Financing a Green New Deal and Sustainable Development Goals on a Global Basis: Is Blended Finance a Feasible Option?

Gary Dymski, Maria Gavris, Penelope Hawkins, and Gissell Huaccha*

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ABSTRACT

Because planetary warming is global in scope, Green New Deal (GND) efforts must be undertaken across the globe. However, most countries lack the budgetary capacity and/or access to financial markets to undertake GND programmes on their own. Further, a disproportionate number of the households in countries in this category fall below the thresholds identified in the United Nations' sustainable development goals (SDGs). Any credible effort to undertake GND investments must therefore simultaneously involve efforts to meet – and thus finance – the SDGs. Not to link them would constitute a declaration that it is the carbon footprint of these nations that merits inclusion in a planetary rescue operation, not their human residents: it would violate even a low-bar human rights standard. This paper takes up the following question: how can a Global Green New Deal and SDG efforts be financed for countries unable to meet SDG standards with their own resources, given the evolution and current status of the global financial system? We first evaluate the 'blended-finance' proposal proposed in mid-2018 by the G-20, then turn to the expanded policy debate that has followed the arrival of the global COVID-19 pandemic, to consider how the needed global finance might emerge.

Keywords: blended finance, climate change, Green New Deal, Sustainable Development Goals (SDGs), United Nations, global financial system

JEL Codes: F33, F38, G23, 015, 023, Q01, Q32

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1. Introduction

The promise of a 'Green New Deal' (GND) is to expand employment via new investment projects that both decrease inequality and reduce carbon consumption, thus inducing a shift to sustainable ecological/economic systems. GND proposals have been most visible in more prosperous countries located at or near the top of the global currency hierarchy. These nations can largely use conventional policy tools to finance their GND efforts.

But the global nature of planetary warming implies that Green New Deal efforts must be undertaken across the globe. This immediately brings in two crucial considerations. First, most countries lack the budgetary capacity and/or access to financial markets to undertake GND programmes on their own. In countries that fall into this category, a disproportionate number of households do not meet the thresholds identified in the United Nations' sustainable development goals (SDGs). This means that, in these countries, any credible effort to undertake GND investments must simultaneously involve efforts to meet – and thus finance – the SDGs (note that there is significant overlap, since the SDGs include environmental goals). Not to link these two global aspirations would be to declare to residents of lower-income nations that it is their carbon footprint that merits inclusion in a planetary rescue operation, not the human beings and communities located within their borders. Given that United Nations support will be needed for any such global initiative, such an approach is not feasible – it would not survive a 'consensus' vote in the UN General Assembly – and more to the point, a violation of even a low-bar human rights standard. This paper takes up the following question: how can a Global Green New Deal, accompanied by a significant effort to meet SDGs in countries with significant portions of their populations who fall below them, be financed? This paper takes up this question, focusing on the 'blended-finance' proposal put 'on the table' by an experts panel of the G-20 in mid-2018. So is that proposal fit for purpose? If not, why not? And if something more is needed, where should we look for supplemental financing mechanisms?

This paper has been written after the COVID-19 pandemic arrived in force globally in 2020. The pandemic highlighted the centrality of human well-being in global sustainability efforts. It dramatically exposed the uneven spread of this virus, the differential response capacity and policy measures undertaken across the globe, and of course had a dramatic and uneven impact not only on global health and mortality, but also on economic activity, including national income levels and cross-border financial flows. Since the premise of this paper is that the capacity to fund a GND and the SDGs differs substantially across the globe, it's clear that the COVID-19 pandemic has dramatically altered the locus and depth of the shortfalls in available GND/SDG financing capacity in that nations already in a pre-COVID deficit position. At the same time, so disruptive has COVID-19 been to economies and global policy discussion that no revised set of estimates on how the pandemic has changed the pre-COVID-19 funding need has been developed. This will be handled by incorporating a section on the likely consequences of COVID-19 for the pre-pandemic parameters at the end of this paper. This somewhat disjoint method of connecting these longer-term pre-COVID-19 goals with the pandemic global emergency, while arbitrary, has the virtue of allowing an analysis of the feasibility of the pre-COVID blended-finance proposal before approaching the question of the further challenges posed after the pandemic's consequences have been realized. This will lead us into the further proposal that has come forth post-COVID-19: the idea of using Special Drawing Rights (SDRs), now administered by the International Monetary Fund, as a further monetary instrument for meeting global needs.

This paper proceeds as follows. Section 2 sets out the relevant policy context: it briefly describes the recent (pre-COVID-19) global commitments made regarding climate change and the sustainable development goals, and then summarizes the G-20 expert panel proposal to use blended finance to fund these commitments. Sections 3 to 5 then introduce the historical and institutional evolution of the global financial system into which these blended finance instruments would be introduced. Section 3 traces the origins of global financialization in its current form to developments in the US, and shows how these developments gave rise to a global financial dynamic that swept up many advanced countries, as well as a number of more market-oriented developing countries. Section 4 shows how this dynamic has brought about a period of international financial integration, a period shaped by the historically-specific role of the US and of the period of widespread financial deregulation that has characterized the post-1980 (neoliberal) period; Section 5 recounts how this system collapsed into crisis and remains financially fragile. Section 6 then turns to the blended-finance proposal put forth in 2018, analyzing its strengths and weaknesses in light of the recent trajectory of financial system development and crisis summarized above. Section 7 discusses the possible impact of the COVID-19 pandemic on both the extent of funding needed and on the blended-finance proposal as a means of raising the necessary finance. The possibility of using SDRs, now under the oversight of the IMF, as an alternative financing mechanism, is then considered. Section 8 concludes with a brief discussion of alternative approaches to generating the finance needed to bring about a more socially and ecologically sustainable world.

2. The 2015 Addis Ababa Action Agenda and the 2015 Paris Accords: Setting global goals

The United Nations' Addis Ababa Action Agenda (agreed in July 2015), set these Financing for Development (that is, SDG) goals for three dimensions of sustainable development: 'promoting inclusive economic growth, protecting the environment, and promoting social inclusion'. The same year saw the opening in Paris of negotiations on an international treaty on climate change. By April 2016, 191 nation-state members of the United Nations Framework Convention on Climate Change (UNFCCC) ratified the agreement.[1] The same month, these 'Paris Accords' set carbon targets linked to participating nations' financing commitments.

