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From the Washington Consensus to the Wall Street Consensus

The financialization initiative of the World Bank and multilateral development banks

By Rick Rowden

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Infrastructure, USA
The image shows an abandoned airport and its leftover infrastructure in Austin, Texas. Photo by Beth Wilson taken on June 4, 2007

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EXECUTIVE SUMMARY

This paper reviews the recent initiative being led by the G20 countries and their respective development finance institutions (DFIs), including the major multilateral development banks (MDBs), for the financialization of development lending that is based on the stepped-up use of securitization markets. It describes the key elements of the new initiative – specifically how securitization markets work and how the effort is designed to greatly increase the amount financing available for projects in developing countries by attracting new streams of private investment from private capital markets. The paper introduces the basic logic underpinning the initiative: to leverage the MDBs' current USD 150 billion in annual public development lending into literally USD trillions for new development finance. In fact, the World Bank had initially called the initiative "From Billions to Trillions," before finally calling it, "Maximizing Finance for Development" (MFD) (World Bank 2015; MFD 2019).

While securitization can be useful for individual investors and borrowers under certain circumstances, the proposal to use securitization markets to finance international development projects in developing countries raises a set of major concerns. The paper lists 7 important ways in which the G20-DFI initiative introduces a wide range of new risks to the financial systems in developing countries while undermining autonomous efforts at national economic development. The 7 risks of securitization are:

1. the inherent risk because securitization relies on the use of the "shadow banking" system that is based on over-leveraged, high-risk investments that are largely unregulated and not backed by governments during financial crises;
2. the extensive use of public-private partnerships (PPPs), despite the poor track record of PPPs, many of which have ended up costing taxpayers as much if not more than if the investments had been undertaken with traditional public financing;
3. the degree of proposed deregulation reforms in the domestic financial sector required of developing countries would undermine the ability of "developmental states" to regulate finance in favor of national economic development;
4. the degree of financial deregulation required would also undermine sovereignty by making the national economy increasingly dependent on short-term flows from global private capital markets and thereby undermine the sovereign power of governments and their autonomous control of the domestic economy;
5. the uncertainty relating to governance and accountability for the environmental, social and governance (ESG) standards associated with development projects. Such accountability has been fixed to traditional forms of public MDB financing for development project loans, but as future ownership of assets is commercialized and financialized, fiduciary obligations to investors may override obligations to enforce ESG implementation;
6. the deepening of the domestic financial sectors in developing countries, as required

by the initiative, can create vulnerability as the size of the financial sector grows relative to that of the real sector within economies; and

7. the privatization and commercialization of public services, including infrastructure services, as called for by the initiative, has faced a growing backlash as reflected by the global trend of remunicipalizations. The fact that the securitization initiative is being promoted in such a high profile way by the G20 and leading DFIs despite all of these risks reflects an intensified contest between those supporting the public interest and those supporting the private interest.

The paper also documents the relatively minor degree of interest expressed so far by global financial markets in the initiative, suggesting it is not likely to galvanize the trillions of dollars claimed by its proponents.

It concludes by reviewing the arguments for the scaled up use of traditional public financing mechanisms and several of the important ways in which this can be done, including steps that could be taken by G20 countries, DFIs and governments.

ABBREVIATIONS

ABS	Asset-backed security
AfDB	African Development Bank
AIIB	Asian Infrastructure Investment Bank
AUM	Assets under management
BIS	Bank for International Settlements
CDO	Collateralized debt obligations
CSO	Civil society organization
DFIs	Development finance institutions
ESG	Environmental, Social, and Governance
FfD	UN Financing for Development
FSB	Financial Stability Board
IFC	International Finance Corporation
IMF	International Monetary Fund
LICs	Low-income countries
MDBs	Multilateral development banks
MFD	Maximising Finance for Development
MICs	Middle-income countries
NDB	New Development Bank
PPP	Public-private partnership
SIVs	Structured investment vehicles
SPV	Special Purpose Vehicle
SDGs	UN Sustainability Development Goals
WBG	World Bank Group
WTO	World Trade Organization

1. INTRODUCTION

In 2015, the international community officially adopted the Sustainable Development Goals (SDGs) at the United Nations. The goals seek to engage all governments in efforts to reduce poverty, address climate change and promote sustainable development by 2030. The same year, governments met in Addis Ababa, Ethiopia at a United Nations Financing for Development (FfD) conference to identify ways to finance the efforts to achieve the SDGs. Confronted with daunting projections of trillions of dollars needed to finance the goals, governments agreed that the public sector would not be able to meet all of the financing needs and therefore a major new role for involving private sector finance was needed.

The 2015 Addis Ababa Action Agenda established the Global Infrastructure Forum, led by the multilateral development banks (MDBs) and the United Nations. In 2017, the forum promoted the adoption of securitization as the new financing model for MDB infrastructure projects.

The FfD Action Agenda was buttressed by the 2015 adoption by 7 MDBs and the International Monetary Fund (IMF) of the "billions to Trillions" strategy, which seeks to deploy billions of dollars of public resources to mobilize trillions in private finance – ostensibly to achieve the SDGs. Long before 2015, however, many MDBs and development finance institutions (DFIs) had been increasingly experimenting with various types of financial engineering to create "blended finance" mechanisms designed to leverage finance from capital markets and use public money in innovative ways to pilot new instruments and reduce risks for private investors.

Some of these experiments with blended finance involve new mechanisms for using public aid to provide advanced purchase agreements, public loan guarantees, interest rate subsidies, risk insurance, various performance incentives and matching funds in order to leverage larger amounts of capital from private investors. Public resources have also been used in creative ways to provide technical assistance and to cover transaction and project preparation costs. One example is the rapid development by national development banks and MDBs of the green bonds market, which requires the proceeds of the bond issues to be directed into environmentally-friendly investments. Other examples of recent blended finance instruments that combine public resources and private capital include health sector financing bonds and "catastrophe bonds" for insurance against health emergencies and natural disasters (Hurley 2017; Kapoor 2019; Allen 2019).

This report describes the "Billions to Trillions" initiative of the Group of 20 (G20) and DFIs to transform the international system of development finance away from its traditional basis on public financing towards a new model based on attracting private financing from global capital markets. The initiative is being championed by a broad group of countries in the Global South and North within the G20 and the major MDBs. Leading MDBs include the World Bank Group, the African Development Bank, and the Asian Infrastructure Investment Bank, which are part of an international network of dozens of development finance institutions (DFIs).

The basic idea is to organize the disparate group of public DFIs that currently give grants, loans, and guarantees – as well as provide equity – for development projects in developing countries into a larger and more efficient collective that can pool funding and resources and improve coordination. In addition, as mentioned above, the initiative calls for stepping up the use of innovative financial engineering, particularly the use of securitization markets, to draw in vast new amounts of private investment from global capital markets to finance development projects in developing countries.

The main claim being made by the G20 and others is that, rather than giving support (e.g., grants, loans and guarantees) to developing countries in the traditional way with public-to-public transfers, the DFIs in general and the MDBs specifically can make much better use of their public resources by using them to lower the risk for private investors in capital markets who could then provide much higher levels of private financing for development operations. Proponents claim that this approach would mobilize far more investment capital and lower borrowing costs for developing countries. This is how the G20 and DFIs are seeking to fill the financing gap needed to achieve the SDGs by 2030.

Box 1. The Launch of Financialization Strategies: Key Documents

- G20 Hamburg Principles (2017)
- G20 Roadmap to Infrastructure as an Asset Class
- G20/OECD/WB (2018) Stocktake of Tools and Instruments Related to Infrastructure as an Asset Class – Progress Report
- World Bank Group et al. (2015) From Billions to Trillions: Transforming Development Finance Post-2015 Financing For Development; Multilateral Development Finance
- World Bank Group (2017) Maximizing Finance for Development: Leveraging the Private Sector for Growth and Sustainable Development
- World Bank Group (2018) Forward Look: A Vision For The World Bank Group in 2030 Implementation Update
- Asian Infrastructure Investment Bank (2018) Strategy on Mobilizing Private Capital For Infrastructure

At the heart of the initiative is the goal of greatly scaling-up the use of securitization markets, which are used for lowering, spreading and transforming risk for investors. The idea is to blend finance that the DFIs provide to developing countries with private finance and then repackage it into a new type of asset class of tradeable securities that are bought, sold and traded by institutional investors – especially sovereign wealth funds, pension and insurance funds. The securities could also be held and used as collateral for obtaining additional financing.

