G-24 Technical Group Meeting

3-4 March, 2016

Cartagena, Colombia

SUMMARY REPORT

The Spring 2016 Technical Group Meeting (TGM) was held in Cartagena on March 3-4, hosted by the current G-24 Chair, Colombia. Members discussed priority issues for the Group at this juncture, including financing infrastructure through domestic resource mobilization and public-private-partnership (PPPs), fiscal policy and inequality, innovations and challenges of financial inclusion and reinvigorating growth. Participants benefitted from the perspectives of expert speakers as well as country discussants, whose inputs served to underpin substantive deliberations and lesson sharing.

Minister Mauricio Cárdenas delivered the opening remarks for the TGM. In this year's TGM, he noted the importance of the topics to the Members' medium term development agenda. He also pointed to the challenge in pursuing the medium term growth and development goals in face of the sharp drop in oil and commodity prices, which has affected the fiscal and external situations of their exporters and the tightening of financial markets. He discussed the implications of these challenges and policy responses from Colombia's perspective. Against this background, he noted the important role of international financial institutions in supporting developing countries manage the risks they face in the short term and pursue their growth agenda in the medium to long term. Minister Cárdenas further indicated that the issues raised and consensus that emerged from the TGM's deliberations will provide a strong foundation for the upcoming Ministerial meeting in April in Washington, D.C., as well as the Annual meeting in October. Discussion elements will also enable the Group to engage productively in current global debates. Key lessons and takeaways from each session are outlined below.

Session 1a: Financing Infrastructure through Domestic Resource Mobilization

The opening session of the meeting focused on financing infrastructure through domestic resource mobilization. Infrastructure investment could boost demand and create jobs in the short-term while expanding the productive capacity and raising potential output in the long run. EMDCs require a major increase in infrastructure investment in order to achieve crucial development goals.

Sanjeev Gupta, Deputy Director in the Fiscal Affairs Department at the IMF, was the first speaker in this session. His presentation focused on improving the efficiency of public investment to create fiscal space for financing infrastructure.

The fiscal space for many developing countries is under pressure, given that domestic revenue in many countries has not kept pace with rising expenditures, and that the global economic growth prospect is weakened. To strengthen the efficiency of public expenditure is one way to alleviate the fiscal pressure in many countries.

Public investment has not fully recovered from historic lows. Public investment as a share of GDP in advanced countries has been declining, whereas it has been slightly picking-up in the emerging markets. For the G-24 membership as a whole, the public investment to GDP ratio is below the one of emerging markets. The same goes for public capital stock, where there is a decline of public capital stock as a percentage of GDP for the G-24 countries. More importantly, public capital stock on a per capita basis is not increasing when compared with output. In addition, public investment inefficiencies are sizeable. IMF recently surveyed 107 advanced countries and developing countries and found that the average efficiency gap for public investment is at 27%, and for the 15 G-24 members in the survey, the gap is about 31%. This means that about a third of investments' potential impact is being lost.

Large disparities remain in quality and access to infrastructure. Survey measures suggest that there are some disparities in infrastructure quality between advanced and emerging countries. The disparities exist for infrastructure access, too. For G-24 countries as a group, the perception of infrastructure quality and measures of infrastructure access are lower than the average of emerging markets.

For public investment management, G-24 countries are found to have relative strengths in: national and sectoral planning, central-local coordination, and multi-year budgeting. On the other hand, the relative weaknesses of G-24 countries are: fiscal rules, management of PPPs, company regulation, project management and the monitoring of assets. This is according to the Public Investment Management Assessment (PIMA) framework developed by the IMF – a framework that evaluates key institutions in the public investment management process including planning, allocating and implementing. Ten countries within the G-24 membership were surveyed.

To improve public investment management, countries are advised to ensure a sustainable level of total investment, a stable allocation of investment spending between sectors, and lower levels of rent-seeking. To achieve these aims, the reforms should focus on multi-year budgeting and management of PPPs, budget unity, project appraisal, selection, procurement, and management. For low-income countries, comprehensiveness of budget, availability of funding, and monitoring of assets.

Other methods to alleviate the fiscal pressure include: generating fiscal space by mobilizing more domestic revenue, and increasing borrowing. Some countries would have the potential for generating more revenue through income taxes, payroll taxes, consumption taxes and other measures. The potential for additional revenue could reach as high as 10% of GDP for certain countries.

Ines Bustillo, Director at the United Nations Economic Commission for Latin America and the Caribbean delivered the second presentation which focused on bond markets as a source of financing for infrastructure in Latin America and the Caribbean (LAC).

There is a substantial gap in infrastructure investment in the LAC region. According to ECLAC estimates, the largest economies in LAC have an infrastructure investment gap of around 6.2% of GDP per annum, and the larger need comes from transportation and energy sectors. The increase in private investment has not offset the decline of public funding for infrastructure. The quality of infrastructure is low, which led to negative impacts on other sectors.