These two agreements arguably mark a turning point in defining both human responsibility for the planet and all its people and the necessary extent of intended action. The urgency built into these agreements reflect the awareness of governments and of people globally that our anthropocentric systems are failing. Human activity, burning through the planet's carbon budget, has put the preconditions for stable biological reproduction of ecosystems of living organisms at risk; and human societies have failed to insure a global right for every person to develop their faculties and capabilities and to flourish during their lifespan.

A huge funding gap must be filled if targets set for the SDGs in Addis Ababa and for the 2015 Paris Accords on carbon targets are to be met. Experts at the United Nations Conference on Trade and Development have estimated that approximately $ 2.5 trillion (US dollars) will be needed annually to meet the SDGs.[2] This figure is feasible in principle: it represents 3% of the global GDP figure of $93

[1] The United States, a signatory to the 2016 agreement, withdrew in 2020 and then subsequently rejoined in 2021.

[2] Note that one of the 17 sustainable development goals – SDG 13, climate action – directly mandates policies to reduce global warming. In addition, fulfilling several other SDGs by meeting the conditions they specify will necessitate effective and sustainable action to reduce global warming: SDG 6, clean water and sanitation; SDG 7, affordable and clean energy; SDG 11, sustainable cities and communities; SDG 12, responsible consumption and production; SDG 14, life

trillion.[3] The overall size of global capital and financial markets, while fluctuating widely over time, has been estimated as encompassing similar orders of magnitude. In 2005, McKinsey and Company estimated the size of global capital markets at $118 trillion; and the Financial Stability Board has recently estimated a narrow measure of the size of the shadow banking system at $45 trillion, a broader measure at $99 trillion, and the overall global financial system at $330 trillion. The question is, how can it be done?

In October 2018, an eminent experts group of the G-20 proposed a solution: blended finance. Blended finance leverages risk-absorbing public funds to attract private capital: the idea is that the private sector creates the needed credit and securitizes it, while sovereign nations and multilateral development banks underwrite the resulting risk.

Blended finance is attracting huge amounts of attention as a possible means of augmenting the shortfall in available finance. It's a way of leveraging available public funds at the national level by attracting pools of private capital. With the global slowdown in private investment, there should be supply to meet what would be a robust demand.

The sum of blended finance initiatives have thus far raised less than $200 billion. THis is far short of the funding needed. It immediately brings to mind the shortfall in ODA – overseas development assistance – globally: the level of funds committed is far too little, and much of that money gets spent in the home country, or 'counted' as ODA when other purposes are served. When it is then considered that there is an overall transfer of resources from the emerging market and developing markets, then it's clear that blended finance hasn't yet filled the required funding gap.

An immediate concern is that a functioning blended-finance system will depend on securitization – the bundling of individual project loans into vehicles that can be bought by financial funds. Thus far, somewhere between $26 billion and $52 billion of blended-finance instruments have been securitized successfully. According to the *BIS Quarterly Review* (2017), $420 billion was issued in dollar-denominated debt to non-financial borrowers in 2017. These are substantial figures, but they fall well short of UNCTAD's $2.5 trillion figure.

Understanding the implications of setting a $2.5 trillion funding initiative in motion via the instruments and mechanisms available in the global system – banks, megabanks, investment and pension funds, shadow banks, and securitization processes – or via innovations in this system, requires a deep dive into its development and recent history. For while this system has grown at rates far exceeding those of global national income, it has also plunged the world into regional and globe-spanning financial crises with devastating consequences for people and places across the globe. The next three sections undertake this deep-dive analysis; section 6 then summarizes the 2018 G-20 plan for blended finance into context.

3. The emergence of a global financial dynamic: deregulation and banking transformation

Financial institutions and practices underwent rapid change in the 1980s after a deteriorating macro environment in the 1970s put the heavily-regulated banking systems of advanced nations in jeopardy. High rates of price inflation in the 1970s led to high interest rates, which led to balance-sheet stress

below water; and SDG 15, life on land. Arguably, a global commitment to achieving all of the SDGs would result in actions sufficient to both mitigate momentum toward global warming and to permit adaptation to climactic changes already in motion.

[33] Unless indicated otherwise, all dollar ($) figures included herein refer to nominal United States dollars.

in the heavily-regulated commercial banking and thrift systems of the United States. Banks were losing traditional blue-chip loan customers and high-balance depositors to direct credit markets and mutual funds. Large banks expanded their lending abroad to replace lost domestic customers.

Deregulation began in earnest with the passage of the Deposit Institutions Deregulation and Monetary Control Act of 1980 in the United States, the initiation of an extended period of bank consolidation in the 1980s and 1990s, and a shift toward market-based finance. The basis of mortgage finance shifted from dedicated local circuits of capital, based on pooled savings, to securities purchased and underwritten by quasi-public agencies sold into the broader markets, including to foreign wealth-holders.

During the 1980s and 1990s, financial markets grew grown continually in scale and scope. Private underwriters stepped into credit markets and more buyers of non-bank credit emerged, expanding the range of contracts that could be securitized. The expanding set of spot and contingent contracts facilitated both cross-border lending and the transfer and hedging of credit and exchange risks. Consequently, bank-based, originate-to-hold lending was gradually replaced by market-based, originate-to-distribute lending; securitization and the ‘shadow banking’ industry supporting it grew steadily, its liquidity enhanced by an expanding complex of clearinghouses, exchanges, and broker-dealer firms.

The global financial dynamic. Since the 1980s, international financial markets’ evolution has unfolded according to a global dynamic defined by two elements: first, a restructuring of global banking, originating in the US and spreading through most advanced economies; second, the asymmetric current- and capital-account position of the US from the 1980s onward. These two elements emerged in the context of another trend not investigated here – an increase in multinational firms’ offshore production facilities in lower-cost regions.

