World Bank Financializing Development[1]

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The World Bank has successfully legitimized the notion that private finance is the solution to pressing development and welfare concerns, including achieving the Sustainable Development Goals (SDGs) through Agenda 2030.

A recent McKinsey report estimates that the world needs to invest about US$3.3 trillion, or 3.8 per cent of world output yearly, in economic infrastructure, with about three-fifths in emerging market and other developing economies, to maintain current growth.

People in Saint-Louis, Senegal. © Ibrahima BA Sané/World Bank

The world financing gap is about US$350 billion yearly. If new commitments, such as the SDGs, are considered, the gap would be about thrice the currently estimated gap as available public resources alone are not enough. Thus, for the Bank, the success of Agenda 2030 depends on massive private sector participation.

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Maximizing finance

The Bank's 'Maximizing Finance for Development' (MFD) strategy marks a new stage. It presumes that most developing countries cannot achieve the SDGs with their own limited fiscal resources and increasingly scarce donor overseas development assistance (ODA).

Bank prioritization of financial inclusion presumes that fintech-powered digital financial inclusion would increase growth, create jobs and promote entrepreneurship in developing countries.

The MFD purports to respond to the G20's April 2017 Principles of MDBs' strategy for Crowding-in Private Sector Finance for growth and sustainable development. The G20 has offered the Roadmap to Infrastructure as an Asset Class for energy, transport and water inter alia.

The 2017 MFD strategy recycled the Bank's 2015 From Billions to Trillions: Transforming Development Finance, arguing that MDBs should increase financial leverage via securitization to catalyse private investment, thus promoting capital markets by transforming bankable projects into liquid securities.

The MFD presumes that public money should mainly be used to leverage private finance, particularly institutional investments, to finance the purported US$5 trillion SDG funding gap.

Financialization coalition

The MFD strategy seeks to enable financialization and transition to securities-based financial systems in developing countries, complementing other initiatives by the Bank, IMF and G20. Such initiatives are expected to encourage investors to use environmental, social and governance criteria to attract, mobilize and sustain needed financing.

The MFD presumes that public money should mainly be used to leverage private finance, particularly institutional investments to finance the funding gap. Government guarantees are deemed necessary to 'de-risk' projects, especially for public-private partnerships (PPPs).

Meanwhile, the International Finance Corporation (IFC), a Bank subsidiary, is helping subsidize capital market involvement in infrastructure development; the MFD strategy envisages capital markets in 'green bonds', 'social impact bonds', infrastructure bonds and so on.

Securities markets are supposed to enable institutional investors to make desirable social and environmental impacts. MFD advocates claim that capital markets provide new solutions to development challenges such as inadequate infrastructure, and poor access to schooling, clean water, sanitation and housing.

The Financial Stability Board has also proposed measures to transform 'shadow banking' into securities-based finance, while the European Commission's Sustainable Finance initiative seeks to similarly reorient institutional investors and asset managers.

Cascading financialization

The Bank's ‘Cascade' approach seeks to institutionalize this bias for private financing. It seeks to facilitate securities lending by enabling ‘repo' market financing and hedging, and ‘rehypothecation', i.e., allowing securities to be used repeatedly for new lending.

The Cascade approach seeks to accelerate financialization with measures to accommodate new asset classes, enable banks to engage in securities and derivatives markets with minimal regulation, deregulate financial institutions creating tradable assets from PPP projects, and facilitate capital flows ostensibly for development.

It presumes market imperfections and missing markets deter the private sector from financing sustainable development projects, and proposes to address such bottlenecks by ‘internalizing externalities' and providing subsidies and guarantees to de-risk investments.

Tito Cordella notes that it prioritizes private finance even when a project is likely to be profitable if undertaken with public funds. He notes the tensions between maximizing private financing and optimizing financing for development, and some implications. Public options are only to be considered after all private options are exhausted or fail.

Thus, the Cascade approach presumes that the private sector is always more efficient, despite actual experiences. Clearly, it not only reflects an ideological preference for private finance, but also seeks to promote securities and derivatives markets, as market liquidity is among the core G20 Principles of MDBs' strategy for crowding-in Private Sector Finance.

Hijacking development finance

The strategy would thus commit scarce public resources to ‘de-risking' such financing arrangements to transform ‘bankable' development projects into tradable assets. This means that governments will bear more of the likely costs of greater financial fragility and crises.

Such government measures will inadvertently undermine needed financial institutions such as development banks. There is no reason to believe that MFD will somehow create the capital market infrastructure to improve finance for SMEs or needed development transformations.

Once a project's future revenue streams are securitized, the multilateral development banks' environmental and social safeguards no longer apply. Contracts to repay securitized debt held by investors would be disconnected from the underlying project financed and its consequences.

Holders of these securities have no incentives to prioritize social or environmental goals. Private equity and hedge funds that have short-term incentives for profit-taking, including by asset-stripping, are not concerned with social, environmental or other public interests.

Not surprisingly, considerable doubt exists as to whether private capital markets and institutional investors can be incentivized to finance long-term public goods as these mechanisms serve the profit motive, not public welfare.

To know more:

- European Commission, Sustainable Finance initiative, EU website, 2019.
- International Financial Architecture Working Group, Principles of MDBs' strategy for crowding-in Private Sector Finance for growth and sustainable development, G20, 2017.
- Woetzel, J., *et al*., Bridging global infrastructure gaps, McKinsey Global Institute, 2016.
- AfDB, ADB, EBRD, EIB, IADB,IMF and WB, From Billions to Trillions: Transforming Development Finance, International Finance Committee, 2015.

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