Traditional financing sources for infrastructure in LAC come from the public sector, commercial banks, development banks and bi-lateral financing. Direct fiscal support accounted for more than 65% of overall investment in infrastructure in LAC. However, given the sharp drop in commodity prices, many commodities export countries are facing fiscal challenges and undergoing a cyclical investment contraction. Commercial banks, which used to be another key player in financing infrastructure, are increasingly risk averse after the financial crisis and constrained by the stronger regulatory requirements of the Basel III. National development banks have been very successful in countries such as Brazil, Mexico, and Colombia, thanks to the reforms aimed at increasing financing and guarantees for infrastructure projects. Regional and multilateral development banks are expected to play a larger role in the years to come. There are new bi-lateral resources available, for example, the Chinese policy banks have financed about USD 40 billion infrastructure projects in LAC since 2005. In addition, PPPs have been particularly important in energy and telecommunications sectors in the LAC region since the 1990s. The financing method was being applied to greenfield investment in recent years. Concerns about PPPs include issues about privatization, how to improve the regulatory and institutional aspects, among others.

Bond issuance is considered a new, innovative and growing instrument for financing infrastructure in LAC. However, the role of capital market in financing infrastructure is still relatively small. A study by the Inter-American Development Bank (IDB) that summarizes the composition of private debt financing for infrastructure in LAC from 2004 to 2014 concluded that capital market makes up about 10.5% of the total private debt, the rest 89.5% came from syndicated bank loans. That being said, there has been a number of successful bond issuances, both local and international, in countries such as Brazil, Chile, Colombia, El Salvador, Mexico, Peru and Uruguay. The issuance of the green bond is another new trend observed in a number of LAC countries. Given the challenges of sustainable development, there is scope for the green bond market to grow in the years to come.

There are a number of factors that could boost infrastructure bond financing. For example the strength and willingness of local pension funds in investing in infrastructure assets; the access to international capital markets; the credit rating and economic potential of the bond issuer; the guarantees or partial guarantees from the government and regional/multilateral banks; and a well-planned risk mitigation system.

Looking forward, bond issuances can be an important part of the funding mixture for infrastructure investment. National, regional, and multilateral development banks play a key role in providing partial or full guarantees, as well as in helping mobilize other relevant parties in this process. However, bond financing is still a tool available only to a set of countries. Therefore, regional and multilateral banks remain crucial in providing direct financing for economies with less developed domestic capital markets and limited access to international capital markets. Given the magnitude of the infrastructure effort required, a mix of public-private and national-international sources of financing is needed.

Clemente del Valle, President of Financiera de Dessarollo Nacional (FDN), followed with the third presentation. His presentation focused on the role of FDN as a specialized and innovative development bank in Colombia.

Colombia faces a critical challenge in the quality of its overall infrastructure, particularly its roads. The country launched the 4G (4th generation) program as an ambitious goal to meet this challenge. The 4G program's aim is to deliver 8,100 km of road networks in 45 projects with an investment of USD 17billion. Traditional infrastructure loans, from bank financing and corporate financing, only contributed USD 2.7 billion, the rest of the 17.5 billion required needed to be leveraged with innovative financing approaches. To meet this challenge, Colombia updated its PPP framework and established a specialized infrastructure development bank to bring together the interests of key international and local players in the infrastructure markets through two key objectives: to provide better financial conditions and to mobilize large amounts of resources for projects.

FDN's strategy involves attracting different sources of finance, practicing proper risk management and promoting standards in project financing. To date, the 4G program has approved 29 projects with equity, CAPEX, and debt worth of USD 3.06 billion, 12.39 billion, and 12.69 billion, respectively. FDN has leveraged more than ten times its financial resources, from USD 0.35 billion to 4.4 billion mobilized through local, international and multilateral banks, local and international capital markets, debt funds and FDN senior debt. Some of the innovative instruments that were deployed include a subordinated multipurpose facility that helps to provide additional liquidity reserve, mitigate the principal risks of the projects and improve the credit rating of the project. As well as supporting the establishment of debt funds that are managed by specialized fund managers experienced in infrastructure project finance, to allow institutional investors to participate in infrastructure projects through credit operations from the construction stage, and to reduce the risk of refinancing.

The experience of FDN provides insight on the important roles that a domestic development bank can play in boosting financing for major infrastructure projects. This include crowding in other sources, developing innovative and flexible products, and having a corporate governance to ensure independence and rigor in investment decisions and stability of the entity.

Gerardo Zuniga, Senior Advisor at the IMF, closed the session with a speech focused on the challenges of promoting infrastructure investment in EMDCs and Mexico's recent experience in tackling these challenges.

EMDCs are facing a string of challenges: low commodity prices, episodes of large capital outflows, sharp exchange rate depreciations, higher financial markets volatility and lackluster external demand. Therefore, policies in EMDCs need to strengthen domestic demand in a sustainable way, and one avenue to do that is in infrastructure investment.

To fully realize the potential of infrastructure investment, it is important to address the challenges and explore the opportunities that come with it. The first challenge is financing. With limited domestic fiscal space and increased risk aversion towards EMDCs in the international capital market, the multilateral, regional and domestic development banks need to enhance their role in catalyzing financing. Besides, countries need to explore diversified and innovative financing approaches to foster private investment.

In Mexico for example, the government is working to create conditions to unlock the country's investment potential by promoting the following measures: a strong commitment to fiscal discipline and macroeconomic stability, strengthening of the institutional and legal framework, and a structural reform agenda that fosters private investment in key sectors of the economy, accompanied by a financial reform that promotes competition and access to better financing conditions.

