A Post-2015 Information System for International Development and Climate Finance

Background Research Paper

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I. Introduction

Financing post-2015 development goals is a means to an end, not the end in itself. While domestic resources mobilised by developing countries themselves will remain the cornerstone of financing to reach these goals, external financing will continue to play a major role. For this reason, the outcomes, impacts and effectiveness of external development finance remain important considerations. Monitoring and reporting progress towards commitments is important to hold developed countries accountable and encourage implementation. For these purposes, it is essential to have a reliable and up-to-date information base on what finance is being provided, officially and otherwise. This should also be readily accessible by developing countries seeking to steer their economic and social development.

To address these demands for information, measurement and reporting systems will need to be transparent, cost effective and robust. They should also avoid creating perverse incentives. There should be consistency among provider and recipient systems, to allow validation of the actual delivery and use of development funds, as well as insights into their effectiveness.

This paper focuses on two specific opportunities – created by the upcoming end-date for the current Millennium Development Goals (MDGs) – for improving information on external financing for sustainable development. The first is the opportunity to modernise the overall system for measuring development finance. This could enable us, for example, to

[1] The ideas expressed in this paper do not necessarily represent views of the OECD, the OECD's Development Assistance Committee (DAC), or their member countries, or the endorsement of any approach described therein.

better distinguish between the fiscal effort of the provider and the volume of development financing that countries actually receive. Another major opportunity would involve updating the measurement system to reflect future reporting needs and capture new financial instruments and incentives. Over time, it will also be essential to find a measurement system that provides a clearer and more comprehensive view of the increasingly important South-South flows of development finance.

After providing an overview of the official development assistance (ODA) concept and the case for its revision, the paper provides emerging insights and lessons learned from monitoring climate finance, including using the so-called "Rio markers". It also outlines future work to improve tracking of climate finance, which has become a prime focus of attention within funding for sustainable development and provides good lessons for future financing frameworks. Finally, the paper then proposes some ways forward for measuring broader external development finance in the post-2015 period.

II. ODA and development finance

The ODA concept

In 1967, the UN Secretary-General commissioned an experts' report – *The Measurement of the Flow of Resources to Developing Countries* – that helped crystallise international thinking around how to define the official concessional element of resource flows for development, for which G77 countries in particular had been demanding a clear target.

In 1969, the OECD's Development Assistance Committee (DAC) – a committee of providers of development assistance that as of today includes 26 of the OECD's 34 member countries plus the European Union as a full member – introduced the concept of ODA. The criteria were defined over the following years, and have basically remained the same since 1972[2]. To qualify as ODA:

1. Resources must be provided by official agencies, including state and local governments, or by their executive agencies.
2. Resources must be used to promote the economic development and welfare of developing countries as a main objective.
3. Resources must be concessional in character (grants are concessional by definition and every loan must include a grant element of 25%, calculated at a discount rate of 10%).

ODA is the key measure used in practically all aid targets and assessments of aid performance. The DAC has established a rigorous reporting regime to collect data on ODA (as well as other non-concessional flows), which is closely tied to its core functions of reviewing its members' aid performance, and encouraging more and better aid. Data are collected through the Creditor Reporting System (CRS), both in the form of key annual aggregates and of their underlying activity-level allocation.