In the United States, money-center banks were at particular risk as regulated banking disintegrated in the late 1970s: they lost depositors to money-market mutual funds and ‘blue chip’ customers to direct credit markets. To compensate, they turned to borrowed funds and to borrowers in less developed countries, especially in Latin America.[4] Similar pressures led to banking deregulation in other advanced nations, and to these nations’ expansion into overseas lending in this period. When high and volatile interest rates and a decline in commodity prices led to systematic defaults by Latin American borrowers, a serious debt crisis arose. Given the balance-sheet fragility of US money-center banks, the US Comptroller of the Currency declared these banks ‘too big to fail.’ Again, while not so explicitly declared, other nations also took steps – then or later – to protect their largest banks.

In the 1990s, these same factors – in particular, the exhaustion of traditional loan markets and competition for size and market share among large and increasingly deregulated banks, in the US and in Europe in particular, led to repetitions of overseas lending excesses – notably East Asia. Recurrent financial crises became a defining feature of the post-1980 global economy.[5] The opening of new lending markets for globally-active banks, along with post-crisis adjustment programs typically orchestrated by the International Monetary Fund (IMF), led to increased entry by foreign banks into developing-economy markets. Frequent crises and post-crisis adjustment programs, in turn, led to an

[4] It is important to recognize that lending to Latin American borrowers was only one cause of the extended crisis of advanced-economies’ banking systems in the 1980s. See, for example, the *History of the Eighties: Lessons for the* Future, Federal Deposit Insurance Corporation (FDIC), Washington DC, 1997.
[5] Luc Laeven and Fabián Valencia, “Systemic Banking Crises Database: An Update,” IMF Working Paper WP/12/163, Washington DC: International Monetary Fund, June 2012.

erosion in (if not the disappearance of) development banking capacity in many countries. State planning and developmental institutions were also dismantled.

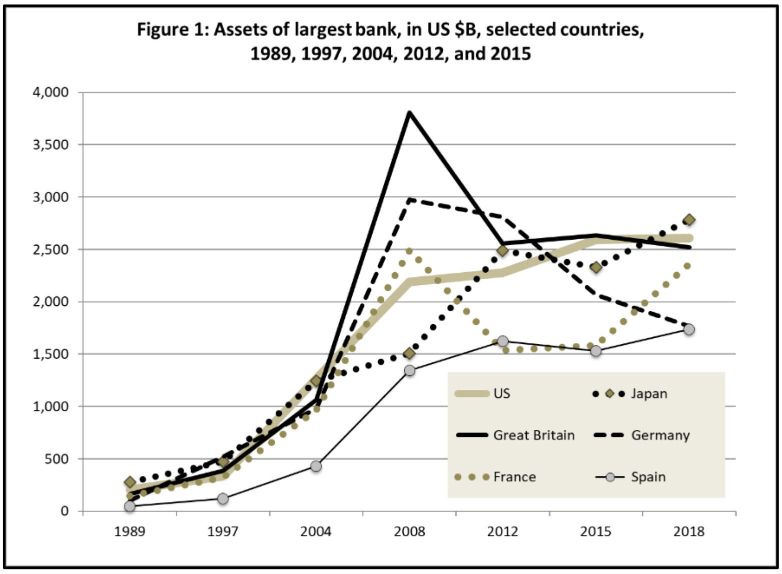


Figure 1: Assets of largest bank, in US $B, selected countries, 1989, 1997, 2004, 2012, and 2015

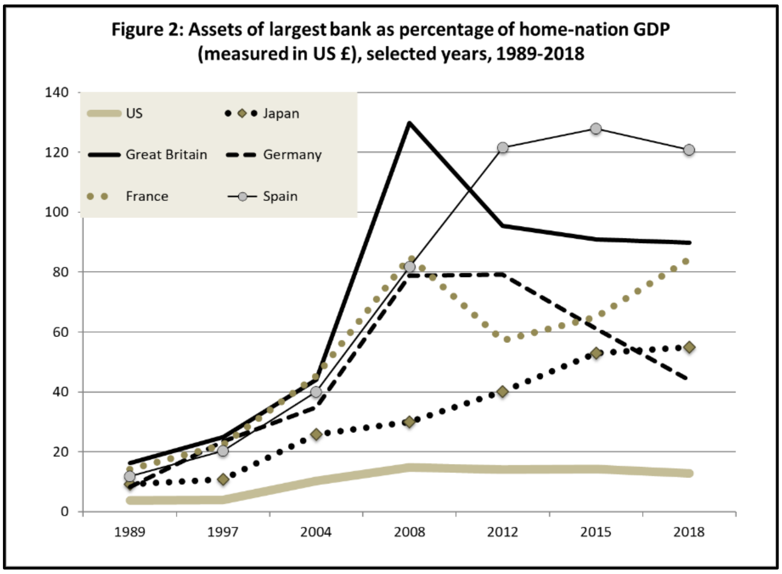


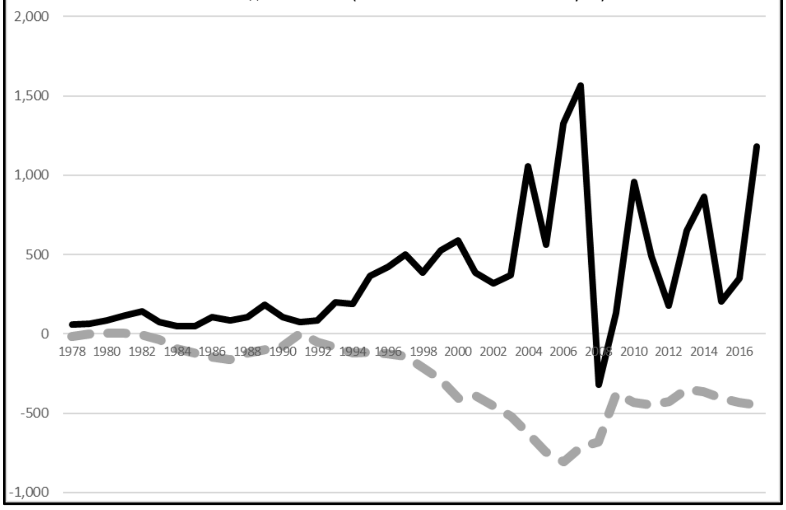
Figure 2: Assets of largest bank as percentage of home-nation GDP (measured in US £), selected years, 1989-2018

Against the backdrop of increasingly frequent financial crises, especially in emerging economies, constraints on financial flows were continually removed in these years. The Delors Commission report of 1989, which led to the European Union's single market, called for "the full liberalization of capital movements and financial market integration." European governments' preparations for the single market included the use of bank mergers to create national banking champions. In turn, the US repealed its Depression-era Glass-Steagall Act in 1999, opening the way to fully deregulated activities by financial conglomerates.