The current infrastructure investment strategy being implemented in Mexico gives important consideration to private investment. Institutional investors are considered to have a key role to play in meeting the infrastructure financing gap given the long-term nature of their liabilities and their corresponding need for suitable long-term assets. Additionally, the institutional investors often have a low investment allocation in infrastructure assets, which presents a large opportunity. To attract these investors, it is key to develop a wide range of market-oriented financial instruments suitable for different investor profiles, and to cover different stages of the infrastructure investment cycle. Some new financial vehicles created by the Mexican government include a real-estate investment trust, investment project certificates that emulate a typical private equity structure, and educational infrastructure certificates, etc.

Furthermore, meeting participants are suggested to think about approaching infrastructure investment in a coordinated way, to promote global infrastructure connectivity to enhance cooperation, and exploit synergies regionally in infrastructure initiatives.

To summarize, for a country's infrastructure investment strategy to be successful, one first has to identify key strategic sectors where the limited resources are going to be focused, after which the country needs to be creative in finding financing vehicles and allowing private participation, and finally it is essential to maintain a solid macroeconomic framework which will facilitate the participation of multilateral development institutions, as well as international investors.

After Mr. Zuniga's intervention, Abebe Tadesse Feyisa, a representative from Ethiopia shared the country's experience on enhancing infrastructure investment. Ethiopia has enjoyed stable double digit economic growth in the last decade, thanks to the investment in infrastructure. Growth has contributed to a reduction in poverty levels from 38% of the total population to 29%. Despite low domestic savings and low tax base, Ethiopia has increased its investment as a percentage of GDP to 38%. The resources for investment are mobilized through a mix of channels that include: reducing government consumption in less efficient areas, maximizing the impact of concessional resources, accessing non-concessional resources through south-south cooperation for major projects such as rail, road and energy, attracting foreign direct investment, and designing monetary policy that is friendly to investment.

Participants raised questions for further deliberation on how to access the resources of domestic pension fund for infrastructure investment, what kind of risks national and multilateral development banks should focus on to catalyze private funding, and what would be the implication of BASEL III on commercial banks' lending into infrastructure projects.

Session 1b: Financing Infrastructure and the Role of Public-Private-Partnerships

The second session covers the relevant challenges and recent developments in public-private-partnerships. Laurence Carter, Senior Director of the Public-Private Partnerships group of the World Bank, opened the session with a presentation focused on public-private partnerships (PPPs) in EMDCs.

In terms of financing, investments in PPP Projects in EMDCs have grown in absolute terms with two notable periods of expansion (1991-1997 and 2004-2012) and one period of contraction (1997-2004), but it has not kept pace with GDP growth. Particularly in the past two or three years, the investment has stagnated. The growth in PPP in EMDCs was increasingly driven by the five big economies: Brazil, India, Turkey, China, and Mexico. These five countries also have the highest investment as a percentage of GDP ratios among EMDCs. For the rest of EMDCs, financing is becoming more evenly distributed across regions, and the market is deepening.

A notable new trend is that a significant number of projects (23%) are originated through unsolicited proposals, particularly in the energy sector. The World Bank is working to analyze the best practices of doing unsolicited proposals in developing countries.

Direct and indirect government support continues to play a critical role in facilitating private sector investment in PPPs. In developing countries from 2010 to 2014, in a number of sectors including energy, transport and water and sanitation, projects with government support reached 63% of the total number of projects. Water and sanitation have the highest percentage (85%) of projects receiving some government support.

Mr. Carter then echoed points made during the first session: that the overall macroeconomic conditions coupled with a country's sound institutional and regulatory framework are crucial for PPP markets to grow. Private participation in infrastructure is more sensitive than foreign direct investment to country risk. Infrastructure data confirms this theory, as countries with established and stable institutions and regulatory systems were able to advance more PPP projects. Mr. Carter then emphasized that the real gap in infrastructure is the infrastructure service gap. The better service is achieved partly through mobilizing financing, and partly through better governance, better management, and mobilizing expertise and innovation from the private sector.

The role of multilateral organizations beyond financing, in supporting PPPs has been significant. Some of the joint efforts by the multilateral organizations include: providing benchmark data that provides measures of PPP readiness for countries; creating a fiscal assessment tool for PPPs that help the country to identify the direct and contingent fiscal implications for PPP projects; creating an analysis tool for prioritizing infrastructure projects and identifying and ranking the projects that should be PPP financed; supporting governments on project preparation by enabling the standardization of projects; developing a disclosure framework that features best practices around the world. The World Bank, in partnership with other development banks, is organizing a Global Infrastructure Forum (GIF) that improve alignment and coordination among MDBs and their development partners to better develop sustainable, accessible, resilient, and quality infrastructure for developing countries. This event will be held on April 16, 2016 in Washington D.C.

Mar Beltran, Senior Director at the Global Infrastructure Hub (GIH), followed with a presentation focused on introducing the GIH and lessons learned in procurement.

The GIH was established during the Australian Presidency over the G20. Its goal is to support the development of PPPs by fostering a knowledge network, building capacity, bridging data gaps, disseminating best practices, fostering project pipeline, informing private sector, facilitating systemic reforms, promoting better procurement, and facilitating market entry. It is organized around three areas of delivery: a knowledge sharing platform to provide information that increases the transparency and efficiency of markets, a toolkit of products to assist private and public sector at all stages of their respective processes, and to provide technical assistance for policy makers to prioritize structural reforms.