The 0.7% and other targets

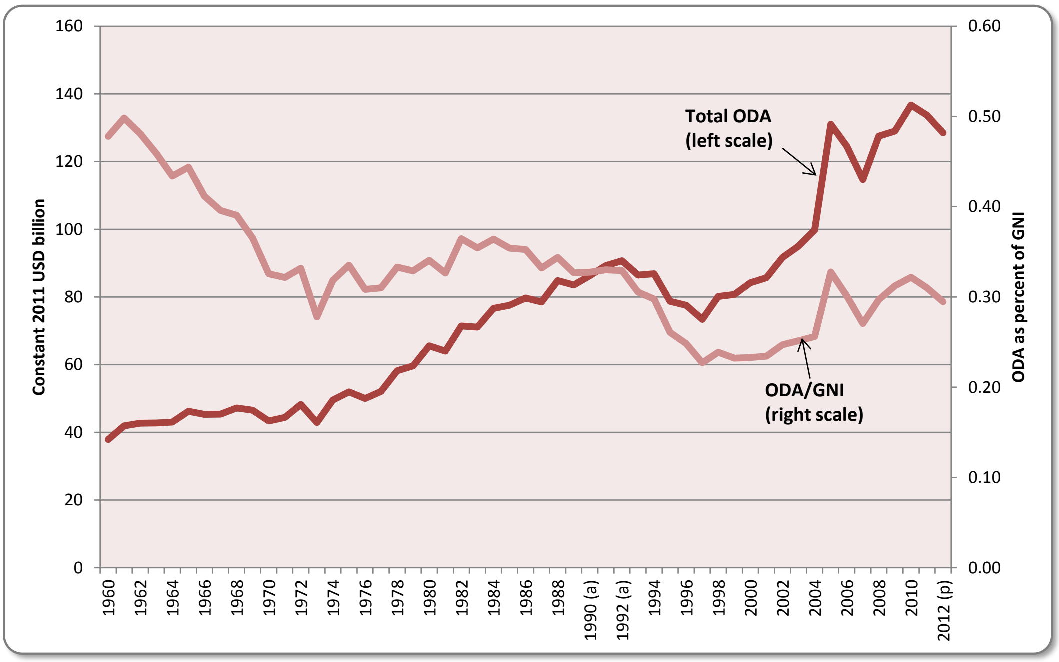
In 1970, the UN General Assembly adopted a Resolution under which each advanced country should "progressively increase its official development assistance to the developing countries and exert its best efforts to reach a minimum net amount of 0.7% of its gross national product at market prices by the middle of the decade" [3]. This target has been repeatedly endorsed at international conferences on aid and development, including the 2002 Monterrey International Conference on Financing for Development. Also, at the Third UN Conference on the Least Developed Countries (LDCs) in Brussels in 2001, developed countries agreed to provide LDCs with between 0.15% and 0.20% of their gross national

[2] http://www.oecd.org/dac/stats/officialdevelopmentassistancedefinitionandcoverage.htm#Definition
[3] UN Resolution 2626 (XXV), 24 October 1970.

income[4] (GNI) in ODA by 2015. This LDC-specific target was re-endorsed at the Fourth Conference on LDCs, held in Istanbul in May 2011. Both the overall 0.7% and the LDC-specific targets are included as targets for the achievement of Millennium Development Goal 8 of developing a global partnership for development.

Through these and other pathways, **the ODA definition, coverage and targets have become firmly implanted in the aid allocation policies and delivery modalities of provider countries**.

Chart 1: Net official development assistance from OECD-DAC countries, 1960-2012



(a) total DAC excludes debt forgiveness of non-ODA claims in 1990, 1991 and 1992
(p) Preliminary data
Source: DAC statistics

While the basic ODA definition has remained unchanged since 1972, its coverage and application have evolved in response to new activities and the changing nature of world

[4] OECD-DAC Members' performance against the targets for both total ODA and ODA to LDCs is now measured in terms of ODA/GNI ratios since the System of National Accounts promulgated in 1993 discontinued the term "gross national product" and replaced it with the equivalent concept of "gross national income". The original targets for aid to LDCs were set at the first UN LDC conference held in Paris in 1981. This already contained the 0.15% objective, but there was also an alternative of doubling the recent levels of ODA to LDCs (OECD, Development Co-operation: 1981 Review, page 21).

development. For example, in the 1980s the DAC agreed to include in the reporting of ODA tuition costs of developing country students, as well as first-year costs of sustaining developing country refugees in donor countries.

The DAC list of ODA-eligible countries and territories has also been repeatedly revised, reflecting substantial improvements in global prosperity over recent decades. Compared to the list as it stood in 1970, only 17 countries have been added – 11 of these being former republics of the Soviet Union. By contrast, 55 countries have been removed from the list, essentially because of increases in their per capita income. This trend towards higher income has continued despite the financial crisis. In the latest revision of the list in 2011, five countries were removed and 25 of the remaining countries rose to a higher income category, whereas only two fell to a lower category.

Country Programmable Aid

As previously mentioned, ODA reporting today includes certain development-related expenditures in donor countries that represent a budgetary effort but do not generate cross-border flows (e.g. student and refugee costs, donor administrative costs); it also includes other finance that does not directly enter developing countries' budgets (i.e., most technical co-operation activities). Some critics refer to these expenditures as "phantom aid", as they are seen as overrating the actual value of support received by the recipient country [5]; they urge that these amounts be excluded from ODA, which, they argue, should only capture "real" aid.