These changes in legal constraints, together with the rapid spread securitization, facilitated the growth of the large banks that, together with growing networks of non-bank banks, dominated the 'originate-to-distribute' markets. Consequently, the explosive growth of securitization was paralleled by that of non-bank lenders, debt, and the large global banks that dominated these markets. The largest banks in advanced economies grew at accelerated rates from the late 1980s into the 2000s, as Figure 1 demonstrates. Figure 2 makes the further point that the asset size of these nations' largest banks came to exceed that of their home-nations' GDP in the years leading up to the global crisis (several years between 1989 to 2008 are shown in these figures).

Initially, the growing numbers of non-banks providing customers for bundled, securitized credit, together with the surge in the supply of credit provided for home purchase and refinancing, for commercial real-estate development, and other purposes, led to great confidence that financial-market efficiency had reached a new plateau. Worries were expressed about the opacity that characterized the instruments being brokered by the 'passive financial intermediaries' at the heart of this new financial system.[6] But the willingness of credit-rating agencies to certify a large volume of securities as investment-grade, and the reliance of the revised Basel Accords on large banks' own assessment of their risk exposure, led to these worries being set aside.

Figure 3: US Current Account Balance and Net Financial Assets Acquired, USB$, 1978-2017 (US Bureau of Economic Analysis)



By 2007, a downturn in US housing prices, the increasingly precarious financing positions of borrowers, and the interconnections among the global systematically-important banks all combined to trigger an implosion of global financial assets and equity prices, launching what Tooze has termed a 'decade of financial crises.'[7] As Tooze has pointed out, the extent and depth of this crisis – which ranged across the US and Europe, and profoundly affected every region of the world – starkly demonstrated the deep integration of the global financial system. Thanks to the measures taken by governments, central banks, and international agencies around the world, this system largely survived intact, and global depression was averted.

[6] The term in quotations appears in Oldfield, George S. "Making Markets for Structured Mortgage Derivatives," *Journal of Financial Economics* 57 (2000) 445-471. To see the doubts about how to characterize the risk and other characteristics of securitized debt that emerged even as this new system of market-based lending was gathering momentum, compare the working paper and published versions of this paper by Fender and Mitchell: Ingo Fender and Janet Mitchell, "Risk, Complexity, and the Use of Ratings in Structured Finance," working paper, Bank for International Settlements and National Bank of Belgium, March 2005; and Fender and Mitchell, "Structured Finance: Complexity, Risk and the Use of Ratings," *BIS Quarterly Review*, June 2005, 67-87.

[7] Adam Tooze, *Crashed: How a Decade of Financial Crises Changed the World*. London: Allen Lane, 2018.

The second factor facilitating this global financial dynamic was the emergence of a systematic US current-account deficit and capital account surplus. This situation can be traced in part to a shift of US companies toward outsourced and global factory-based production, as well as to the emergence of competitive producers elsewhere in the world. Macroeconomic accounting can readily be used to show that these two imbalances are systematically connected for any economy. Figure 3 illustrates the persistent US current account deficit, and net capital inflows from the early 1980s to the present.

This persistent structural imbalance has global consequences. An immediate consequence is that there has been, through these years, a steady inflow of money into the US looking for assets to buy. A further consequence is that the US has been systematically exporting the ownership of its liabilities – T-bills and T-bonds are held in reserve portfolios the world over. These in turn, once obtained, become ‘safe assets’ that provide both security against speculative financial attacks and also high-quality collateral in the event of the need for further borrowing. The tremendous growth of global reserves reflects both the importance of protections against speculative attacks and also the growth in the size and intensity of these attacks – the possibility of ‘sudden stops.’

The interplay of these two structural factors since the 1980s has been underscored by the asymmetric treatment of the ultimate lenders and borrowers in the episodes of deep financial distress on both ends of this historical epoch – the early-1980s’ Latin American financial crisis and the late-2000s’ subprime meltdown. While large US banks (and other adanced-nations’ lenders) survived the Latin American default of 1982 relatively unscathed, borrower nations experienced a ‘lost decade’ with diminished economic growth; their debts were not forgiven, but were consolidated into Brady bonds on which payments were made into the 2000s.[8] This asymmetry of outcomes – in which debts taken on initially by private parties are converted into the sovereign-debt obligations of developing nations, while lenders’ losses are mitigated – foreshadowed the treatment of bad debt in the subprime crisis.[9]

4. International financial integration

Developing countries’ vulnerabilities are not due to their failure to organize themselves and to create policy space for themselves; they are bound within the constraints imposed by a world whose policy parameters are shaped by unregulated international financial markets. And while too-big-to-fail megabanks are protected by national governments, they are unaccountable and part of a financial megaplex that protects its flexibility.