The distinguishing feature of the GIH is that it provides the perspective of private capital on infrastructure investment. These private capital include infrastructure equity, infrastructure debt invested in unlisted funds, pension fund, and privately managed infrastructure fund, among others. Views from some sovereign wealth funds are also studied by the GIH. In 2015 there was USD 221 billion invested in deals in infrastructure. However, most of them happened in mature markets and brown fields. In developing countries, the funding for infrastructure projects largely came from the public sector, including MDBs. Therefore, the issue, as mentioned by Mr. Carter, is that public investment as a percentage of GDP is decreasing, and the gap for infrastructure investment is widening.

Public and private sectors need to align for more countries to attract private investment. Both sides need to understand each other better. Therefore, initiatives like the World Bank's Global Infrastructure Forum and GIH's meetings are really important. A well-functioning market and a good investment environment are critical for creating investable infrastructure markets that are aligned with private sector capital. Other important factors that the private sector considers when evaluating a potential investment are government capability, infrastructure market, and public and private financing.

Since the outset, procurement of infrastructure projects has evolved considerably and continues to do so. There is no one-size-fits-all approach; however, patterns of good practice have developed. The important areas of consideration for a private investor include: opportunity costs, bid costs, structuring of the deal, contracts, timetable, and governance.

Private commitment to a new country is driven primarily by the investment environment and government capability both in terms of project pipeline and track record. For governments, they need to apply skillfully the general risk allocation guidelines to the local commercial and financial reality. Ms. Beltran further shared some of past experiences that have led to failure of a project. For structuring: using a template for the process rather than asking if the process and requirements are relevant and required, providing inconsistent or incomplete data that makes it difficult for investors to appraise a deal, and proposing too rigid financial structures like fixed periodic payments that are not linked to operating cash flows or credit rating. For contracts: contract clauses that are too inflexible and/or disregard commercial reality, inflexible pricing unrelated to economic indicators or production costs, and regulatory incentives to build too much capacity ahead of demand which result in costly maintenance and suboptimal unregulated returns.

Furthermore, political leadership is critical to the success of key projects and needs to be factored into timeframes. It is important for project leaders to aligning shareholders' interests through a shared vision and a business plan and an agreement that is designed for the long term.

Jorge Kogan, Senior Advisor at CAF, then presented on PPPs in Latin America.

Latin America needs to invest no less than 5% of the GDP per annum to bridge the infrastructure gap and achieve growth aspirations in the coming decades. Currently, the investment level is less than 3% of GDP, which is much less than the level in the 80s. The need for infrastructure investment from 2011 to 2040 is projected to be between USD 8 to 13 billion. 55% of the total need will come from Brazil and Mexico, and 88% of the total need is going to be concentrated in seven countries.

The private sectors' engagement in infrastructure investment in Latin American countries is high compared to those in developing countries of other regions. About one-third of the investment in infrastructure in Latin America came from the private sector. Going forward, approximately an additional 2% of GDP per year need to be mobilized from the private sector, which amounts to around 100 to 150 million dollars per year.

Many things need to be done to attract more private capital to invest in Latin America infrastructure through PPPs. For example, it is necessary to demonstrate that PPPs create value and are a better option than conventional public investment. Additionally, it is important to understand that PPPs are a means to achieve more and better quality projects that are economically and socially relevant and viable. Successful PPPs projects require improved preparation of portfolio and projects, and more competition from the participants. They should also try to access all funding sources available in the market: national and foreign, multilateral banks, and the capital market through infrastructure bonds or asset securitization, which will require countries to improve their legal and institutional framework to ensure maximum competition in financial markets. On the deal structuring side, it is important for revenues to be adjusted to service provision, and the various risks to be distributed in a more effective and balanced way. Furthermore, it is recommended to have in place regulations on contract changes and conflict resolution. It is also important to promote social support and information transparency.

In conclusion, the critical factors that would contribute to the success of the PPPs include political and social stability, positive economic prospects, stable and reliable legal and regulatory frameworks, professional and independent regulators, political and social support and finally, access to long-term financing.

The first country intervention for the session was delivered by Kenneth Chua, Chief of Staff of the privatization group in the Philippines' Department of Finance.

The Philippines has had a very successful PPP program in the past five years. The goal has been to increase infrastructure investment from 2% of GDP to 5% of GDP, in addition to bringing expertise and execution capability from the private sector to build a high-quality infrastructure network under time constraint. To date, Philippines' infrastructure pipeline already includes 51 projects spanning five years, with a total value of 1615.75 billion PHP.

The factors that contributed to this success include the establishment of a clear legal framework, a central agency to advocate and align interest, a clear governance structure and clarity of roles, a solid policy framework, a robust but fast approval process, and a mechanism to procure advisers to develop projects.

The second country intervention was delivered by Mfundo Hlatshwayo, Director of the National Treasury in South Africa. His presentation focused on sharing experiences of South Africa's renewable energy procurement program in the form of PPP, the Independent Power Producer (IPP) Program.

South Africa is going through a massive infrastructure investment program, which amounts to USD 16 billion per annum for the next three years. With the program the government also hopes to increase the mix of the renewable energy in South Africa. In South Africa's experience, PPP is very important in crowding in private sector resources to meet the country's growing demand for infrastructure. Specifically for the IPP, it comprises three key stakeholders, the government, the procuring entity, and the private sector.

Mr. Hlatshwayo introduced the specifics involved in the structuring, bidding processes. Some of the lessons learned during South Africa's massive renewable energy construction program include the need to adopt a business-friendly approach, to take advantage of external sources of funding, to find a program champion, to make a case for renewable energy when identifying a program, to have a design that suits country circumstance, and to ensure quality procurement and contracting documentation and processes are in place.

