obligations and pursue expansionary fiscal policies without hindering their future development.
- The policy orientation of the countries of Latin America and the Caribbean is also central for building forward better. The countries can increase their policy space by eradicating tax avoidance and tax evasion, and by placing the weight of taxation on direct taxation, property and wealth taxes. They can also reorient public expenditure towards employment creation and transformative and environmentally sustainable activities. To this end, public expenditure should prioritize public investment, basic income, universal social protection, support for small and medium-sized firms (SMEs), digital inclusion and the development of green technologies.

⁴² The fiscal and monetary stimulus packages, implemented predominantly in developed countries, are estimated at US\$ 12 trillion and US\$ 7.5 trillion, respectively.

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