The result has been global financialization and a ‘business of debt’ that permeates the activities of households and firms. Throughout the world, falling wages for workers, and the loss of development-banking capacity to support enterprise, has made increased debt a necessity for a larger and larger share of economic units. Complementing this ‘demand’ is the rise of market-based

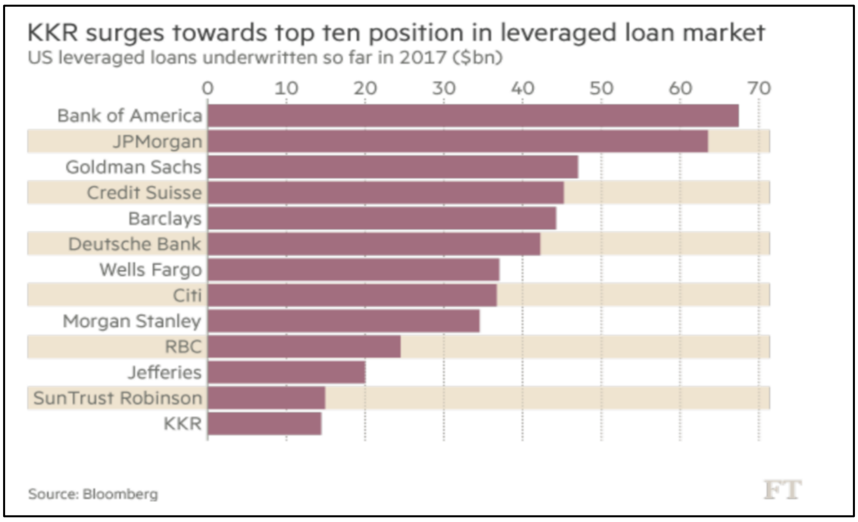
[8] The Brady bond process continued into the 1990s and was used to restructure the debt of nations outside Latin America; by 1999, $130 billion of Brady bond debt was outstanding. Mexico retired its last Brady bond in 2003, Brazil in 2005.

[9] In the US, the Emergency Economic Stabilization Act of 2008 authorized the Troubled Asset Relief Program to provide support for affected banks and for homeowners with ‘underwater’ mortgages. Just over half of the $205 billion authorized for capital support for banks, $115 billion, was paid out to 8 large banks in October 2008. Some $50 billion was set aside for homeowner relief; as of 2016, only $27 billion had been paid out. According to the US Treasury Department, approximately 1.5 million homeowners received some form of mortgage modification under federal and state programs. An estimated 12 million homes were foreclosed due to the subprime crisis; one in every 12 US homeowners having initiated foreclosure proceedings after 2007, with minority homeowners and neighborhoods being disproportionately impacted (Matthew Hall, Kyle Crowder, and Amy Sprint, ‘Neighborhood Foreclosures, Racial/Ethnic Transitions, and Residential Segregation,’ *American Sociological Review* 80(3), 2015: 526-49.

lending. This has created a set of instruments that can be sold to customers who are risky, for reasons unrelated to 'productive use', backstopped by national governments that have largely immunized the investor/lender sector against loss.

As noted in Section 1 above, the integrated system of global finance that matured in the early 2000s generated an unpayable excess of debt by 2007, leading to a global financial crisis in 2008. IMF staff attempted both to construct a database of the last four decade's financial crises and to assess their cost. For example, Laeven and Valencia (2010) estimated banking crises in the 1970-2006 period had cost output losses of 33 percent of GDP; and the 2007-2009 crisis had cost a further 25 percent; these authors calculated that emerging markets had lost 29 percent of GDP to 1970-2006 crises, and only 5 percent to the 2007-09 crisis.[10] A significant 2015 IMF study found that the countries most exposed to risk of loss from future financial crises are those with large banking-asset/GDP ratios and/or with high debt levels.[11]

Figure 4: US leveraged loans underwritten in 2017 as of mid-year
Source: see footnote 8



In the post-crisis period, some of the megabanks at the heart of global finance have shrunk, either in absolute terms or relative to GDP, but others have continued to grow, or have resumed their growth; The depictions of the largest banks' sizes in six advanced economies, shown in Figures 1 and 2 for the post-crisis years of 2012, 2015, and 2018 provide an illustration of this mixed post-crisis experience. Even where shrinkage has occurred, these large banks' excessive size relative to their home economies implies that they must grow faster than those economies, *ceteris paribus*, to avoid declining rates of return.

As in the 1980s and 1990s, this means developing new instruments in their home markets, and by looking again to grow their position in emerging market economies. On the home-economy front, in both the US and Europe, the latest area of innovative and possibly risky growth is the largely unregulated $2 trillion leveraged loan market. Figure 4 illustrates that many of the same banks that

[10] Luc Laeven and Fabian Valencia, 'Resolution of Banking Crises: The Good, the Bad, and the Ugly,' *IMF Working Paper* WP/10/44. Washington, DC: International Monetary Fund, August 2010. Tooze (2018), referenced in footnote 6, notes that emerging economies, as well as European Monetary Union countries, felt the brunt of the crisis that began in 2007 only after 2009.
[11] David Amaglobeli, Nicolas End, Mariusz Jarmuzek, and Geremia Palomba, 'From Systemic Banking Crises to Fiscal Costs: Risk Factors,' *IMF Working Paper WP/15/166.* Prepared by

were active in subprime lending and securitization are dominant in US leveraged lending as well.[12] Other areas of domestic megabank expansion include the resumption of subprime lending, the entry of at least one megabank into the payday lending market, and the rapid expansion of the automobile and student debt markets.

Figure 5: Cross-border flows reported by the Bank for International Settlements - Percentage by global final-market areas, 1990-2015