In sum, the current program would allow South Africa to procure 4,000 megawatts of renewable energy with investment from private sector amounting to USD 14 billion. Going forward, South Africa plans to diversify further its energy mix.

Session 2: Fiscal Policy and Income Inequality

Session two of the meeting focused on fiscal policy and income inequality. Recent studies document rising inequality in societies around the world, and the impediment to growth this would cause. Fiscal policy has a role in increasing efficiency, improving inclusion and tackling inequality.

Sanjeev Gupta, Deputy Director at the Fiscal Affairs Department of the IMF, opened the session with a presentation that focused on the redistributive role of fiscal policy.

In the last two decades, the world income inequality has been going down. The trend is reflected by the Gini coefficient and the mean income gap between the top 10% and the bottom 10%. Large developing countries have been contributing more to the share of output, further contributing to the decline of world poverty.

However, inequality within countries has been increasing. It has increased in most advanced economies, as well as in some large developing countries. Wealth inequality is significantly more pronounced than income inequality. In a number of countries examined by Mr. Gupta, the wealth Gini on average is twice as much as the income Gini. In countries such as US and Switzerland, the top 10% have about two-thirds of the wealth, and in countries such as Chile, UK, and China, the top 10% have about 50% of the wealth. Furthermore, inequality and inequality of opportunities tend to be related, which has implications for social mobility.

There is now a growing recognition that inequality may have social consequences and has the potential to undermine macro-stability and growth. The IMF addresses these issues to various degrees in their programs of surveillance, lending and capacity building. The work for these issues intensified in the wake of the global financial crisis.

The contribution of fiscal policy to reduce inequality is more pronounced in advanced countries. An analysis of the redistribution role of fiscal policy in some OECD countries has indicated that the countries examined have reduced inequality by one-third, mostly through spending programs. Much of those impacts were channeled through transfers and pensions. The spending programs include in-kind spending that covers education and health, which also have a very effective influence on income distribution.

The contribution of fiscal policy to reducing income inequality is much smaller in developing countries than in advanced countries. This is partly because in advanced countries, on average 35% of GDP could be mobilized for tax revenues, however in many developing countries the ratio of revenues to GDP is much lower at around 15 to 20%. Therefore the ability to pay for the social programs is very limited. Additionally, spending in developing countries is not necessarily directed towards the low-income groups. One example is that of energy subsidies, for which a large percentage of the beneficiaries belong to higher income groups. Countries should design efficient redistributive fiscal policy that is consistent with macroeconomic objectives, carefully designed taking into account indirect and medium-long term effects, as well as administrative capacity. The impact of tax and spending policies should be evaluated jointly.

For developing countries, the reform options to achieve more efficient redistribution of taxation include: implement progressive personal income tax (PIT) rate structures; expand coverage of PIT; more effectively tax multinational corporations; utilize better opportunities for recurrent property taxation; minimize VAT exemptions and special VAT rates; and use specific excises mainly for purposes other than redistribution.

For developing countries, the reform options to achieve more efficient redistribution of spending are as follows: improve access to education for low-income families; expand coverage of publicly financed basic health package; ensure or maintain access of low-income groups to essential health services; expand conditional cash transfer (CCT) programs as administrative capacity improves; increase effective pension retirement age while protecting low-income pensioners; and expand noncontributory means-tested social pensions.

Given the outlined reform options, countries should also consider heterogeneity when designing their own fiscal policies. Because the forms and nature of inequality differ significantly among countries, the administrative capacity, and institutional design will all have impacts on the effectiveness of the policies.

The unemployment rate and Gini coefficient increase during fiscal consolidation, and this is according to a study that looks at 91 episodes across 49 advanced and developing economies between 1945 and 2012. The implication is that tax and expenditure measures should be designed in a way that does not hurt the poor and the low-income groups in the society. In the long term, fiscal policy helps in mitigating the worsening of the market Gini coefficient, according to a study by IMF staff that looks at 27 episodes of fiscal consolidation between 2007 and 2013.

To conclude, fiscal policy is a powerful and adaptable tool for achieving distributional objectives. Improving both distributional outcomes and efficiency is possible. Considering taxes and spending programs together enhances the effectiveness of fiscal redistribution.

Estuardo Moran, Associate Director at the Commitment to Equity (CEQ) Institute, closed the session with a presentation that focused on fiscal policy incidence of poverty and inequality in Latin America. Mr. Moran discussed the following three questions: What is the impact of fiscal policy on inequality and poverty? What is the contribution of direct taxes, and social spending to the overall reduction in inequality? And how pro-poor is spending on education and health?

Mr. Moran stressed the importance of the need to analyze the impact of both tax and spending policies at the same time when evaluating the influence of fiscal policy on inequality. This is because the effect of one policy could be compensated or offset by the other. He also pointed out that the traditional poverty indicators can be misleading when the fiscal system shows a reduction in poverty and yet a substantial share of the poor could have been further impoverished by the combined effects of taxes and transfers.

The policy tools that have equalizing effects based on Mr. Moran's research include cash proportion of the net fiscal system, marginal contribution of direct taxes and direct transfers, and marginal contribution of spending on education and health. The effect of indirect transfers can be hard to determine.