While sovereign wealth, pension and insurance funds in the advanced economies currently hold trillions of dollars in investment capital (over USD 100 trillion), they have traditionally been reluctant to invest in development projects in developing countries because of the perceived high risk. Therefore, the goal of the G20-DFI initiative is to use a combination of the pooled finance, the MDBs' Triple A credit ratings, and instruments such as public loan guarantees and subsidies to effectively "de-risk" portfolios of investment projects – thus, making them "bankable" or more attractive to institutional investors. This de-risking process is central to the initiative. With the diminished degree of perceived risk for private investors, borrowing costs are projected to be lower for developing countries while the amount of financing available for development projects in developing countries is projected to greatly increase.

The initiative focuses on the infrastructure sectors as a first priority, in which a new asset class of securities based on project investments is being established. These new securities enable investors to invest directly in infrastructure projects or indirectly through infrastructure-related funds and companies. Financial engineering enables project financing to be split apart into different investments with varying degrees of risk that can cater to a variety of different types of investors with different appetites for risk, thus increasing the overall number of investor participation. This splits apart the higher risk activities (e.g., construction) from the lower risk parts of the project (e.g., operations and maintenance). It is argued that securitization markets will enable higher-risk investors the opportunity to exit after a project's construction phase is completed and have their place taken by other institutional investors not inclined to take on construction risk (Humphrey 2018a). The initiative would transform the decades-old model based on public financing into a new model based on private capital markets. Or, in other words, the MDBs and DFIs "must evolve from lenders to mobilizers of private finance for development" (Lee 2018).

To rationalize the dramatic nature of the required overhaul of the development finance system, advocates of the G20-DFI initiative often point to the gargantuan estimates of trillions of dollars of development finance that are projected to be needed for the world to achieve the SDGs by 2030, with nearly USD 7 trillion projected to meet infrastructure needs alone. Then they argue that the public sector will not be able to finance all of this, so new ways must be found to lure in private capital and the use of securitization markets is the best way to do this.

The political backdrop to this far-reaching initiative is the emergence of the China Development Bank, the Chinese Export-Import Bank and other Chinese development banks as major sources of overseas aid and investment in developing countries over the last decade. In addition, new MDBs such as the Asian Infrastructure Investment Bank (AIIB) led by China and the New Development Bank (NDB), led by the BRICS countries, have become important new sources of development finance. In response, the historically dominant, western-led MDBs are today feeling compelled to catch-up with China in the intensifying competition for markets and natural resources in the developing world. And within this context, both western-led and China-led institutions have been stepping up their use of market-based financing mechanisms.

For example, the Beijing-based AIIB recently established a USD 500 million fund that will hold a diversified portfolio of bonds from corporate issuers in the emerging and frontier markets of Asia to finance infrastructure investments. The fund is designed to promote infrastructure as an asset class and develop capital markets for infrastructure in the region (Sender 2019). Within China, securitization markets have greatly expanded in recent years, and the China Development Bank and China's other DFIs, known as "policy banks", have stepped up the use of securities comprised of bundled infrastructure loans (Shen and Ruwitch 2017).

In many respects the G20-DFI initiative to scale up the use of securitization markets reflects a competitive response to the growing use of these markets by the China-led DFIs.

At stake is not just providing development finance to developing countries, but the question of how much geopolitical influence accrues to which lenders (Hillman 2019). And as both the western-led and China-led MDBs have been experimenting with various forms of blended finance lending instruments and securities in recent years, this competition will no longer play out in the realm of public resources, but increasingly in the realm of securitization markets. In this regard, the ambitious initiative may signify that the western-led MDBs intend to increase their coordination and collaboration in efforts to draw-in vast new sources of private capital in order to better compete against China's rising influence in the arena of development finance.

At the same time, however, there are interesting examples of the western-led and China-led MDBs both competing against one another while cooperating among one another at the same time. For example, there has been an increase in joint-lending initiatives and collaboration and coordination in lending between the western-led and China-led MDBs, such as by the World Bank and the AIIB (nearly half of AIIB's total loans distributed so far have been coordinated jointly with the World Bank and others). Yet both are seeking to expand their use of securitization markets.

Box 2. The MDBs and DFIs

The term development finance institutions (DFIs) refers to all public institutions which provide development financing for projects in developing countries. They provide funds for development projects that would typically not be able to get funds from commercial lenders. DFIs provide financial support (loan and/or equity) to the public sector, or directly to private sector companies; some are export credit agencies (which may not have any development mandate), etc. Below are examples of various types of bilateral, regional and international DFIs. Many of the regional DFIs are multilateral organizations and are commonly known as the multilateral development banks (MDBs). While some DFIs are only local or national in scope, such as community development banks or national development banks, this paper is primarily concerned with DFIs and MDBs which provide international development financing.

Bilateral

UK: CDC Group plc
France: Proparco
Netherlands: Netherlands Development Finance Company (FMO)
Germany: KfW Development Group; Deutsche Investitions- und Entwicklungsgesellschaft mbH (DEG)
Sweden: Swedfund
Norway: Norfund
US: Overseas Private Investment Corporation (OPIC)
Japan: Japan Bank for International Cooperation (JBIC)
Canada: Export Development Canada (EDC)
Spain: Compañía Española de Financiación del Desarrollo (COFIDES)

Regional

African Development Bank (AfDB)
Asian Development Bank (ADB)
Asian Infrastructure Investment Bank (AIIB)
European Investment Bank Group (EIB)
European Bank for Reconstruction and Development (EBRD)
Inter-American Development Bank Group (IDBG)
Islamic Development Bank (IsDB)
New Development Bank (NDB) (“BRICS Bank”)

International

World Bank Group - International Finance Corporation (IFC)
World Bank Group - Multilateral Investment Guarantee Agency (MIGA)

2. BACKGROUND

2.1 Securitization and market-based finance ("shadow banking")

This section describes the process of securitization, what it does and how it works, since this process is at the heart of the G20-DFI initiative. In order to run smoothly, securitization markets require high levels of liquidity in financial markets, which means that short-term buyers and sellers need to be able to raise financing, purchase assets and sell assets with speed and ease. Particularly at issue is the need for investors and traders to transform illiquid (hard to sell) assets into liquid (easy to sell) assets, at least temporarily, in order to facilitate a range of other investment activities. This is where the transformative function of the "shadow banking" sector comes in. Shadow banks, or "non-financial banking institutions," use financial innovation to develop new instruments that enable investors to perform various types of financial acrobatics, like financing long-term investments by constantly rolling over short-term debt and repeatedly re-using the same collateral for financing multiple investments simultaneously.

Box 3. Understanding Securitization

The simplest way to understand securitization is to think about a loan that is scheduled to be repaid in installment payments over long periods of time, such as a home loan, a student loan or a business loan. The loan, or contract between a lender and borrower, is a thing of value because it represents a claim on a future stream of revenue that will be forthcoming. Because the loan is a thing of value, it can be considered an asset that can be bought, sold, traded and even used as collateral for obtaining new financing for other investments. Furthermore, a single asset can be divided into multiple assets that can each be bought, sold or traded according to different degrees or risk and reward for investors. Securitization is this process of taking loans, equity and loan guarantees and transforming them into such tradeable assets in these and other ways.

The process of securitization dismantles the original creditor–debtor relationship by transforming traditionally illiquid and immobile contracts, such as home mortgages or student loans, into liquid or mobile contracts that can then be bought, sold and traded quickly and easily through a vast array of intermediaries and ultimately involve a wide array of other creditors and debtors, each holding claims on multiple pieces of assets with maturities that range across different lengths of time, rates of interest and degrees of leverage involved. So, whereas the original debtor had one creditor, one rate of interest and one period of time over which to repay the loan, securitization transforms the relationship so that now one debtor can have multiple creditors, who are constantly shifting in and out, with multiple interest rates and multiple periods of time for repayment.

Because one loan by itself is often too small to function as a security, investors bundle together a large group of loans (contracts representing future revenue streams from their scheduled repayments) and turn this bundle into a security, or what is called an "asset-backed security" because it is based on the underlying loans which are assets. Then this security can be traded or sold-off completely to other investors and traders (true sale securitization) or it can be used in innovative ways to serve as collateral for obtaining new loans and credit for financing other unrelated investments.