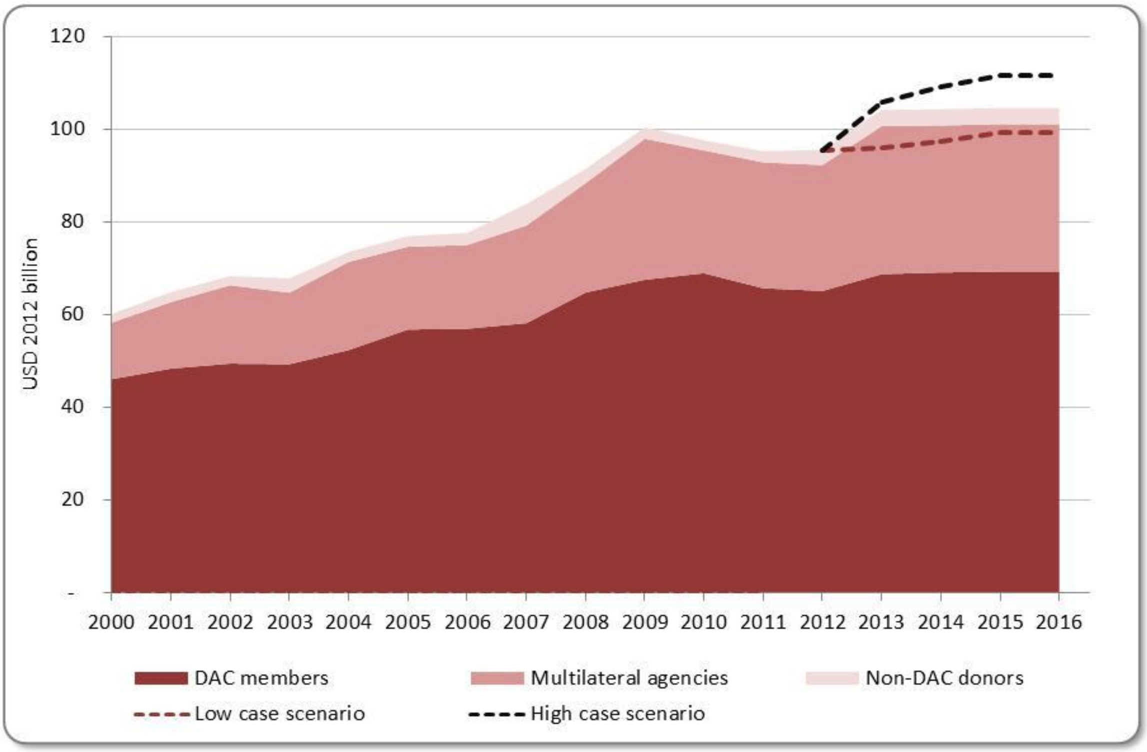
The DAC introduced the concept of Country Programmable Aid (CPA) in 2007 to enable partner countries to identify just how much aid is directly usable by them to fund their priorities and programmes[6]. While CPA is not perfect (it includes technical co-operation and project-specific donor contracts not recorded in recipient governments'

[5] https://www.actionaid.org.uk/news-and-views/the-g8-actionaid-internationals-talking-points

[6] CPA excludes expenses incurred in donor countries, such as for private students and refugees, as well as debt relief. See http://www.oecd.org/dac/aid-architecture/cpa.htm.

budgets), studies have shown that it is a good approximation of the overall flows recorded at country level[7]. Chart 2 below shows how CPA has evolved since 2000.

Chart 2: Actual and projected CPA volume 2000-2016



Source: DAC statistics

<u>Concessionality</u>

The “concessional in character” criterion for ODA loans has been a topic of extended debate among DAC members, who follow diverse approaches in determining what makes a loan concessional. The most recent debates have highlighted issues of whether and how risk should be taken into account in concessionality assessments, and how to deal with loans that are preferential to the borrower even though they are extended at terms that are near to or above the provider’s borrowing costs.