Jomo Sundaram, former Assistant Secretary-General for economic development at UNDESA and former Research Coordinator at the G-24, focused his presentation on inequality at a global level.

About two-thirds of global inequality is due to disparities among countries. This fact has a lot of implications on the potential of fiscal policy to reduce inequality, given that intervention is done at the national level.

At the global level, some of the important drivers of inequalities are: the shift in recent decades from labor incomes to incomes of capital, the effect of globalization, the increasingly financialized world and the disconnect between finance and the real economy, and employment level associated with levels of growth. Looking forward, the recent sharp decline in commodity prices is expected to have a significant implication on the geography of the income distribution. There is increasing recognition that inequality can have much more contradictory effects, and may well slow growth in certain circumstances.

In terms of policy, Mr. Sundaram brought to the forefront a few key issues that need to be considered by participants. He emphasized that economically unproductive and socially regressive government spending is not welfare increasing. The income tax rate in developing countries is still relatively low compared to the advanced countries, and governments should reduce reliance on indirect taxation which worsen inequality. Many developing countries depend heavily on government revenues from tariffs, which affects their ability to deepen trade liberalization. The practices of Base Erosion and Profit Shifting (BEPS) by multinational corporations hurt the tax income of host countries. Global financial regulation could have unintended impact on financial inclusion, noting the unintended consequences of the Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) policies on the cost and ease of money transfers/remittances and the availability of correspondent banking in developing countries.

To conclude, countries should consider the following policies to further enhance fiscal revenue and reduce inequality: further engage in international tax cooperation under the framework of OECD and IMF, avoid the 'race to bottom' tax competition and recognize the need and limits of fiscal policies to address the issue of inequality.

Towards the end of the session, participants discussed issues that require further examination and deliberation in the international community, including: how to support developing countries in building their capacity in tax administration and collection in order to move towards a more effective and progressive tax system, how to balance between offering tax incentives to attract companies and raising tax revenue, and how a global tax system or an international financial system can help to reduce the income and wealth gaps between advanced countries and EMDCs. Participants also asked how fiscal consolidation can be implemented without hurting infrastructure investments, how capital repatriation from the poorest countries to the rich countries can be addressed, and how the IMF can boost their support for countries' efforts to maintain macroeconomic stability and reduce inequality. Finally, there was also acknowledgement that capital flow liberalization could have unintended consequences.

Session 3: Financial Inclusion: Innovations and Challenges Ahead

Financial inclusion is a powerful tool for enhancing inclusive growth, poverty reduction and expanding a country's domestic financial sector. This session focused on technological innovations to advance financial inclusion and the challenges that are posed by international regulations. Presentations comprised an overview of technological advancements in financial inclusion and country experiences promoting financial inclusion.

The first presentation by Pablo Arabéhéty, the regional representative of Latin America and the Caribbean at Consultative Group to Assist the Poor (CGAP), focused on the digital aspect of financial inclusion. To date, there has been two generations of innovation in financial inclusion: the 1st generation which focused on increasing access, efficiency and setting up infrastructure; and the 2nd generation which is focusing on data, personalization and context. The technological advances in the second generation have led to breakthrough innovation in products and services by reducing customer pain points, opening new opportunities for customers, creating more meaningful ties to customers' lives, and easing customer journeys towards formal products and services. An example of such a product is MPESA's MSHWARI, a savings and loan product, which has garnered over 8 million accounts since its launch in 2012. The speaker emphasized that formal services facilitated by financial inclusion need to be better than current available informal services as financial inclusion is a stepping stone into a broader ecosystem of economic sectors such as agriculture, transport, health, energy, and insurance, to name a few.

Maria Ines Agudelo, the Managing Director of FOGAFIN, then presented on financial inclusion and financial education within the realm of deposit insurance in Colombia. Key issues that deposit insurers have to consider include: coverage, membership, mapping insurance to complement safety-nets, creating public awareness of benefits and limitations, and arranging funding. In Colombia, the importance of financial education is recognized at the national level. Its National Strategy on Financial Education involves the cooperation of different stakeholders including the Ministries of Finance and Education, the National Planning Department, a Deposit Insurer, and a Financial Supervisor. The strategy establishes a roadmap to achieve predetermined objectives and provides guidance for individual programs to assist them to efficiently contribute to the national strategy.

Saurabh Vijay, Advisor to the Executive Director at the World Bank, followed with a presentation on India's experience with financial inclusion. The Governor of the Reserve Bank of India has described financial inclusion as a means of 'liberating the poor from dependence on indifferently delivered public services'. As per a 2011 Census, financial coverage in India constituted 58.7% of households, served by 130,000 banking branches and 190,000 ATMs. In 2014, the increasingly successful National Mission on Financial Inclusion (PMJDY) was announced by Prime Minister Modi. PMJDY seeks to provide universal access to banking facilities for all households with at least one Basic Account that includes inbuilt accident insurance, an overdraft facility, a Life Cover and other services. To the beneficiaries, PMJDY has created a platform that inculcates a savings habit, provides financial literacy, and provides formal facilities and freedom from the clutches of usurious money lending. To the economy the program improves and enables growth by bringing savings into the financial system, improves savings to GDP rate, increases digital transactions, and plugs leakages in public subsidies and welfare programs. In 2015 India was recognized by the Guinness World Record for achieving a financial world record for the most bank accounts opened in a week (over 18 million accounts), as part of the financial inclusion campaign.