So what the G20 and the MDBs have in mind is to use bundles of MDB loans and repackage them as asset-backed securities. The MDB project loans are for development projects for building roads, bridges, hospitals or some other assets that will hold value in the future. These securities would then be managed by asset-backed securities trusts, which could use them as collateral for obtaining new loans and credit with which to make other unrelated investments (i.e., typically for purchasing and selling corporate bonds, etc.). With the profits generated by these other investments, one idea is that the asset-backed securities trust would be able to pay back the MDBs for their loans early, far ahead of schedule, making these loans appear as though they have been fully repaid on the MDBs' balance sheets, and thus making those loan dollars then available for making new rounds of MDB loans to new developing countries. Other uses involve using public financing and loan guarantees to lower the level of risk of the loans so that the MDBs are then required to hold fewer reserves on hand and can thus free reserves for use in new additional lending. Still other uses include re-using the same collateral for multiple investments many times over (rehypothecation), dividing the security into different tranches with different risk profiles targeted at different categories of investors, and selling off the securities to new investors altogether. In this regard, the G20-DFI initiative envisions constantly using and re-using these recycled MDB resources and profits generated by other investments, and thereby vastly multiplying the lending firepower of each MDB dollar. Herein lays the alchemy of "securitization" – and the claims to be able to turn Billions into Trillions.

There are two basic types of securitizations: the more common "true sale securitization" and the increasingly popular "synthetic securitization". For the G20 and the MDBs, one of the ways true sale securitizations could work would involve transferring legal ownership of the bundle of MDB loans to an external Special Purpose Vehicle (SPV) that would turn it into a security and place it in an asset-backed security trust. The trust would then use it as collateral for issuing bonds to sell to investors. The interest ("coupon") paid to bond investors would come from the stream of scheduled repayments of the underlying MDB loans by the original borrowers in developing countries. The asset-backed security trust would profit from the difference between the higher interest from the MDB loans to borrowing countries and the lower interest paid to bond investors.

In contrast, if the MDBs were to use synthetic securitizations, they would actually retain legal ownership of the loans on their balance sheets but transfer only a portion of the credit risk of the bundled loans. Under this approach, the MDBs would provide a loan guarantee (or credit derivative) that reduces the level of risk of the loans, which in turn would reduce the amount of capital reserves that the MDBs are required to have on hand. As their level of capital requirements is reduced, this would free up resources that would become available for making new loans to more countries while still keeping the MDBs within their capital adequacy limits, thus also increasing the lending power of each MDB dollar. Investors would be paid for their loan guarantees via a fee from the MDBs (the originator), which would be financed by the repayments of the underlying MDBs loans by the original borrowers in developing countries (Kaya 2017; Humphrey 2018b).

For example, in September 2018, the African Development Bank marked the first major use of a synthetic securitization by an MDB when it arranged a deal to transfer the risk embedded in USD 1 billion in loans already made by the AfDB to a group of investors, for a fee. The de-risking element provided by the synthetic securitization, named Room2Run, freed up space for the AfDB to make USD 650 million more in new loans, without requiring further capital increases from its shareholders. In other words, synthetic securitizations function like an insurance policy provided by investors on a chunk of AfDB loans. The insurance lowers the risk, which reduces MDBs' capital requirements, and thus frees up additional resources for lending (Humphrey 2018b).

Levine (2017) and Gabor (2018a) described the transformative functions of shadow banking institutions as those which "issue short-dated, information-insensitive, money-like debt claims and use the proceeds to buy longer-dated risky assets – and doing the core maturity-transformation and risk-transformation functions of banking – but outside of a bank."

The major function of shadow banks is to serve as intermediaries by bringing together potential investors (those who have money to lend) with potential borrowers. So, for example, rather than going to a regular bank for a business loan, a corporation may go through a shadow banking institution to borrow funds more easily available or under more flexible terms which have come from pension funds or insurance companies looking to make new investments. On the other end is an investor who wishes to make higher rates of return than those offered by the regulated banking sector. The shadow institutions provide an array of new investment vehicles that can be structured to offer maximum flexibility for both parties, including opportunities for higher risk/reward scenarios. For providing this service of connecting the two parties and managing the investment structures, the shadow banking institutions earn fees and commissions, or profit from the difference in interest rates between what they pay the investors and what they receive from the borrowers (Noeth and Sengupta 2011).

Box 4. What is the Shadow Banking System?

"The shadow banking system is the group of financial intermediaries facilitating the creation of credit across the global financial system but whose members are not subject to regulatory oversight. The shadow banking system also refers to unregulated activities by regulated institutions. Examples of intermediaries not subject to regulation include hedge funds, unlisted derivatives and other unlisted instruments, while examples of unregulated activities by regulated institutions include credit default swaps" (Chappelow 2019).

The Bank for International Settlements (BIS) has described the structure of the shadow banking system in the following way: "With the development of the originate-to-distribute model, banks and other lenders are able to extend loans to borrowers and then to package those loans into asset-backed securities, collateralized debt obligations, asset-backed commercial paper (ABCP) and structured investment vehicles. These packaged securities are then sliced into various tranches, with the highly rated tranches going to the more risk-averse investors and the subordinate tranches going to the more adventurous investors" (Hannoun 2008). So an original investment with certain degree of risk is transformed into many little different investments each with different degrees of risk that appeal to different groups of investors, making the original investment "de-risked" and the financing more affordable for the borrower.

The shadow banks also provide the maturity-transformation function that would enable long-term institutional investors, such as pension and insurance funds and sovereign wealth funds, to invest in infrastructure projects (in which contracts may govern projects for 25-40 years) while using capital from investors with short-term horizons, such as hedge funds and private equity funds.

In other words, the shadow banking sector is a like a second-tier banking system which provides a wider array of creative financing mechanisms that are not available in the regular banking system, but these mechanisms are not regulated nor backed up by federal deposit insurance.

Although there is not yet a universally accepted definition of exactly which institutions comprise the shadow banking sector, it is often considered to include a range of various complex legal entities such as: hedge funds, structured investment vehicles, credit investment funds, exchange-traded funds, credit hedge funds, private equity funds, securities broker dealers, credit insurance providers, securitization and finance companies, special purpose entity conduits , repurchase agreement ("repo") markets and other non-bank financial institutions (Pozsar et al 2012; Jones 2013).

While providing similar functions as regular banks (i.e. providing credit), shadow banking institutions are very different from regular banks. Shadow banks typically do not have banking licenses so do not take deposits like normal banks, and therefore they are not subject to the same oversight regulations as regular banks. However, as with regular banks, shadow banks are financial intermediaries which provide credit to borrowers and generally contribute to increasing the amount of liquidity of the financial sector (but without using regular bank deposits).

Some view the term "shadow banking" as pejorative and instead prefer the term "market-based finance." But the term "shadow banking" is more useful for two reasons: it clarifies that the institutions are shadowy because they are broadly unregulated with minimal government oversight over the degrees of leverage and risk they are generating in the financial system; and it clarifies the shadowy nature of their investment instruments and products which are so complex and opaque that investors and regulators are unable to accurately assess their risk. So from a macro-prudential and regulatory perspective, their activities and probable impacts on financial fragility are "in the shadows," so to speak.

At present, the world's major shadow banking institutions operate primarily across the American, European, and Chinese financial sectors, and in tax havens worldwide (Bouveret 2011; Boesler 2012; Martin 2012). But now the initiative of the G20 and DFIs would vastly expand their operations into the financial sectors of developing countries in order to facilitate the development of securitization markets to scale up resources for development finance.

Box 5."Repo Markets"

In order to run smoothly, the shadow banks rely on having sufficient liquidity in financial markets – or the ability of investors and traders to raise financing and buy and sell assets quickly and easily. Repurchasing markets ("repo markets") are one of the most important markets used for generating such liquidity. Unlike regular banks, which use deposits to supply credit to borrowers, shadow banks rely on short-term funding provided by the repo market.

In the simplest sense, repo markets enable owners of assets to temporarily sell financial assets (turn them into cash) for a short period of time and use the cash for anything else while maintaining the right to repurchase those same assets at a future time and at a set price, hence the name "repurchasing agreement market". At the same time, the repo market also enables others to temporarily purchase assets, quickly use them as collateral for obtaining new financing for other investments, and then re-sell the assets back to the original owner at an agreed time and price. In other words, investors are able to temporarily purchase an asset; use it as collateral for obtaining other new financing for something else; and then sell it back to the original owner. Therefore, repo markets basically offer one of the key transformational functions in finance – they enable investors to temporarily turn normally illiquid (hard to sell) assets into very liquid assets and allow others to temporarily own assets as a very quick way of obtaining credit before selling them back to their original owners: both activities by these short-term buyers and sellers thereby generate increased liquidity in financial markets – the very liquidity upon which securitization markets depend.