In December 2012, while recognising that loans extended to developing countries at preferential rates are making an important contribution to development, DAC Ministers

[7] OECD Development Co-operation Directorate, 2011 OECD Report on Aid Predictability: Survey on Donors’ Forward Spending Plans, 2011 – 2013, OECD, Paris, October 2011.

agreed to establish – as soon as possible – a clear quantitative definition of "concessional in character" that is in line with prevailing financial market terms and conditions[8]. In this respect, it is important to keep in mind that public guarantees for institutions providing loans help these institutions manage the financial risks of some development investments.

List of ODA-eligible countries

The DAC list of ODA-eligible recipients[9] includes all low- and middle-income countries, except G8 members, EU members and countries with a firm date for entry into the EU. The countries on this list are divided into income groups based on GNI per capita. The first group includes the LDCs, as defined by the UN, and other low-income countries; the second, lower-middle-income countries and territories; and the third, upper-middle-income countries and territories such as Brazil, Chile, China and Turkey. Even though the list has, as noted above, shrunk substantially over the years, it still comes under criticism for including as ODA recipients some emerging economies that are themselves becoming increasingly important as providers of development co-operation. This implores questions, for instance, of whether scarce ODA resources are being diverted away from the neediest countries, resulting in diminished development impact.

The next review of the list, scheduled for the second half of 2014, may provide an opportunity to encourage a concentration of ODA in the lower-income countries. **In the new geography of poverty, however, there are large pockets of poor in emerging and middle-income countries, as well as in the least developed countries.**

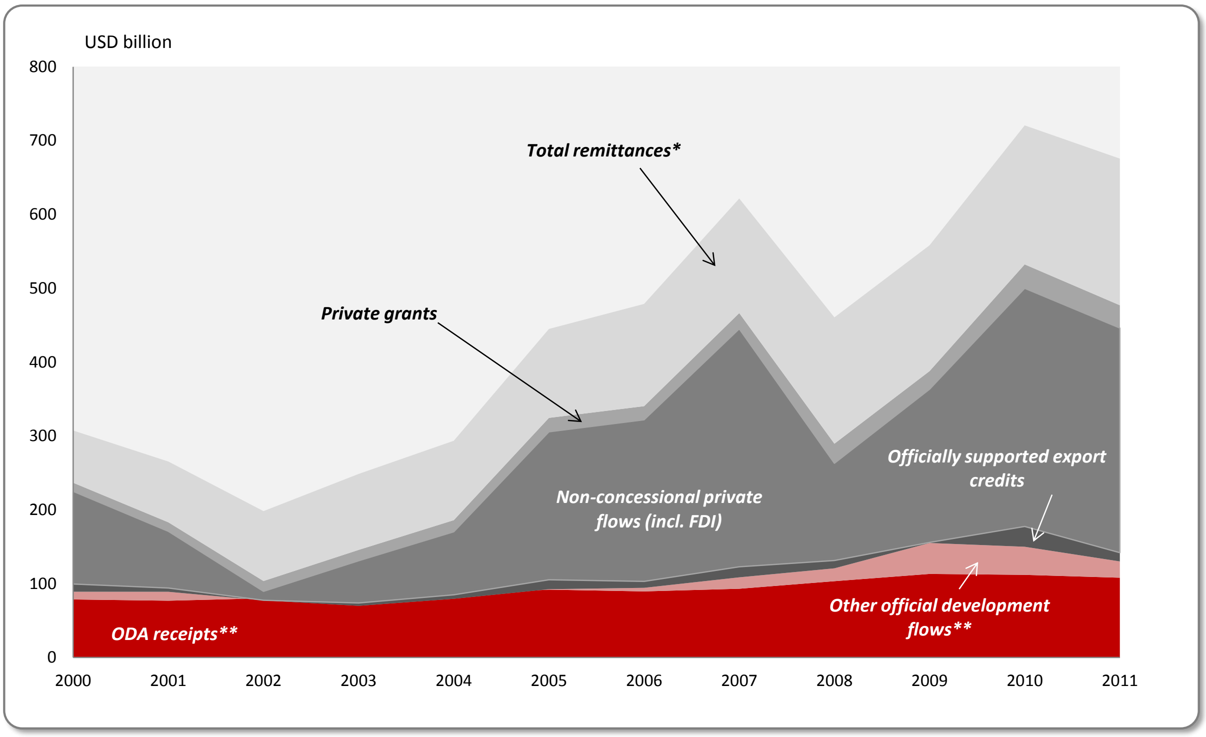
ODA in the context of broader "resources for development"

