Crises are eating into development funding

Rich nations need to top up financing for multilateral institutions and initiatives

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The World Bank and IMF spring meetings are taking place this week in the shadow of rising geopolitical uncertainty. Upcoming elections in the US, ongoing conflict in Ukraine and now the eruption of hostilities between Israel and Iran are all weighing on policy-makers' minds. But amid these crises, the international community must not lose sight of the pressing need to keep funding global development, health and climate initiatives.

These issues have started to take a back seat. New data from the OECD, the rich-country think-tank, shows that advanced nations' official development assistance budgets have increased in recent years. But the majority of that rise represents funding for Ukraine and the cost of hosting refugees from Ukraine and elsewhere. The amount for multilateral organisations, including the World Bank, IMF, and health funds such as Gavi, the immunisation initiative, has only risen slightly overall, and even shrank in two of the last six years.

Moreover, low-income countries' access to finance has come under pressure. A wave of countries has been flirting with default, as high rates have locked them out of bond markets. China, once the largest bilateral creditor to developing countries, has stepped back from funding, instead starting to draw back capital as loans come due. China and private creditors have also confounded the Paris Club's efforts to restructure debt. This has forced countries into a difficult choice: endure a lengthy default like Zambia, or tighten already strained budgets like Nigeria.

As a result, many poorer countries have been unable to invest adequately in public welfare and climate mitigation. This has raised pressures on already impoverished households in nations that are also less resilient to global shocks, creating regional instability and driving more migration.

Multilateral institutions are constrained. The World Bank's International Development Association — the arm that offers financing to low-income countries — can raise funding via capital markets. But IDA's chief fundraiser recently told the Financial Times that its fiscal headroom is shrinking due to high borrowing costs. The IMF's equivalent, the Poverty Reduction and Growth Trust, has also run down its capital amid unprecedented levels of lending.

IMF managing director Kristalina Georgieva, who will be re-elected this year, has built a strong partnership with the World Bank's Ajay Banga. Both leaders should convey a clear message this week: the global community cannot afford to be distracted.

They should first push for more funding. Banga has called for the “largest ever” funding haul for IDA this year. Georgieva should make similar calls for PRGT before its funding next year, as these are the funds with the most latitude to help low-income countries.

Second, they should encourage donors to explore innovative financing strategies. This includes using special drawing rights — a reserve asset created by the IMF — to issue bonds on behalf of developing countries, or making it easier to transfer them.

Finally, they should focus on improving existing processes. In a curtainraising speech, Georgieva foreshadowed that adjustments to the G20’s Common Framework for debt treatments would be a focus this week. This includes adding stricter timelines, and ensuring a more standardised treatment of different types of creditors, which has been a sticking point for China.

Rising tensions in the Middle East coinciding with the spring meetings this week illustrate the spending dilemmas facing donor countries. But the imperative is clear: pay up, or things will only get worse.

Better risk data will help improve confidence in EMs

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Emerging market businesses have long been perceived as risky destinations for investment. But how risky, exactly? We now have better information with which to answer that question — thanks to a pair of reports published in March by the Global Emerging Markets Risk Database Consortium (GEMs), a group of 25 multilateral development banks and development finance institutions.

The statistics yield clear messages: investment risks in EM companies compare favourably with those experienced in other asset classes. Moreover, the portfolio diversification provided by EMs gives the most benefit (versus assets with similar default rates) in times of global stress.

The reports provide a robust set of statistics taken from this database that spans 30 years of lending by GEMs members. The consortium pools credit risk data and publishes it as a resource for public use.

It has evolved over time into a community that develops common approaches and data methodologies to record default and recovery frequencies.

In debt financing, default rates are a guiding metric for investors, measuring how often a financial obligation is unmet. Between 1994 and 2022, these rates in the GEMs portfolio averaged around 3.5 per cent.

This is roughly comparable to average default rates observed in companies that receive a B credit rating from S&P (3.4 per cent) and a B3 from Moody's (4 per cent).

Moreover, during global crises, default rates in the GEMs portfolio were lower than for the S&P's B rated and Moody's B3 comparators, a welcome counterpoint to somewhat higher default rates in non-crisis times.

Recovery rates, which measure the amount of investment recovered after a default occurs, were also higher than expected. At 75 per cent, the recovery rates within the GEMs data set surpass those reported for Moody's Global Loans at 70 per cent, Moody's Global Bonds at 59 per cent and JPMorgan Emerging Market Bonds at 38 per cent.

Looking at our data, the IFC's private sector portfolio had a low average default rate of 4.1 per cent from 1986 to 2023 — suggesting the untapped potential and resilience of investments in EMs, where more capital is needed.

Research published by the National Bureau of Economic Research in 2020 showed that IFC's equity investments over the previous four decades outperformed the S&P 500.

It must be noted that these statistics reflect the unique experience of multilateral development banks and development finance institutions. GEMs members deploy more in-country staff than global commercial investors, providing detailed knowledge of the regulatory and political aspects of the market and informing our choice of clients.

Moreover, such institutions often accompany lending with advisory services to clients to build their capacity. Such factors may explain the lower defaults and superior recovery rates.

We also typically deploy “patient capital”, which seeks a strong return over longer time horizons. As a result, our grace periods before default tend to be longer than other investors. These variations may skew comparisons.

But with this understanding, investors can take general encouragement about the state of EMs and invest accordingly.

Reallocating just 1 per cent of assets under management globally to EMs each year could have a transformative impact on growth and development in these countries.

However, investors need more than just encouraging statistics. They seek regulatory certainty, political risk insurance and foreign exchange risk mitigation.

As a co-founder, along with the European Investment Bank, and the largest private sector statistics contributor to the GEMs consortium, IFC remains committed to pooling data with our partners to optimise future reports.

By providing the public with essential risk-reward calculations, we aim to equip investors with the information they need to make decisions about EMs.

These efforts, combined with the International Bank for Reconstruction and Development’s recent release of sovereign default and recovery rate statistics, means that the World Bank Group will continue to support this important initiative by providing loan portfolio data, focusing on alignment, utility and consistency.

Investor confidence in EMs must be built layer by layer. These new statistics offer a robust foundation.