However, by enabling investors to finance long-term illiquid and risky investments through a constant series of short-term borrowing in repo markets, often with high degrees of leverage involved, shadow banking institutions introduce greater fragility and risk into financial markets. The danger of such fragile arrangements is that any disruptions in short-term credit markets could quickly make such investments subject to rapid deleveraging and force investors to quickly sell their long-term assets at huge losses that could be destabilizing to financial markets (Geithner 2008).

2.2 Launching the initiative for securitization of development finance

At the July 2017 G20 summit in Hamburg, Germany, the G20 member countries and the MDBs adopted the Hamburg Principles on Crowding-in Private Finance. The principles reaffirmed the commitment of G20 member countries and the MDBs to "foster effective approaches to maximize the mobilization and catalyzation of private sector resources to support countries with the implementation of the 2030 Agenda for Sustainable Development – including through financial and management resources and innovation." This means the new plan will be based on exploiting leverage in securitization markets and repo and derivatives markets. The principles provide a common framework among the MDBs and new measurements by which to quantify their success in "crowding-in" private capital into future development financing going forward.

For example, the G20 countries have each set a target of achieving a 25-35 percent increase in private capital mobilization for MDB projects over the next 3 years (Hamburg Principles 2017). Similarly, the New Partnership for Africa's Development launched its "5% Agenda" – a campaign to increase the allocations of African asset owners to African infrastructure from its current level of 1.5 percent of their assets under management to 5 percent (PIDA 2018). The OECD's Development Assistance Committee has also weighed in on the issue of how to count so-called Private Sector Instruments (subsidies to the private sector) within overseas development assistance as a new type of foreign aid, despite concerns raised about the dilution of traditional definitions (Meeks 2019; Postel 2018; Atwood, Manning, and Riegler 2018).

This G20 effort to prioritize the use of securitization markets for financing new infrastructure development projects is presented in a paper titled, "Roadmap for developing infrastructure investment as a new asset class." Notably, the G20 countries are the ones which hold the dominant shares of votes on the executive boards of the World Bank and the other MDBs. The G20 paper proposes a roadmap of steps to take for getting the broader set of MDBs and DFIs to work more closely together as a larger lending collective, and for a streamlining process that would coordinate future lending across the institutions.

The G20 Roadmap also includes steps for standardizing the financial funding contracts for future infrastructure lending across all the MDBs. This standardization in project design, preparation, financing and implementation across the MDBs would be established by developing comparable covenants and legal enforcement principles. These steps, according to the G20, would improve these phases of the infrastructure project life-cycle, and enable the MDBs as a group to build a pipeline of much larger "bankable projects" that could be more readily bundled into the new asset-backed securities that would be attractive to investors (G20 2017).

The G20 Roadmap also calls for bridging the gaps in necessary data for investors to better assess the risks of projects, the allocation of risks and risk mitigation steps needed to make the investments more appealing to investors. The Roadmap also calls on developing countries to deregulate their financial sectors in order to encourage greater portfolio flows and to enable the establishment of shadow banking markets required to generate the short-term liquid secondary markets needed to facilitate securities trading.

Several of the major MDBs are planning to collaborate on the new G20-DFI initiative, as declared in their "Joint MDB Statement of Ambitions for Crowding In Private Finance", which articulates their collective targets for increasing mobilization of private finance. This group includes the World Bank Group and its sister institutions in Asia, Africa, Latin America, and Europe as well as the Islamic Development Bank, the European Investment Bank, and the newest MDBs — the AIIB and the New Development Bank (MDBs 2017).

In 2017, the G20 Eminent Persons Group on Global Financial Governance (EPG), chaired by Singapore's Deputy Prime Minister Tharman Shanmugaratnam, was asked by the G20 Finance Ministers and Central Bank Governors to draft a series of recommended reforms to the global financial architecture and governance of the international system of MDBs. In October 2018, the EPG released its report, "Making the Global Financial System Work For All," also known as the Tharman Report, with recommendations that called for a major overhaul in two areas, among others:

1. Exploiting the largely untapped potential for far greater collaboration and coordination among the disparate group of public MDBs and DFIs in order pool their

resources together and converge around new system-wide set of core standards for coordinated project identification, financing, design and implementation; and

2. Embarking on an MDBs system-wide effort to provide insurance and diversification of risk by creating a new large-scale asset class with which to de-risk investments and thereby mobilize significantly greater private sector financing from capital markets (EPG 2018).

By bundling MDB loans into securities that could be used and re-used as collateral for obtaining new financing for other investments (rehypothecation), and by transferring risk and thus lowering the cost of lending, the G20 is hoping the MDBs can stretch their billions of MDB dollars into trillions for development finance.

In a high-level panel presentation after the G20 EPG released its report, Tharman, the panel chair, drove home the seriousness with which the G20 proposal is intended to be taken: "And this is not, by the way, a think tank report. I mean, I have great respect for think tank reports. It is a policy report. It's a report that is meant to be implemented. And we think that most of its proposals can be implemented within the next few years" (CFR 2018).

2.3 World Bank Group & Maximizing Finance for Development

Former World Bank President Jim Kim is widely credited with enthusiastically pushing the institution towards high finance. Kim personally invested a great deal of time and energy in finding new ways to attract private equity firms, insurance companies and sovereign wealth funds to invest in World Bank projects, and aggressively advanced the Bank's support of blended finance and public-private partnerships (PPPs). The World Bank's private sector lending arm, the International Finance Corporation (IFC), has long provided financing to private companies in exchange for equity stakes. By 2017, the World Bank was actively raising more than USD 7 billion a year from the private sector to invest in various blended finance initiatives in developing countries, with goals to vastly increase this amount (Thomas 2018).

With backing from the G20 governments, the MDBs are now being given the political green light to prepare the groundwork for scaling up such activities by orders of magnitude in the future. As noted above, in 2015, the Development Committee of the International Monetary Fund (IMF) and World Bank published a report entitled, "From Billions to Trillions: Transforming Development Finance Post-2015 Financing for Development: Multilateral Development Finance." The report, which had been drafted by a group of six MDBs and the IMF, underscored the point that while domestic public spending presently provides the largest supply of development resources, private finance offers the greatest potential for a major expansion of development resources in the future. Therefore, the report called on the MDBs to enhance their financial leverage and take steps to catalyze private investment.

In 2018, Kim helped engineer a general capital increase for the World Bank Group. The capital increase is based upon two sets of documents that are intended to chart the

Bank's future: "Sustainable Financing for Sustainable Development" and "Forward Look: A Vision for the World Bank Group in 2030 – Implementation Update." The former document describes the role of 3 arms of the Bank Group: the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Association (MIGA) this way:

> Overall, the WBG (World Bank Group, the author) will significantly expand the use of private sector solutions, multiplying the impact of its resources and opening opportunities for private investment. The IBRD will increase its mobilization ratio to 25 percent on average over FY19-FY30 (vs. 18-20 percent with no capital increase). IFC also leverages the political risk insurance and credit enhancement of MIGA through the IFC-MIGA Business Development Agreement (para 55).

At the same time, the World Bank launched an ambitious strategic approach to its operations called "Maximizing Finance for Development" (MFD) (formerly called "Billions to Trillions"). According to the World Bank, the MFD approach:

- Will include identifying the right investments, taking the financial risk to initiate them, and implementing them effectively and efficiently by leveraging the private sector;
- Will create the imperative to leverage the private sector for economically beneficial, sustainable investments that contribute to development goals and optimizing the use of scarce public resources;
- Is necessary because the public sector faces limitations in meeting this need, including in fiscal space, capacity, and governance (Hoque 2017).

The MFD project will comprise two basic areas of work:

- "MFD-Enabling Projects": Activities that address binding constraints at the country, market, or sector level in a way that is expected to unlock private solutions within a short timeframe (three years' post-completion);
- Private capital mobilized: The World Bank Group Corporate Scorecard already tracks private finance mobilized, directly or indirectly, in compliance with the MDB-agreed methodology (Hoque 2017). Indeed, all the MDBs report their leveraging ratios to the G20 using this agreed-upon methodology.

The World Bank describes what it means by "MFD-Enabling Projects": Getting developing countries to enact a host of domestic policy reforms that broadly deregulate their domestic financial sectors and allow the entry of international banks as well as shadow banking institutions from advanced economies and China, and enable the establishment of new securitization markets that are supported with short-term liquidity markets and local currency bonds.