The ODA concept has come under criticism over the past decade for other reasons as well. Many argue that the specificity of its criteria and the focus on the 0.7% target

[8] http://www.oecd.org/dac/HLM%20Communique%202012%20final%20ENGLISH.pdf
[9] http://www.oecd.org/dac/stats/DAC%20List%20used%20for%202012%20and%202013%20flows.pdf

have obscured changes in development financing needs, and in the modalities for meeting them. Today, external sources of funding to developing countries have a much greater magnitude than ODA, yet these are only partially captured by the broader DAC statistical system. For example, remittances were excluded from this system in the 1960s on the grounds that they generally fund consumption rather than development. Yet remittances have grown strongly in recent years and are now seen by many as a major actual or potential source of development finance.

Chart 3: Developing countries' net resource receipts from DAC countries and multilateral agencies, 2000-2011, USD billion, 2010 prices



* Total remittances estimated from DAC members to developing countries.
** Includes bilateral and multilateral outflows to developing countries.
Source: DAC statistics and World Bank statistics for remittance

<u>A focus on more than flows</u>

Following balance of payments practice (and despite including some expenditures not generating cross-border flows), the measurement system for external development finance is based primarily on actual cross-border transfers of resources. This focus on outflows has been seen as a disincentive to most bilateral agencies to develop new, innovative financial mechanisms that could mobilise significant amounts of private investment for development through risk mitigation instruments. Such mechanisms are of great interest today, when **an increasing number of developing countries need loans, guarantees and equity – rather than grants – to boost infrastructure financing and economic growth, and to stimulate the private sector**.

Some providers have been urging more generous terms for ODA, to allow coverage of programmes and activities extended by their development finance institutions[10] – such as non-concessional lending, and loan and investment guarantees – that have minimal immediate cost to providers but offer large potential benefits to recipients. In fact, the current focus on net outflows tends to give more credit to investment projects that fail. This is because loss-making investments, like debt relief or forgiveness, score as positive net ODA whereas loans repaid on schedule and profit-making equity sales score as nil and negative ODA, respectively. The DAC's current measurement system will need to be fundamentally revised if it is to capture more than "actual disbursements" and provide information on the catalytic and leveraging effects of official finance. Yet devising an agreed methodology for calculating leverage ratios will be challenging, and care will need to be taken to avoid double counting[11].

All this makes clear the increasing importance of distinguishing between measures that focus on donor budgetary efforts, on the one hand, and flows to developing countries on the other. The present ODA system includes both efforts that do not result in outflows (e.g. in-country refugee costs), and flows that require no direct budgetary effort (loans raised in the capital market, backed with a government guarantee).

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[10] Examples of development finance institutions include the European Investment Bank; the FMO – Netherlands Development Finance Company; and Norfund – Norwegian Investment Fund for Developing Countries.
[11] There are forthcoming OECD papers that touch upon the technical issues surrounding the measurement of leveraging.

III. Emerging insights and lessons learned from tracking climate finance

Dealing with global challenges that are common to both developing and developed countries is becoming an increasingly important part of the global development agenda. It is, therefore, fundamental to relate development financing with the broader agenda of financing for global challenges, such as climate change. Emerging insights from tracking climate finance make this an illustrative case study from which we can learn lessons for monitoring, measuring, reporting and verifying commitments in a future development finance framework.