Mr. Vijay pointed out that there has been an increase in technological products to make this plan possible; including: mobile banking, Micro-ATMs, a National Unified USSD Platform (biometric identification), among others; products that have the potential to cut down costs, enhance convenience and increase the speed of coverage. Subsequently, India also launched an SME financing bank (Mudra) in 2015, with a capital allocation of $3.2 billion and a credit guarantee fund of $480 million. Through the JAM (bank accounts, universal Identification, and mobile phones) trinity platform, the infrastructure is being created to extend the financial inclusion agenda to link with other government programs and subsidies, such as India's large fuel subsidy cash transfer program.

Nigeria's financial inclusion strategy was subsequently presented by Moses Tule, Director in the Monetary Policy Department of the Central Bank of Nigeria. Access to financial services remains a great challenge in Nigeria. In 2010, 46.3% of the population (39.2 million) was without access, with 54% representing women and 80%, individuals residing in rural areas. In 2012, the National Financial Inclusion Strategy was launched with a goal to reduce the percentage of those without access to 20% by 2020. Implementation is coordinated by the Financial Inclusion Secretariat within the Central Bank. The strategy covers a broad range of initiatives to improve payment, savings, credit, insurance, pension and literacy of the capital market. Key partner agencies involved in implementing the strategy include: the National Pension Commission, the Securities and Exchange Commission, the National Insurance Commission, and the Ministry of Communication Technology. A number of challenges currently inhibit progress in financial inclusion; namely, low financial literacy levels, a poor savings culture and poverty, inadequate infrastructure, security concerns, a low risk appetite, inadequate research and data, traditional and religious beliefs, and balancing the social and commercial viability for serving the unbanked segment. However, the prospects for financial inclusion are also numerous, including: reducing income inequality, building household assets, stimulating micro-enterprise and job creation, among others.

The session was rounded off by Michelle Durham-Kission, Advisor to the Executive Director at the World Bank, with a presentation on the impact of de-risking in the Caribbean. The Caribbean is experiencing a decline in financial services resulting from an exodus of correspondent banks in the US and major banking centers in Europe that were doing business with indigenous banks and banks in the offshore sector of the region. The Caribbean Association of Banks (CAB), assisted by a committee of finance ministers, was tasked by the region's heads of governments to find a solution to this problem. Out of 22 respondents in a survey launched by the CAB, 77% rely on one correspondent bank, increasing the vulnerability of the region. Jamaica's Money Service Businesses have been affected as a leading local bank no longer accepts foreign instruments and remittances from some MSBs. The Bahamas, Cayman Islands and Turks and Caicas have also lost their intensive business in money transfers and all 7 local banks in Haiti have experienced terminations or restrictions in service.

The labeling of the region as a high risk area has contributed to this problem. Fifteen Caribbean countries were blacklisted by the EU as non-cooperative jurisdictions, despite the region being evaluated as fully or largely compliant by the Global Forum on Tax Transparency and Exchange of Tax Information. A study carried out by the World Bank at the request of the Financial Stability Board establishes that about 50% of banking authorities and slightly more local and regional banks indicate a decline in correspondent banking relationships (CBRs). The Caribbean is the most severely affected region with the US being the most mentioned home for correspondent banks withdrawing from foreign CBRs. The most affected services and products include: check clearing, clearing and settlement, cash-management services, international wire transfers, and trade finance. An appointed Committee of Ministers of Finance on Correspondent Banking chaired by the Prime Minister and Minister of Finance in Antigua and Barbuda have been charged with the responsibility of representing the interest of the region at the United Nations, World Trade Organization and the United States Congress, to create greater international awareness of the challenge confronting the region.

Session 4: A dialogue on Reinvigorating Growth

The global economy is facing significant transitions. Growth in emerging markets and developing countries (EMDCs) is moderating, albeit at different paces. The macroeconomic environment presents challenges but also opportunities for countries to explore new sources of growth at this critical juncture. It has therefore become necessary for emerging and developing countries to identify potential areas for action to stimulate growth.

The keynote speaker of the TGM, Danny Leipziger, Managing Director at the Growth Dialogue, opened this session with a presentation on a big picture perspective of current global challenges and global solutions. There is a broad consensus that the global economy hangs in the balance. From 2009 to 2016, OECD countries have broadly underperformed: their output gaps, or the difference between potential and actual output, have persisted, and the consequent loss to world GDP is estimated to be about $7.6 trillion. Recent growth in developing countries has also been declining. Existing global stimulus will not deliver the necessary punch to boost global recovery: advanced economies' fiscal conditions have deteriorated, while the scope for monetary easing is reaching its limits and investment broadly is weak despite historically low interest rates. Consumption of households is affected by declines in asset prices and levels of confidence. The elements of the growth story include a capital stock that is not growing amid low growth and disruptive technologies, total factor productivity that has been near zero since 2012, and labor markets that face low employment elasticities and job displacement. Furthermore, in many countries, dependency ratios are falling, and inequality is rising. For example, there are high risk of setbacks for the new middle-class in Latin America and more urban poverty in Sub-Saharan Africa. The middle class in some advanced economies like the US is also shrinking.

Looking forward, EMDC's growth strategies will need to cope with weak global growth drivers, uncertainty from new financial crises, the need to improve resource allocation, and managing the social and political impact of gaps between public expectations and the ability of governments to deliver. In this context, EMDCs face five major challenges; namely, managing instability in capital flows and exchange rates, and building resilience; reducing inefficiencies such as wasted subsidies and poor logistics; shifting resources to higher productive sectors and becoming more competitive; reducing mandated government spending to favor higher investment levels and productivity; and preserving income gains of the working poor.