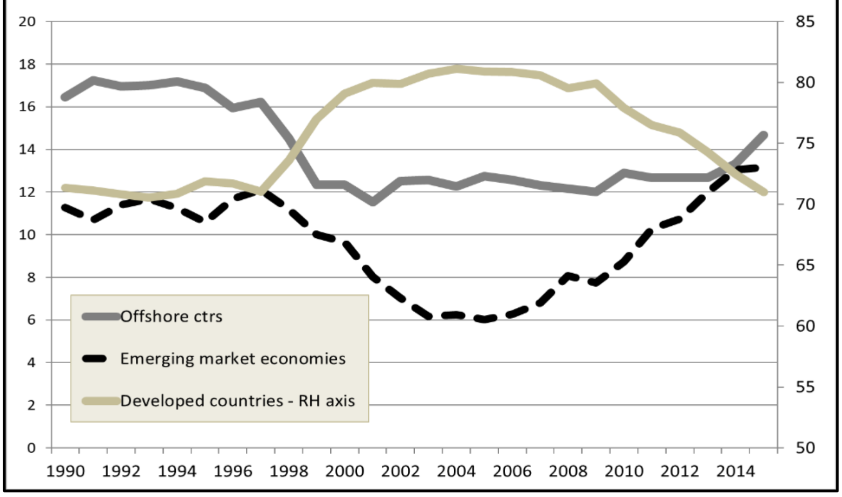
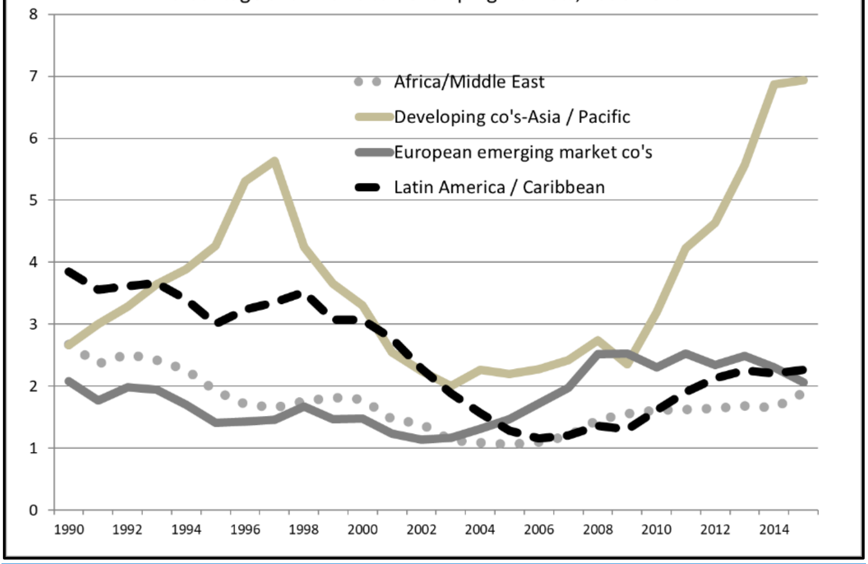
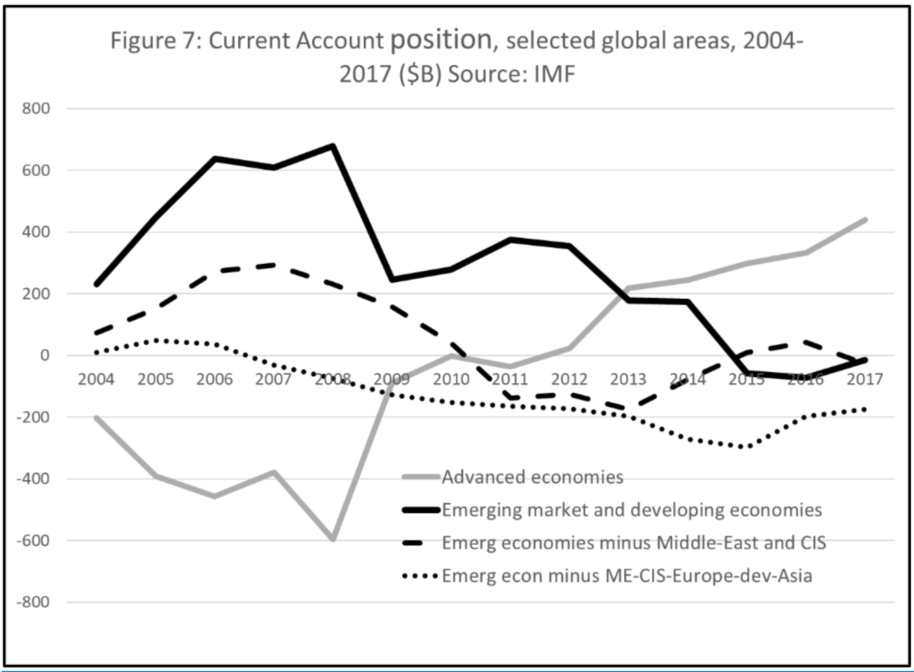


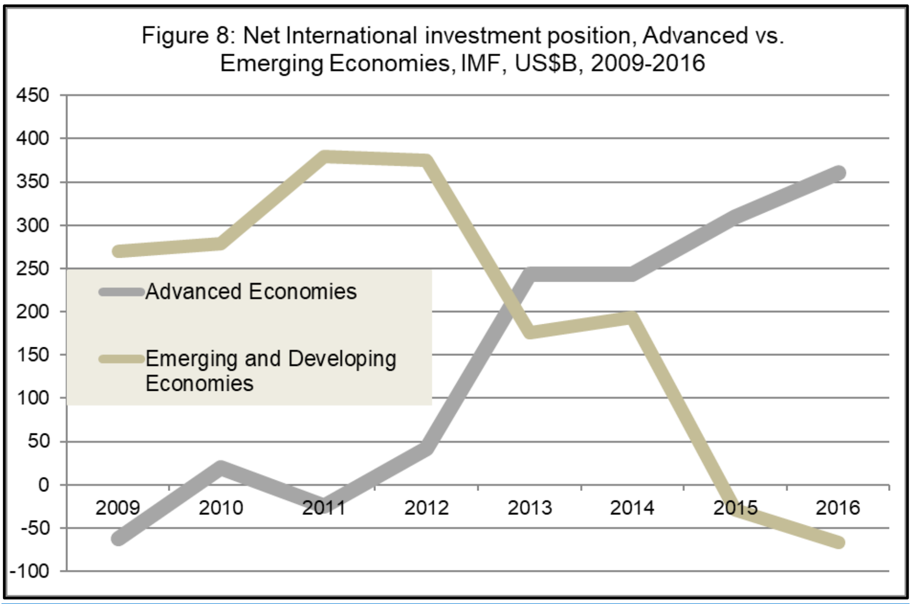
Figure 6: Cross-border flows reported by the Bank for International Settlements - Percentage of all flows to developing markets, 1990-2015



Lending to borrowers in emerging-market economies has also gathered force in the post-crisis period. Figure 5 shows that cross-border lending flows as reported by the Bank for International Settlements (BIS) have shifted away from advanced economies and toward emerging markets. Figure 6 provides some detail on lending to different sub-areas within the emerging-market cluster; it shows that emerging Asia has accounted for virtually all of this percentage increase, with cross-border flows to Africa, Latin America and the Caribbean, and emerging Europe closely bunched.