To benefit from the huge new private capital inflows promised by the MFD approach, the World Bank is telling developing countries they must "address binding constraints to enable sustainable private sector solutions for development projects." These binding constraints are identified as "bottlenecks in the enabling environment at sector or country level, or physical, operational, or system bottlenecks which prevent private sector solutions from being implemented."

It is worth deconstructing what is meant by such "bottlenecks in the enabling environment": all kinds of labor and business, land acquisition, environmental and social laws and regulations. To access higher flows of securitized development lending in the future, developing countries are being told by the World Bank that they will be expected to remove such laws and regulations deemed to be bottlenecks "preventing private sector solutions" from being implemented. In particular, developing economies will be required to undertake a set of financial liberalization reforms to make securitized development lending accessible.

In other words, the World Bank means developing countries must get rid of pesky macro-prudential financial regulations that safeguard financial stability and instead adopt reforms to liberalize their rules to expand the entry of international banks and shadow banking institutions and increase the integration of their domestic financial sectors with global capital markets. To remove bottlenecks and provide inducements to the private sector, the World Bank Group has advised its borrowing governments to implement its "Cascade" guide to decision making about the use of public or private resources for financing development projects in which each decision privileges the private sector over the public sector (See Box 6 below).

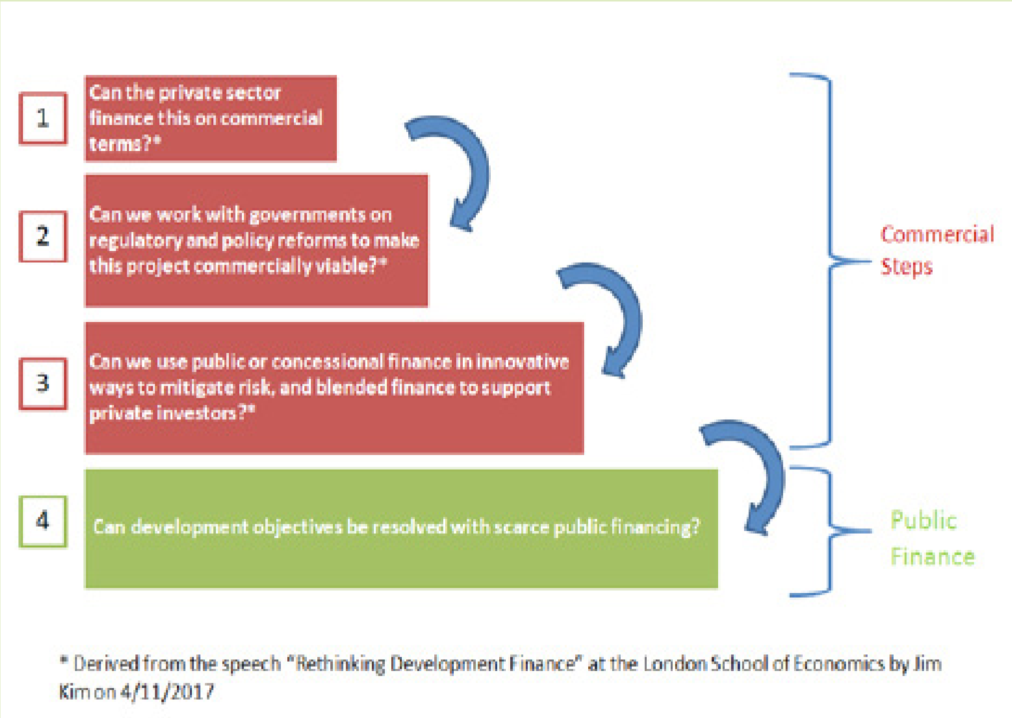
Box 6. The Cascade: The "Operating System" of Maximizing Finance for Development

To support this effort, the World Bank Group is implementing MFD by applying a "Cascade" of questions to guide borrowing countries' decision about how to finance development projects. The guide ensures that countries first fully exhaust all possibilities for private financing options before deciding to use traditional public resources. The "Cascade" model encourages developing countries to ask the following questions: Can the private sector pay for this project by itself? If not, what types of financial liberalization, deregulation and other domestic policy reforms could be adopted by the country to enable to private sector to be able to pay for the project by itself?

If those steps fail to attract private investors, the model asks what steps the state could take to redirect its public resources to the project financing; Could the state offer to provide risk guarantees and subsidies to help make it artificially profitable enough for private investors to undertake the project? And if, even after all of these possible steps have been fully considered, a project still cannot be made to be profitable enough to entice private investors, then – and only then – should the project be financed with traditional public financing.

The World Bank's Cascade model overturns conventional thinking based on the history of the traditional public financing model that has been used for most infrastructure development projects in most countries. Instead, it starts from the overriding presumption that most projects could be financed through private investment if the governments would deregulate and liberalize their financial sectors enough, and if their states would use enough of their public resources as loan guarantees and subsidies for private investors. The presumption is that the financing for almost everything can (and should) be privatized, and even securitized.

Figure 1. Public or Private? The World Bank's Cascade Model for Decision Making



Ghana's Country Private Sector Diagnostic is an example of how the Cascade works. In it, the IFC looked at 22 sectors for their attractiveness to the private sector, concluding that agribusiness, information and communications technology and education are ripe for integration into global value chains linked to multinational corporations. According to the diagnostic, several sectors such as light industry had too much public support to attract the private sector. *It is notable that this reflects a dramatic inversion of the traditional approach to prioritizing development financing, which was to support long-term national economic development goals and examine the potential of an investment to reduce poverty and inequality over time. The new approach is to use public development financing for prioritizing whatever is the most profitable for the private sector.*

But the Cascade model for decision-making may turn out to be more than just suggestions. As more development finance from the MDBs is distributed through private channels, borrowing countries may feel increasingly compelled to follow the Cascade's suggested reforms in order to become eligible for receiving aid, credit or private development finance.

2.4 Prescriptions for financial deregulation

As the Cascade model suggests, before private capital markets can pour billions of dollars into financing for portfolios of projects, developing country governments will be required to undertake a series of major economic policy reforms to prepare themselves. The aforementioned 2015 report by the IMF and six MDBs, "From Billions to Trillions," provided a detailed explanation of the policy reforms that would be required of developing countries (IMF et al 2015). Because of their major implications for national economic development, two of the major sets of policy reforms are highlighted below.

The first major set of policy reforms is to change the domestic regulatory and legal regimes to make the domestic financial sector more business friendly. Many current regulations and restrictions governing the financial sector will need to be reformed or eliminated, and a new policy framework will need to be devised to enable the establishment of securitization markets and the short-term liquidity markets and derivatives markets upon which they depend. Specifically, in order to make the whole plan work, securities traders and investors must be able to take advantage of short-term daily changes in the market price of securities, and therefore foreign investors require liquid secondary markets that allow them to quickly and easily create or liquidate securities positions (buy or sell). These include markets needed by the shadow bank institutions such as repo markets and derivatives markets that enable investors to obtain financing through securitization markets without any significant regulatory obstacles.

According to the World Bank (2019), "[A]a focus in these countries will be on reforms that create markets and institutions that can attract and manage private capital, so that projects pose an acceptable level of risk to investors. Without this upstream work, many of these countries remain excluded from the private financing options that wealthier countries enjoy".

Establishing such liquid secondary markets will require developing countries to undertake a set of major financial liberalization reforms, including issuing local currency bonds, capital account liberalization, i.e., removing capital controls or other regulations for easier entry and exit by foreign investors, etc. (Gabor 2018b; 2019). The repo markets in China and many emerging market economies are different from those of advanced economies in some key ways because legal and market practice does not force (shadow) bankers to care about, or to make profit from, daily changes in securities prices. This approach provides for longer-term transactions, which makes for a greater availability of "patient capital" and more resilient "plumbing" in the financial system (Gabor 2018c). However, the G20-DFI initiative would compel developing countries to move towards the U.S. and European model that provides for shorter-term transactions and less resilient plumbing.

The second major set of policy reforms would require developing countries to redirect public resources away from public investments towards "de-risking" activities to attract private financing, especially using public resources to provide private risk guarantees and subsidies to lower costs to help make various projects more profitable for private investors.

The main effort to kick-start the MFD approach was launched in 2017 by the World Bank with pilot projects in nine countries. These pilots are focused on development projects for the infrastructure sector and use an array of instruments to try to attract new private finance for the projects. The nine countries—Cameroon, Cote d'Ivoire, Egypt, Indonesia, Iraq, Jordan, Kenya, Nepal, and Vietnam—include one lower-income, seven lower-middle income, and one upper-middle-income country. Two are considered fragile or conflict-affected states.