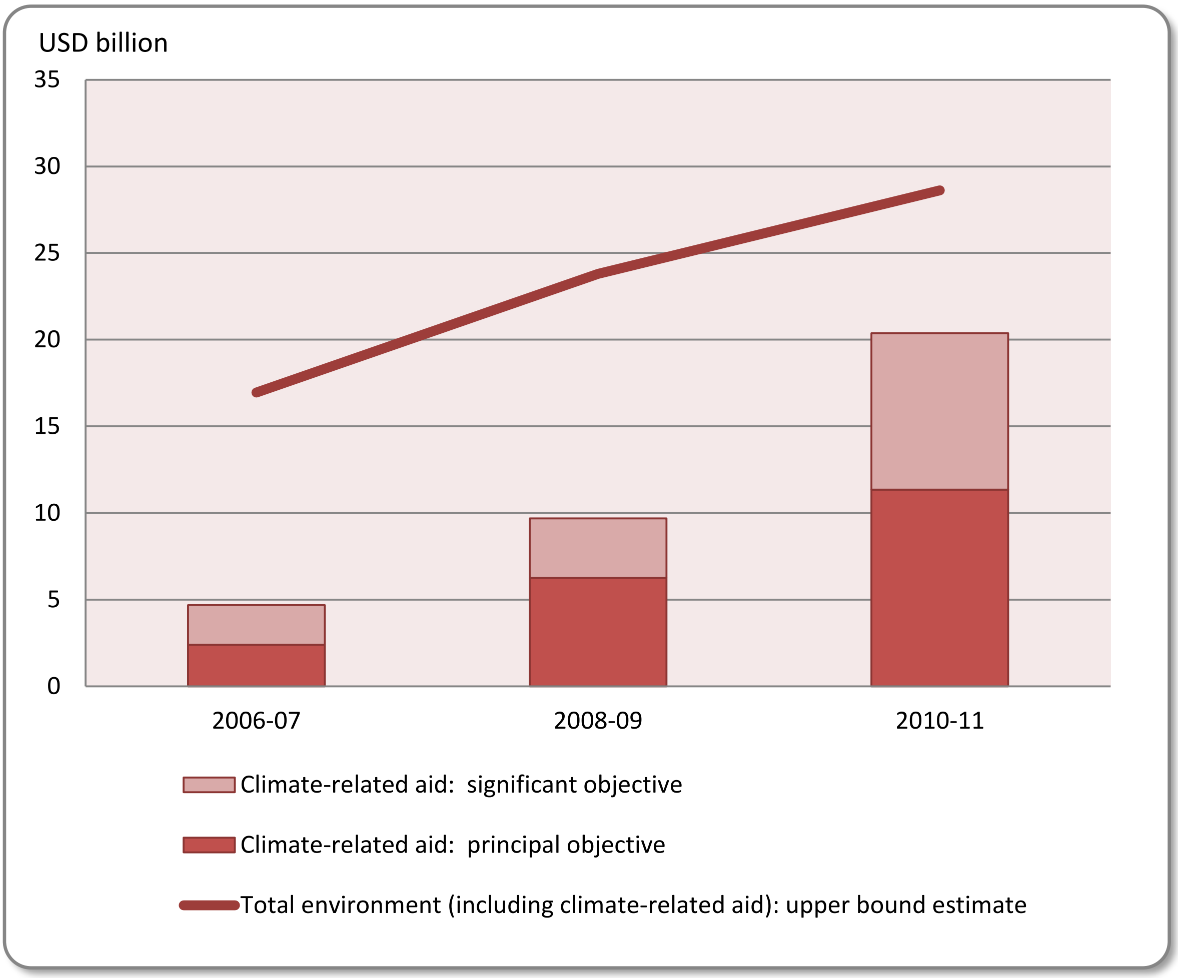
The UN Framework Convention on Climate Change (UNFCCC) has formalised two collective international climate finance commitments for developed countries: a **Fast Start Finance** commitment to provide new and additional resources approaching USD 30 billion to developing countries over the period 2010-2012, with balanced allocations between mitigation and adaptation; and a goal of **mobilising jointly USD 100 billion per year by 2020** from a wide variety of sources – public and private, bilateral and multilateral, and including alternative sources – to support mitigation and adaptation in developing countries.

The Rio Convention markers

The DAC has developed a comprehensive system for measuring **aid in support of climate-related mitigation and adaptation objectives** as part of a wider system of "Rio Convention markers". These markers also cover aid towards environmental purposes, including biodiversity and desertification. The definitions and examples provided in guidance by the DAC enable aid projects and other official financing to be assessed as to its climate focus[12]. The Rio marker system recognises that climate finance may target both mitigation and adaptation objectives and cannot be completely isolated from the broader measurement of aid flows, through allowing commitments to be scored against multiple objectives while also avoiding double counting.

[12] See the Handbook on the OECD-DAC Climate Markers.

Chart 4: Trends in environment and climate-related aid, 2006 to 2011 commitments, constant 2011 prices



Source: DAC statistics.
Note: "climate-related" aid covers both mitigation and adaptation aid from 2010, but only mitigation aid pre-2010. Reported figures for 2006 to 2009 climate-related aid may appear lower than in practice, as pre-2010 adaptation spend is not marked.