[12] See Eric Platt, 'KKR muscles into US leveraged loan business,' *Financial Times* 20 June 2017. Figure 4 appears in this source.





This shift of this global lending flows toward emerging markets should be seen in light of broader cross-border macroeconomic imbalances, as discussed above. And Figures 7 and 8 demonstrate that the aggregate structural position of advanced and emerging-market economies has indeed been shifting in the post-crisis period. Figure 7 shows that whereas emerging-market economies, taken as a whole, held a surplus current account position prior to the crisis, offset by advanced economies' deficit position, that relationship has steadily been reversed in the post-crisis period. The developed economies – many vigorously pursuing austerity policies, as Tooze (2018) has demonstrated – now are in surplus, while emerging markets are in an aggregate deficit position. Figure 7 successively removes Middle-East and the CIS countries, and then emerging Asia; but the pattern persists even when Latin America and Africa constitute the bulk of the emerging-market group.

This pattern is reinforced by BIS data on net international investment position, as shown in Figure 8: between 2009 and 2016, the advanced economies have shifted from a net debtor to a net creditor position, while the opposite has occurred for developing economies.

The global patterns shown in Figure 7 and 8 demonstrate that developing countries' vulnerabilities cannot be attributed solely to their governments' failure to be sufficiently disciplined: these countries are operating within the structural parameters of a world system in which much larger nations (in terms of GDP size) have been systematically pursuing austerity policies whilst providing a backstop for the megabanking sectors whose very size mandated the implementation of (declared or undeclared) too-big-to-fail policies. That these megabanks and the shadow-banking system that surrounds them were chastened and made to reinforce their capital buffers post-crisis does not change the fact that the extraction of rentier income by hyperglobalized, inadequately regulated megabanks and megafirms in international financial markets is worsening global inequality and squeezing developing-economies' policy space still further.[13]

5. Asymmetric lender-of-last-resort capacity, unsustainable national provisioning and sustainable development

The asymmetric resolution of the decade of global financial crises has, then, increased global inequality and exposed the weak financial substructures on which the celebrated takeoff to post-2000 growth of various combinations of developing nations – first the 'BRICS', and then the 'MINT' countries – was based. Expectations that financial deepening would accelerate growth have been replaced by warnings of 'too much finance.'[14]

It is in this context that post-crisis concern about increasing corporate debt and debt servicing burdens, especially in developing countries, has arisen. Heightening this concern is the fact that these commitments are in many cases bundled into opaque instruments subject to legal frameworks largely controlled by financial centres, and exposed to volatile investor sentiments. The asymmetric power of global financial markets relative to national governments has led Rey (2013) to famously argue that monetary-policy independence has been largely eradicated, in a world driven by global financial cycles.[15] Developing economies provide bubble- and fad-driven venues that either accompany booms or provide investment outlets in busts.

Only one nation within this system has the capacity to be a global lender of last resort. It is precisely because of that capacity – linked to the 'exorbitant privilege' of the US – the government of the US has little incentive to rein in the arsenals of financial speculation. The US's central bank was able to rescue the increasingly risky system a decade ago. A second test of that capacity may not be feasible, for reasons explained by Tooze (2018) and made clear in an extended Brookings Institution interview with Ben Bernanke, Tim Geithner, and Henry Paulson: working through the pressurized choices during the global meltdown required close cooperation among private-sector and governmental principals, necessitated bending the letter of the law, and depended on close

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[13] See chapter 6 in the 2017 *Trade and Development Report*. Geneva: United Nations Conference on Trade and Development, 2017.

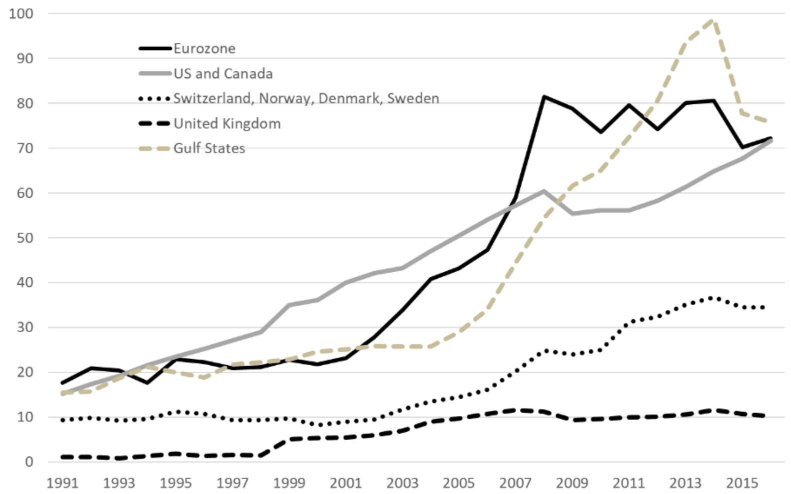
[14] Jean-Louis Arcand, Enrico Berkes and Ugo Panizza, 'Too Much Finance?' *IMF Working Paper WP/12/161*. Washington, DC: International Monetary Fund, June 2012.

[15] Hélène Rey, 'Dilemma not trilemma: The global financial cycle and monetary policy independence,' *Proceedings - Economic Policy Symposium - Jackson Hole.* Kansas City: Federal Reserve Bank of Kansas City, 2013. Pp. 285-334. Thomas Palley offers an alternative, complementary, explanation; see his 'A theory of Minsky super-cycles and financial crises,' *Contributions to Political Economy* 30(1), June 2011: 31-46.

cooperation with the executive leaderships of the US, UK and Europe.[16] Working relationships and trust among policy principals in the advanced nations have eroded in recent years, as has the policy space for the sort of unilateral actions needed to quell fast-developing crises.

The apparent resolution of the global financial crisis, celebrated at the aforesaid colloquoy, was followed since 2009 in the advanced economies by austerity policy; after a lag, austerity policy was adopted almost universally in the developing nations, China being the outstanding exception. The resulting pattern of global austerity, urged by financial-market analysts and finance theorists as a way to increase the global stock of 'safe assets', has steadily compromised the capacity of sovereign nations to provide for the welfare of their citizens. Austerity, which represents the consequence of not confronting the global financial crisis, affects developing countries as much as advanced nations.