These nine pilot efforts will build on existing World Bank programs in the countries, and in some cases, are being guided by the World Bank's infrastructure sector assessment tool (InfraSAP) that provides a roadmap for the various policy reforms the governments will need to undertake to deregulate financial sectors and establish securitization markets. In some countries, pilot efforts are building on policy reforms already underway to develop domestic capital markets under the World Bank's Joint Capital Markets Development Program. The World Bank calls these reforms "strengthening the sector and crowding in the private sector where it is deemed appropriate" (World Bank 2019). Observers of the new MFD strategy are waiting to see the outcomes of these pilot projects in particular, and to see to what degree private investors have been persuaded by the efforts to "de-risk" such investments.

3. THE DANGERS AND CONCERNS

This section describes the main ways the G20-DFI initiative presents an array of dangers and introduces a high degree of risk into the traditional system of development finance.

3.1 Securitization is risky

Because the G20-DFI initiative is centered on securitization markets, which depend on shadow banking institutions – which in turn require liquid secondary markets and repo markets – the initiative would introduce a wide range of new risks into the system of development finance. Unfortunately, the same features that enable the shadow banking system to be so flexible in providing credit (high leverage and maturity and interest rate mismatches) are also what make it so worrisome – it is unregulated – and therefore lacks both proper regulatory oversight and access to central bank funding or safety nets such as public deposit insurance and debt guarantees during financial crises (Martin 2012).

It is precisely because shadow banking institutions are not subject to the same regulations as regular banks that they can keep fewer financial reserves on hand relative to their degree of market exposure. *In other words, shadow banks can use very high ratios of financial leverage – that is, of debt relative to the liquid assets available to pay any immediate claims as demanded. This enables them to take extreme risks that would never be allowed in the regulated banking system.*

This reserves-to-leverage mismatch tends to also make financial markets more prone to procyclicality – i.e., high leverage magnifies profits during boom periods but makes shadow institutions much more vulnerable to catastrophic losses during down times, when market circumstances shift and massive claims must suddenly be paid. In other words, high leverage makes the intensity of boom and bust cycles much more acute.

For example, in the case of investment banks in the lead-up to the 2008 global financial crisis, the reliance on short-term financing required them to return frequently to investors in the capital markets to refinance their operations. When times were good, it worked well. But when the housing market began to deteriorate, the ability of the investment banks to obtain more funds from short-term markets suddenly dried up as investors and banks became reluctant to lend more. This left the investment banks unable to finance their long-term investments through constant short-term borrowing, forcing many to have to sell off their long-term investments at fire sale prices and ultimately leading to the failure of Bear Stearns and Lehman Brothers and triggering a system-wide financial crisis.

What's worse, due to the lack of regulation and considerable opacity of the instruments, the actual degree of high leverage is often not readily apparent to investors, and "shadow institutions may therefore be able to create the appearance of superior performance during boom times by simply taking greater pro-cyclical risks" (Simkovic 2012).

While there is a reasonable need to facilitate liquidity in financial markets, securitization markets based on shadow banking institutions can encourage profit-seeking based on massive indebtedness built on a frail foundation of equity or real wealth. By definition, investors with high debt-to-equity ratios can easily become over-leveraged. Under such circumstances, the issue is no longer about the good or bad fortunes of any one single investor, but the systemic risks to the entire economy generated by this type of activity on a large scale. Therefore, the question of the public interest is inextricably linked to financial stability. **For example, the high degree of leverage by firms on Wall Street prior to the 2008 financial crisis was underscored by the fact that the value of the total volume of traded derivative financial instruments was an estimated USD 740 trillion, compared to a world gross domestic product of USD 70 trillion (Bello 2019). Thus, such elevated risk taking by investors can have huge implications for the overall public interest.**

So securitization markets are inherently risky, and the shadow banking institutions needed to generate the short-term liquidity required by securitization markets are also inherently risky. So it's a double-whammy of stepped up riskiness. Yet it is precisely this degree of risky activity that allows the G20 and MDBs to dream that they can turn billions into trillions.

3.2 Systemic risk

The maturity and interest rate mismatches that allow investors to place such fragile bets and seek high rewards also subject such investors to considerable market, credit and especially liquidity risk. Because the business model is based on using very high degrees of leverage in ways that are unregulated, these features of shadow banking institutions represent a clear and present danger to the stability of the financial system. This is because, as mentioned, shadow banks do not have deposits on hand to draw on nor do they have access to the support of their central bank in its role as lender of last resort in a crisis. Therefore, while the high risk/high reward bets placed when things are going well can be very profitable, there can also be periods of market illiquidity, or worse, if (when) another financial crisis occurs, when the shadow banks could very likely be subject to rapid deleveraging, meaning they would have to pay off their short-term debts by quickly selling their long-term assets at bargain prices and could easily go bankrupt (Roubini 2008; Simkovic 2009).

For investments in which the underlying assets have been rehypothecated (used as collateral many times over for multiple investments), only those deemed priority creditors by bankruptcy courts are likely recover losses, while others deemed lower in the pecking order are likely to sustain damaging losses. Yet, the G20 and MDBs seem prepared to put billions of public development dollars at such risk.

But even more worrisome is the degree of overlap and interdependence that exists between the higher-risk shadow banking institutions and the supposedly safer formal regulated banking sector. In fact, there is a great deal of overlap between the two. According to the Bank for International Settlements, investment banks as well as commercial banks often use shadow banking institutions to carry out some of their activities, such as borrowing in the repo market and the issuance of bank-sponsored, asset-backed commercial paper. Additionally, many shadow banking institutions are either sponsored by big regulated banks or are affiliated with banks through their subsidiaries or parent bank holding companies (Hannoun 2008; Noeth and Sengupta 2011; Schiller 2012).

The actual degree of such regulated bank activity in shadow banking is unknown, but some experts suggest that it is so large that regulated banks may in fact be the largest shadow banks (Fein 2013).

Here, the concern is about the dangers posed to the entire financial system because of the degree of interconnectedness between the regulated banks and the shadow banks. This concern about the overlap was well articulated in the midst of the 2008 global financial crisis by former U.S. Treasury Secretary Timothy Geithner, who was then President and chief executive officer of the New York Federal Reserve Bank. Although he did not use the term "shadow banks," he placed significant blame for the freezing of credit markets on a "run" on the entities in the shadow banking system by their counterparties (investors who stopped rolling over the shadow banks' short-term loans). Geithner (2008) noted:

> The rapid increase of the dependency of bank and non-bank financial institutions on the use of these off-balance sheet entities to fund investment strategies had made them critical to the credit markets underpinning the financial system as a whole, despite their existence in the shadows, outside of the regulatory controls governing commercial banking activity. Furthermore, these entities were vulnerable because they borrowed short-term in liquid markets to purchase long-term, illiquid and risky assets. This meant that disruptions in credit markets would make them subject to rapid deleveraging, selling their long-term assets at depressed prices.

In other words, it was the widespread use of shadow banking activities by the big regulated banking organizations that was responsible for the severity of the financial crisis (Fein 2012; Fein 2013). When such crises strike, governments typically have to step in and bail out the financial sector, which redirects needed resources from the real sector (companies that actually produce goods and services) to the financial sector – a process which can aggravate economic inequality over time (Brei et al 2018; Piketty 2014).

Research by the European Commission's Joint Research Centre also expressed concern that the shadow banking system poses a potential risk to the stability of the financial system because of its opacity and the inability of regulators to understand the actual size of the shadow banking sector (Bauer et al 2016; Deutsche Bundesbank 2014; ECB 2012). Securitization of loans in the regulated banking system and the risk transfer to the unregulated, shadow banking system creates and increases the degree of linkages between the two systems, which can increase the risks in the entire system (Wallace 2015; Pozsar and Singh 2011).

The European Commission's Joint Research Centre found a tendency for some banks to not actually transfer and diversify the risk but to instead retain it through explicit guarantees and thereby increase their risk exposure. While the shadow banking system may enhance the stability of the financial system if it shares and diversifies risks in an efficient manner, researchers found that its opacity poses a risk as concentrations of risks and unknown linkages and channels of transmission cannot be readily identified by regulators, let alone investors (Baur et al 2016).