Mr. Leipziger further highlighted the growing challenge of urbanization globally as people continue moving towards cities. Development challenges in Africa and South Asia can't be solved without effective urban strategies linked to national strategies. Dealing effectively with climate change will require dealing with carbon emissions in cities. In Africa urbanization poses a very important challenge as populations are becoming urbanized but are not escaping poverty. There is a clear two-way causation between urbanization and GDP per capita, and increases in urban growth will be in intermediate-sized cities. Against this backdrop, there is a need to redefine effective growth strategies; effectively use public policy to address unemployment and inequality; link national development policies with smart city strategies beyond mega-cities; see urban approaches as central to achieving climate change; and see sustainable and shared growth as goals that can be met despite current global challenges.

Mr. Leipziger ended his presentation with a number of key questions for the audience. For example, does the new global reality imply the need for new growth strategies? What are the immediate dangers faced by policy makers in a prolonged economic slowdown? Are there policies that are both pro-growth and pro-equity, if so how can they be implemented? And lastly, how can EMDCs effectively tap into liquidity pools to finance needed infrastructure investments?

Guillermo Perry, visiting professor at UNIANDES and former Minister of Finance in Colombia, followed with a presentation on how these global challenges and opportunities are playing out in Latin America . Latin America is experiencing the end of a decade of high growth, along with the rest of the world. The slowdown in economic growth in emerging markets is particularly acute for Latin America and within the region more pronounced for South America. Mr. Perry noted that the leading cause for a decline in growth has been the sharp fall in commodity prices, but that differences in growth across countries are not only explained by this factor. The rise and fall of commodity prices, and the consequent changes in terms of trade, have had different impacts across Latin America countries. For instance, Venezuela and Argentina lost reserves well before the recent fall in commodity prices while Brazil's decline in reserves started in 2013 and for Colombia, mid 2015.

Overall investment rates in Latin America have declined in recent years. Additionally, capital inflows have diminished, which has led to exchange rate depreciations across the region. The exchange rate adjustments helped boost industrial activity that had suffered during the period of currency appreciation, but devaluations have also brought inflationary pressures. In adjusting to these new realities, countries with stronger fiscal positions like Chile and Peru have been faring better while others may see their growth affected by fiscal adjustments. Other risks for the region include: unexpected effects of monetary normalization in the U.S., deepening of present economic woes in China, and the protracted weak recovery in Europe.

Mr. Perry emphasizes that the long term challenge for the region is increasing productivity. In this regards, he highlights the importance of a micro agenda, whose elements could vary by country and that could include increasing the quality of education, stimulating innovation, increasing flexibility in labor markets, enhancing trade, overcoming transport infrastructure lags, improving SME access to finance, and reducing the cost of doing business. Overall, amidst these development challenges, there is cause for a positive forward look for the region. He notes the emergence of a large middle class and an overall reduction in poverty levels. The region has experienced increased resilience to financial crises and stronger macro-financial frameworks than in the past. There also are encouraging trade agreements on the table.

The session was brought to a close with a presentation on Sri Lanka's experience on reinvigorating growth delivered by Swarna Gunaratne, Alternate Executive Director at the IMF. The Sri Lankan economy experienced an annual contraction in growth of about 1-2% due to violence and terror in the North and East of the country from 1980-2009. In the post-conflict period of 2009-2015, the country experienced accelerated growth with an average of 7%. Many initiatives led to this growth, including: disbursement of bank loans at concessionary rates; massive infrastructure investments in road developments, power, port and airport projects; and an uptake in the tourism industry. Growth has been accompanied by improvement in Human Development Indicators, lowering of the unemployment rate below 5% over the past couple of years, and an improvement in the poverty head count ratio which currently stands at 6.5%.

It is also notable that the composition of Sri Lanka's GDP has changed over the past 40 years with a marked expansion in the services and industrial sectors. Exports have been diversified from primarily agricultural products to industrial products. There are however still a number of issues that need to be addressed in Sri Lanka, namely: increasing infrastructure investment, enhancing financial inclusion, addressing an aging population and low labor productivity, increasing accessibility to higher education, increasing export growth, and expanding the tax base.

Ms. Gunaratne pointed out that in addition to domestic policies required to address these issues, international support is also essential in bridging the resource gap for technological advancement, emphasizing the importance of the G-24 forum in raising the voice of developing countries and the group within international fora.

At the end of the session, participants raised a number of questions and concerns regarding future growth prospects. For example, how can EMDCs achieve and sustain inclusive growth amidst the need for fiscal adjustments? What are international financial institutions, like the IMF, doing differently to address the new forms of crises in the global economy? What are the implications of increasing inequality in advanced economies on developing countries; could income inequality be a source of new forms of crises in the future? Given current interest in the formation of trade blocs, how can countries left out of such partnerships do to boost trade and reinvigorate growth? Concern was voiced regarding the potential impact on credit availability of policies implemented to address the 2008 financial crisis. Given the importance of global trends and policy spillovers, participants emphasized the importance of enhancing the voice of developing countries in international fora such as the G20.

Ms. Ana Milena López, Director of Public Credit of Ministry of Finance Colombia delivered the closing remarks.