FIgure 9: Outflow of Remittances for Selected Global Areas, 1991-2016
US$B (Source: World Bank remittance/migration data)



The long chain of events, then, from the spread of global finance, to recurrent financial crises, to their subordinate position in the global response to the global financial markets' extended meltdown in the past ten years, has drained many developing nations of the capacity to provision for their citizens.[17] The global increase of economic migration, and the concomitant rise in remittance payments, is a consequence of the breakdown of provisioning mechanisms in many developing nations. Remittances are now larger than all global cross-border flows apart from foreign direct investment; and much of their growth (and that of economic migration) has been occurring in nations in which social-democratic governments are under assault. Figure 9 sets out World Bank data for the regions with the highest levels of remittance outflows.

These structural dilemmas are coming to a head just when the need for global action to address global problems has become crystal clear. Recent years' setting of targets for sustainable development and for a response to climate change represent unprecedented levels of global cooperation. But achieving the sustainable development goals, and responding to climate change will

[16] 'Ten years after the financial crisis: Reflections by Bernanke, Geithner and Paulson,' video transcript edited by Jeffrey Cheng and David Wessel, recorded September 19, 2018 at the Brookings Institution, Washington, DC. See https://www.brookings.edu/blog/up-front/2018/09/19/reflections-by-bernanke-geithner-and-paulson/

[17] Of course, a series of non-financial factors could be sited here as well. The point made is simply that global financial structures, as these have evolved, experienced crises, and then been reconstructed in advanced economies, have crucial implications not just for developing economies' policy space but for the well-being of their citizens.

require in all likelihood investment flows and fiscal transfers from developed to developing nations. We need, for this purpose, financial instruments that are purpose-driven, and which are not exposed to financial speculation.

6. A blended finance solution in a world of post-crisis securitized shadow banking?[18]

Given that a global system for originating loans and bundling them into securities has been in operation for over 20 years – with lessons learned by global financial monitors such as the Bank for International Settlements, as well as advanced nations' central banks and prudential regulatory offices, a securitization-based solution to a new global funding need seems a logical way forward.

The opportunities and barriers to using private markets to provide infrastructure finance in developing economies were analyzed extensively by Tyson in 2018.[19] While Tyson's analysis did not focus specifically on blended finance – that is, on the de-risking of funding instruments through public or quasi-public underwriting, her analysis indicates that there are a sobering number of steps to be completed before a system of the kind anticipated in the G-20 experts' document would be up and running. Specifically, Tyson developed a checklist of what would be needed to, if they had not already done so, or repurposing existing models to focus on developing economies' needs. She pointed out that market-building, with a focus on early-stage financing and project development, would then have to be undertaken, across many such countries. She identifies these must-have steps:

1. Re-orientate international financial institutions (IFIs) to adopt 'originate-to-distribute' business models and to focus on project development.
2. Deliver more 'bankable' projects by scaling up successful project-preparation facilities and by developing capacity for 'state-of-the-art' national infrastructure planning and execution.
3. Develop syndication and securitisation, using 'mega-funds' as a key financing model to crowd in institutional investors.
4. Deliver affordable, more flexible and longer-tenure foreign exchange (FX) and political risk hedging by scaling up existing successful IFI seed-funded providers.
5. Deepen pension and life-insurance markets in domestic economies to deliver local currency financing of infrastructure.

We might note, in light of previous sections' discussion, that items 3-5 of this list were undertaken, more or less successfully, in building the global market for global subprime-mortgage securities. As such, these steps would involve repurposing securitization mechanisms and markets for these funding purposes. However, her first two steps are not about re-purposing: each would require revolutionary changes in the operation of global finance. Her first step involves turning the IMF and World Bank – perhaps especially the latter – from lenders into underwriters. This list could be extended to include other multinational development banks, such as the Inter-American Development Bank or even the European Investment Bank. In some cases, underwriting and risk-sharing activities are underway at these institutions; but what is intended here is a functional separation: the IFIs would partner with developing countries to create 'bankable' projects, and then

[18] A section 7 on the COVID-19 pandemic and the IMF's release of SDR allocation in reaction thereto will be developed and inserted after section 7, as will a concluding section 8.
[19]Judith E. Tyson, *Private infrastructure financing in developing countries: Five challenges, five solutions*. Overseas Development Institute. London: ODI, August 2018.

present them to the private markets to be bundled and sold. Note that substantial expertise on the part of developing-country participants is implied in Tyson's second step.

This elaborate plan suggests the need, at the very least, for caution, if not redesign, for several reasons. For one thing, Tyson's suggestion talks about market creation for a new set of instruments; but these would not represent institutional innovations in any sense. The securitization market has been growing apace at least since the 1980s – initially (in the case of 'conforming' mortgages in the US) with de factor public underwriting, and then with private underwriters and insurers, most notably AIG. The subprime mortgage markets that came to maturity in the early 2000s involved precisely the bundling and redivision ('tranching') of portfolios of time-dated claims on borrowers, which are then sold by date-to-maturity and risk-class to the ultimate lenders.

Further, the G-20 experts' proposal does not actually involve a new instrument. Securitization – the bundling and redivision ('tranching') of an initial set of time-dated claims on a borrower – has become common in financial markets since the early 19902. So this proposal amounts to a call to 'modernize' development finance by making the switch from 'bank-based' to 'market-based' credit and arranging for public or quasi-public institutional underwriting of residual risk.

7. The Covid-19 pandemic and the IMF's repositioning of Sustainable Drawing Rights. [To be developed.] Section 7 discusses the possible impact of the COVID-19 pandemic on both the extent of funding needed and on the blended-finance proposal as a means of raising the necessary finance. The possibility of using SDRs, now under the oversight of the IMF, as an alternative financing mechanism, is then considered.

Section 8. Conclusion: Rethinking the policy options for truly global solutions for climate-change and SDG-financing. [To be developed.] This section contains a brief discussion of alternative approaches to generating the finance needed to bring about a more socially and ecologically sustainable world.

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