In 2014, the Financial Stability Board cautioned:

> The shadow banking system can broadly be described as credit intermediation involving entities and activities outside of the regular banking system. Intermediating credit through non-bank channels can have important advantages and contributes to the financing of the real economy; but such channels can also become a source of systemic risk, especially when they are structured to perform bank-like functions (e.g. maturity and liquidity transformation, and leverage) and when their interconnectedness with the regular banking system is strong. Therefore, appropriate monitoring of shadow banking helps to mitigate the build-up of such systemic risks.
>
> (FSB 2014)

But in the absence of such appropriate monitoring, it is difficult to know the true levels of risk. As the world witnessed in 2008, unregulated securitization markets with multiple actors are susceptible to dangerous declines in underwriting standards, as happened with mortgaged-backed securities. Off-balance sheet treatment for securitizations, along with guarantees from the issuer, can hide the extent of leverage of the securitizing firm, and thereby lead to risky capital structures and an underpricing of credit risk. Investors and regulators were unaware of the high degrees of leverage of US financial institutions because the complexity of securitizations before the 2008 financial crisis had obscured this. They were also unaware of the degree of the need for government bailouts when conditions began to deteriorate (Simkovic 2009).

Securitization markets can mitigate the credit risk of borrowers. But unlike regular corporate debt, the credit quality of securitized debt is "non-stationary" due to regular fluctuations that are time- and structure-dependent. As noted, this flexibility makes them both useful and attractive, but also dangerous. If the security is properly structured and the pool of assets performs as expected, the credit risk of all tranches of structured debt improves. But if the security is improperly structured, the affected tranches may experience dramatic credit deterioration and loss (Raynes and Rutledge 2003). The problem with the lack of oversight in unregulated securitization markets is that it is difficult to know if securities have been properly structured or not. It is unclear how the G20 or the MDBs propose to adequately address this problem of complexity and opacity when it comes to assessing risk in securitization markets.

A 2017 assessment of risks posed by shadow banking activities undertaken by the FSB noted that while some of the more vulnerable aspects of shadow banking have shrunk from pre-2008 crisis levels, others have grown or remain relatively large. It cautioned that the continued existence of interconnectedness and potential for financial stability risks "warrants continued attention by authorities" (FSB 2017).

Of particular concern, the Financial Stability Board (FSB) pointed to:

- "The size and considerable growth of collective investment vehicles that are susceptible to runs (representing 65 percent of the narrow measure of shadow banking), such as open-ended fixed income funds, credit hedge funds, real estate funds and money market funds, have been accompanied by a combination of a relatively high degree of credit risk, as well as liquidity and maturity transformation;
- Although finance companies, which are dependent on short-term funding to support lending activities, have declined since the global crisis to about 8 percent of shadow banking assets, they still tend to have relatively high leverage and engage in some maturity transformation, which makes them more susceptible to roll-over risk, including during periods of market stress;
- Market intermediaries dependent on short-term funding such as broker-dealers still comprise over 11 percent of shadow banking assets. Given their business model, broker-dealers engage in significant leverage and maturity transformation (e.g., through repos), and in some cases their level of interconnectedness with other sectors of the financial system is relatively high." (FSB 2017, p. 3).

And more recently, in March 2019, the FSB again expressed concern, announcing it had launched an examination of parts of the USD 1.4 trillion leveraged loan market, as regulatory officials have been intensifying scrutiny into potential financial stability risks surrounding corporate debt. The focus of the FSB's review, which is expected to be published in the fall of 2019, will be on so-called collateralized loan obligations (CLOs), or bundles of leveraged loans that are sold in tranches. The FSB "wants to identify the holders of CLOs around the world and assess the risks that investors could pull money from exposed institutions during a severe downturn. Among the investors in CLOs are banks, investment funds and insurers" (Fleming 2019). Included in the FSB review is the shadow banking sector, "which is often more lightly regulated and is swelling in size around the world." The FSB's latest assessment of what it now calls "non-bank financial intermediation" found the sector has ballooned to more than USD 50 trillion (Fleming 2019).

As the G20 and World Bank and other MDBs consider the use of special purpose vehicles to create asset-backed securities, it is not yet clear if they intend to sell-off the securities to other investors and traders (true sale securitization) or if they will retain ownership of the loans on their balance sheets and just use the assets as collateral for additional finance or transfer the credit risk in order to reduce the amount of capital reserves that they are required to have on hand, thereby freeing up more resources for making new loans to more countries (synthetic securitization). In either case, however, the G20-DFI initiative could place billions of dollars of public development finance at the DFIs, including the

MDBs, in jeopardy as these public resources get leveraged through securitization markets administered by unregulated shadow banking institutions.

Unfortunately, as Minsky was famous for pointing out, people have a tendency to forget about the need for financial regulation until once again, some day, another financial crisis hits and then they remember again about the need for regulation (Wolf 2019; Economist 2016; Wolfson and Epstein 2013). On the gamble that the global economy will never again face another major financial crisis and that short-term liquidity markets will never again suddenly dry up, the G20-DFI initiative is putting billions of public dollars in development loans for developing countries in jeopardy. Since capitalism as a system is structurally prone to generate periodic financial crises, the wisdom of this initiative must be questioned.

3.3 Securitization takes Public-Private Partnerships to the next level

The over-arching claim by the G20 and MDBs is that pursuing securitization will allow the MDBs to "de-risk" infrastructure development projects that are otherwise perceived as too risky by private capital markets. But a key lesson from the experiences with public-private partnerships (PPPs) is that there is no such thing as "de-risking" – just a reallocation of risk. In many regards, such efforts at de-risking have been a hallmark of PPPs over the preceding two decades.

Regarding the infrastructure sector, PPPs are "arrangements whereby the private sector provides infrastructure assets and services that traditionally have been provided by government… [which] … should involve the transfer of risk" (See OECD glossary of statistical terms).

Increasingly, the DFIs/MDBs are seeking to mobilize financing for mega-projects which, as Bent Flyvbjerg of Oxford's Saïd School of Business describes, carry risks as massive as the projects themselves. The risk of megaprojects is compounded when they are implemented as PPPs. As those observing the track record of PPPs have warned, such projects almost always involve some degree of risk due to setbacks, delays, and cost-overruns often due to external events such as earthquakes or hurricanes, climate change, poor design, social conflict, demand or foreign exchange fluctuations, mismanagement, and so on. These risks in infrastructure projects – whether due to human error or external causes – can never be done away with, but the critical questions are about who pays when something goes wrong, or how the allocation or risk can be reengineered.

Normally, publically-financed infrastructure has large up-front costs that decline over time, but with PPPs, contracts can commit the private investors to financing most of the up-front costs and then require governments to pay a set unitary charge over time. Dexter Whitfield, Director of the European Services Strategy Unit, said this process gives the impression "of infrastructure being privately financed when, in fact, it is ultimately entirely funded by taxpayer and/or service users" (Whitfield 2010). By back loading the public funding element, PPPs can create the illusion of short-term fiscal restraint by governments and private sector efficiency, when often it does not actually work out that way

(Van Waeyenberge 2016).

The actual experience with PPPs shows that often these arrangements can end up being far more costly to tax payers than if the public sector had just used traditional public financing methods for infrastructure and other development projects (Timmins and Giles 2011). The reason is that the process for designing PPP contracts presents numerous opportunities for padding the numbers, inflating the costs and other forms of rent-seeking by private providers. Griffiths and Romero (2018) documented a host of ways private investors have engineered higher direct costs, including: charging the state higher interest rates than the state could have otherwise got on its own; structuring contracts to guarantee a high expected rate of return for the private operators; charging higher construction costs; leading to higher indirect costs from limited competition and the costs of negotiating complex contracts, including high fees from consultancy firms and the renegotiating of contracts (more than half of all PPPs are renegotiated); leading to other higher costs that are "hidden" within accounting methods that keep PPPs off the government's books; and by allocating higher levels of "contingent liabilities" for the public sector (meaning the state picks up the bill if something goes wrong) (Griffiths and Romero 2018).

If the recent track record of PPPs is anything to go by, then what the G20 and DFIs might actually mean by "de-risking" infrastructure finance is to reallocate significant risks from the private investors to the borrowing governments of developing countries (Gallagher 2019; Shrybman and Sinclair 2015).

For example, a legal analysis of the 2017 edition of the World Bank's Guidance on PPP Contractual Provisions shows that the public party would assume all or a significant part of the risk for many contingencies – from "force majeure" to performance failures on the part of the private party. The "contingent liabilities" built into such PPP contracts oblige the public sector to cover any such losses for private firms, regardless of whether a PPP project is successful and actually provides the intended goods or services to citizens or not (Mann 2018). Therefore the World Bank's guidance to developing countries on how to structure PPPs "does not take an equitable approach to balancing public and private interests" (Foley Hoag, et al 2019; Aizawa 2017).