Chart 4 presents the total amount of bilateral ODA in support of environment, as well as the share of climate-related aid within this. The chart illustrates the detail captured by the Rio marker system, distinguishing between the shares of climate-related aid that target climate change as a "principal" or "significant" policy objective. The growth in climate-related finance has been significant: annual average bilateral aid commitments targeting climate change as a "principal objective" have quadrupled since 2006/7, reaching almost USD 12 billion in 2010/11; the share of aid targeting climate change as a "significant objective" follows a similar trend.

Climate-related aid represents not only a growing share of the total environmental aid commitment – it is also an increasingly important part of total ODA, rising to 13% in 2011. This indicates that climate change is increasingly being mainstreamed into core development co-operation portfolios, and that climate finance is often designed and delivered to achieve multiple development objectives. Yet despite recent growth in climate finance, the scope for further increases over the short term may be somewhat limited. Indicative forward spending surveys suggest that in the face of the current financial crisis and the large fiscal constraints in donor countries, ODA as a whole will grow slowly, at best, over the coming years; following this trend, environmental aid is also likely to level off in the near future.

Measurement challenges

Various definitional, methodological and practical challenges arise when considering measurement and monitoring of climate finance flows, both in general and towards specific financing goals. Numerous lessons are emerging, drawing also on the experience of measuring ODA, which may be applicable to future efforts to measure financing for development:

The need for an agreed upon definition: There is no internationally-agreed definition of climate finance, resulting in major challenges for consistently measuring public and private climate flows across all actors and sources, in particular towards the USD 100 billion financing goal mentioned earlier. For example, questions remain as to the definition of the climate relevance of different forms of development finance (e.g. from grants to non-concessional loans or loan guarantees), as to what constitutes 'mobilised' climate finance, and as to the sources that count as climate finance (e.g. all private finance, including mobilised domestic finance, or only North to South finance).

The need for an agreed upon data collection methodology or system: To date, in reporting to the UNFCCC on Fast Start Finance commitments, each country has adopted its own approach and methodology. There is no integrated international system for collecting and assessing all sources of climate finance, no agreement on whether the commitment should be reported on collectively or individually, and no agreed basis or methodology for comprehensive measurement.

While some international climate finance flows are already defined and measured within existing international statistical systems (e.g. the ODA flows measured by the Creditor Reporting System's Rio markers, outlined in the previous section), new sources of finance (in particular private finance) and flows mobilised by innovative development finance instruments (such as guarantees) are not. New methodologies need to be developed and implemented to systematically and robustly measure these.

The need to achieve and recognise multiple sustainable development co-benefits through delivery of international financial commitments: Many DAC members channel their climate finance through their bilateral aid agencies and through multilateral development banks, to ensure that its delivery supports country-owned sustainable development priorities. There can be multiple co-benefits from mainstreaming climate change mitigation and adaptation strategies and programmes into development efforts. For example, forestry or sustainable energy projects clearly can have both development and climate objectives, with proper design of these programmes. It is therefore useful to monitor the multiple objectives of climate finance in the broader context of development finance and other development flows, acknowledging that it is impracticable to completely separate climate finance from development finance; care must be taken, nonetheless, to avoid double counting when isolating and reporting against individual goals.

A more comprehensive and transparent monitoring framework for future financing goals will ideally build on existing systems to ensure the delivery of comprehensive and comparable data across sources, channels, targeted sectors, types of programmes, and recipient countries. Progress is likely on several fronts and the OECD aims to contribute to this progress through its various work programmes.

New OECD work on measuring and monitoring climate finance

Work is currently underway at OECD to extend the CRS and the Rio markers to cover non-ODA flows (such as guarantees, non-concessional loans and export credits) that target both development and specific environmental concerns.

The OECD is also collaborating closely with multilateral development banks (MDBs) to record their finance in the DAC statistical framework, which includes partial information on DAC member contributions to specific climate funds. The MDBs have developed a joint approach to tracking climate finance, which builds on the Rio marker system but aims to arrive at a single figure for climate-related aid, rather than grading activities according to whether they have a "principal" or "significant" climate objective. Work is being undertaken to harmonise the multilateral and DAC approaches, recognising the differing natures of bilateral and multilateral climate finance and the need to avoid double counting and allow aggregation across diverse international sources and channels for delivery.

The OECD has recently taken on the coordination of a Research Collaborative on tracking private climate finance. This project aims to contribute to the development of methodologies and systems for more comprehensive tracking of private climate finance flows to, between and in developing countries; it also seeks to determine which private flows are mobilised by developed countries' public interventions. The Collaborative functions as a network of interested governments, relevant research organisations and international finance institutions that share the best available data, expertise and information to advance policy-relevant research in a comprehensive and timely manner. It serves as a co-ordinating platform for identifying research priorities and gaps, sharing information, weaving a coherent narrative across what would otherwise be disparate research outputs, and communicating results to raise awareness in this area.

IV. Improving information on development and climate finance in a post-2015 world

As the international community moves towards a post-2015 framework, broader measures of development finance – within a comprehensive financing framework for the post-2015 development goals – will be needed. The OECD is contributing by revising its methods of monitoring and measuring development co-operation and broader external development finance, with the following expected outputs:

- **A broader measure of external development finance, beyond the current ODA concept**: This would provide a better "anchor" for discussions on global financing needs, greater accountability and monitoring, more efficient allocation of development resources, and improved impact evaluation. The measure will need to address questions such as whether to measure only flows to developing countries or also development-related expenditures that may not give rise to such flows, and whether to include all flows with clear development impact or only those with clear development intent. This broader measure will need to address both public and private flows in order to comprehensively capture all resource flows for development.
- **Better comparison of provider effort:** In measuring effort, comparability is of the essence. The recent concessionality discussion among DAC members has revealed that with current low interest rates, some donors are able to lend at attractive rates without making a budgetary effort. Other issues include whether and how to count

instruments that do not give rise to cross-border financial flows (e.g. guarantees, preferential tariffs, tax concessions and expenditures). A new, broader measure of development finance will provide a better basis for analysis and comparison of donor effort.

- **Better ways of measuring receipts and concessionality from the developing country perspective:** The concept of Country Programmable Aid (CPA), described earlier, provides a useful starting point for measuring aid from the viewpoint of the recipient. Nonetheless, a broader measure of total official development finance from the recipient perspective may be desirable and useful for numerous purposes.
- **Additional measures to provide a better picture of the new development landscape:** Beyond the measures suggested above to better monitor "provider effort" and "recipient benefit", a new measure could aim to assess forms of South-South co-operation using different metrics, such as technical co-operation expressed in "person-years". Yet another measure could aim to capture the extent of developing country domestic resources allocated to development.
- **Options for quantifying leveraging and catalytic effects:** A better understanding of the relationship between the different flows – especially leveraging effects – is needed. The DAC proposes to examine forms of leveraging, catalysing and associating financial flows to promote value-for-money in achieving development outcomes. A detailed study of current innovative financing mechanisms and their ODA components was produced in 2011[13], and a new study on the effects of guarantees in stimulating loans and investments will shortly be issued. Looking more broadly, the DAC has a traditional role in studying how different types of flows interact and what triggers these interactions; it will continue to look at ways of ensuring that aid does not crowd

[13] OECD Development Co-operation Directorate, *Mapping of some important innovative finance for development mechanisms*, DCD/DAC/STAT/RD(2011)1/RD1, OECD, Paris, 7 February 2011

out other development flows, for instance in areas where commercially viable investment is feasible.

- **Accounting for global public goods and other development "enablers":** More comprehensive monitoring of development finance in the context of the post-2015 goals is likely to prompt discussions on the need to monitor the financing of global objectives or public goods (e.g. prevention of contagious diseases, biodiversity protection, peace and security, and open and fair global trade). Monitoring new resource flows in support of the eventual post-2015 framework will necessitate a review of statistical methods to track financing for such global objectives or public goods.

VI. The way forward

Clearly, major changes in the global development landscape call for a new and more comprehensive approach to financing the post-2015 development goals. The many useful lessons learned in tracking ODA and climate finance should be brought to bear in the elaboration of a financing framework for post-2015. In addition, work will need to be undertaken on new methods of monitoring and measuring development co-operation, and on analysis of broader external development finance.

The OECD is committed to sharing its knowledge on monitoring and measuring development finance. It will seek to fully engage all key stakeholders (partner countries, emerging providers, international organisations, the private sector, civil society and academia) in pursuing this work to develop the statistical categories and methods that will capture all relevant finance. And it will facilitate reporting by all providers of development co-operation, public and private, to ensure that there is a robust measurement system for development finance in place by 2015.

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