Along the same lines, the IMF has expressed concerns about such "contingent liabilities" clauses within PPP contracts that have saddled many countries with massive public sector debts when PPP projects have gone badly. The IMF warned, "While in the short term, PPPs may appear cheaper than traditional public investment, over time they can turn out to be more expensive and undermine fiscal sustainability" and PPPs are "generally considered to carry higher fiscal risks than budget financing" (IMF 2018a; IMF 2015a).

The European Network on Debt and Development completed a study on the impact of 10 PPP projects that have taken place across four continents, in both developed and developing countries. It found that the projects came with a high cost for the public sector, an excessive level of risk for the public sector and, therefore, ultimately a heavy financial burden for citizens. Every PPP studied was riskier for the state than for the private companies involved, as the public sector was required to step in and assume the costs when things went wrong. Five of the 10 PPPs reviewed impacted negatively on the poor and contributed to exacerbating economic inequality, and three of the projects resulted in serious social and environmental impacts. Nine out of 10 of the projects lacked transparency and/or failed to consult with affected communities, thereby undermining democratic accountability. All cases showed PPPs were complex to negotiate and implement, and that they required specific state capacities to negotiate in the public interest, including during the renegotiation process. Three of the PPP contracts had to be cancelled due to evident failure in the process, including the failure to do proper due diligence to identify the possible impacts of the project (Eurodad 2018).

In recent years, the UK has suffered a series of scandals and controversies over poor service, high prices and large payouts to shareholders with PPPs (called PFIs in the UK). Audits have repeatedly showed that tax payers have ended up paying much more for many PPP initiatives than if they had been publically financed in the first place (Chakrabortty 2018; IMF 2018b; Shaxon 2018; Ford and Plimmer 2018; Timmins and Giles 2011).

Whereas the UK had been a leader in privatization as well as forging PPPs, today a major national debate is raging over how to run its essential utilities while a political movement is calling for the renationalization of the utilities. In 2018, when the construction firm Carillion collapsed, its 450 public service contracts were thrown into limbo (Inman 2018; Plimmer 2018; Sandle and O'Leary 2018). This was an example of how the complexity and opacity of the contracts allowed investors to "run rings around the watchdogs set up by the government to regulate the industries" (Ford and Plimmer 2018).

In recent decades, dozens of UK utilities were turned over to the private sector under outright privatizations or under PPPs, and they brought in tremendous amounts of private capital to support investment. But critics claim that the private operators have failed to deliver both the market discipline and the innovation that had been promised and that regulators have been too lenient in setting the efficiency targets that are used to justify extra returns for that private capital. Critics of PPPs are calling for regulators to be given stronger executive powers to "intervene in extreme financial engineering initiatives and aggressive tax tactics" (Ford and Plimmer 2018).

Research by the European Parliament compared the financing costs of a range of alternative mechanisms for infrastructure projects and found that PPPs were clearly the most expensive way to finance projects, with significant liabilities or costs ultimately carried by the state (Griffiths et al 2014; Van Waeyenberge 2016).

Based on such audits, IMF researchers reached some very simple conclusions: "If the use of a PPP instead of public financing does not change the net present value of the government's cash flows, the PPP does not make the investment more affordable. If the government cannot afford to finance the project using traditional public finance, it probably cannot afford to undertake it as a PPP. Conversely, if the government can afford to undertake the project as a PPP, it can probably also afford to finance it traditionally" (Funke et al 2013; Van Waeyenberge 2016).

Despite the many lessons and warnings over PPPs in the last decade, official efforts to draw in the private sector into development finance through an innovative blend of public resources and private capital have not slowed. Now the G20-DFI initiative to "turn Billions into Trillions" seeks to build off of this legacy and take the PPP approach to entirely new levels through the expansion of securitization and market-based finance.

3.4 Undermining the use of "developmental states"

Another set of concerns about the initiative to financialize development operations is related to the deregulatory reforms and further financial liberalization that will be required of developing countries – and how these would further erode the role of the state in the process of structural transformation (shifting over time from an economy based on primary agriculture and extractive industries to one based more on manufacturing and services). Therefore, the G20-DFI initiative also has larger implications for the overall development model for developing countries.

If fully adopted, the types of policy reforms needed to comply with the proposed financialization of development operations would prevent developing countries from being able to use many types of financial regulations, capital controls and other policies needed to steer capital into productive activities that support long-term national economic development priorities. Such regulations and controls were historically used by all of the successfully industrialized countries when they were first developing, from the UK, the US and Europe to Japan, the 4 Tigers of East Asia and China. Such "developmental states" created domestic markets, but then used regulations to deliberately distort them in order to pro-actively support the building-up of domestic manufacturing firms over time (Amsden 2001; Chang 2002: Reinert 2007; Rosnick et al 2017).

Today's rich countries figured out long ago that if national economies are not moving beyond an over-reliance on dead-end activities that tend to provide diminishing returns over time (primary agriculture and extractive activities such as mining, logging, and fisheries), and into activities that can provide increasing returns over time (manufacturing and services), then they were not "developing" in the conventional sense. The increasing returns from manufacturing activities provided much higher wages, which contributed to building the domestic tax base, both of which are necessary to reduce poverty and support national economic development. But for the last few decades, the widespread adoption of free market economics has suggested that developing countries should not try to industrialize, but rather just stick with their "comparative advantage" in primary commodities, which tend to suffer from diminishing returns over time (Reinert 2018; Reinert 2007; Chang 2002).

During the last few decades, the host of industrial policies required by governments to help to build their domestic manufacturing sectors over time – including regulating domestic finance – have been largely limited or done away with under free market economics principles, World Trade Organization (WTO) membership rules and in a range of free trade agreements and international investment agreements. According to free market principles, using industrial policies and regulating finance came to be regarded as harmful "state intervention" in the economy that should be abandoned.

Today, although manufacturing sectors must move away from earlier environmentally destructive practices and increasingly use renewable energy resources, new technologies, decrease pollution, use recycled inputs and new materials in green manufacturing, nevertheless these fundamental basics of national economic development – i.e., the need to move beyond diminishing returns activities and towards manufacturing and services – remain the same for most developing countries which seek to raise wages and reduce poverty.

Typically, in the long-term pursuit of building their manufacturing sectors, "developmental states" used a combination of public financing, financial regulations, incentives, disincentives, exchange rate management, capital controls and other measures in order to regulate the domestic financial sector and ensure that it supported building-up the domestic manufacturing sectors. The approach was based on the recognition that, if they deregulated their financial sector too prematurely under a laissez faire approach, investors would pursue different short-term speculative opportunities and would not by themselves invest in the key economic areas necessary to pursue long-term national economic development priorities.

Successful developmental states also recognized that foreign investors operating in their domestic economies could also not be left unregulated. Rather, incentives, disincentives and regulations were necessary to prioritize the most appropriate types of foreign direct investment (FDI) needed to support strategic development priorities. For this reason, most successfully developed countries only allowed the entry of FDI if it contributed new technologies and purchased local goods and services to support beneficial forward and backward linkages with local companies within the domestic economy.

Developmental states understood the difference between infrastructure for building long-term national economic development and infrastructure for simply enabling foreign investors to extract natural resources. Traditionally, public infrastructure has been financed with public resources in line with national economic development strategies for the purposes of building linkages among key transportation, labor and production markets within the national economy. Efforts to build domestic manufacturing sectors were especially important drivers of infrastructure policies and priorities. Infrastructure decisions were therefore not determined by their potential for profitability for private investors, but by public priorities and long-term national development strategies. In contrast, privately-financed infrastructure for road, rail and ports has tended to prioritize the export of natural resources and is not necessarily helping developing countries with their long-term efforts at structural transformation and sustainable development (UNCTAD 2018).

Additionally, developmental states understood the important role of public development banks as critical institutional tools for financing long-term national economic development goals. Public development banks (and sometimes even central banks) provided the essential long-term, low-interest "patient capital" that private banks and international financial markets cannot provide. This is because maximizing return on investment is not the overall goal of public development banks. Instead, their goal is to support public policy objectives that are necessary for implementing long-term national economic development strategies. Public development banks were also used to steer needed finance to important sectors or regions that would otherwise not get it from private finance, to supplement the financial sector by filling gaps in credit supply or demand, and to promote economic stability through counter-cyclical lending. They also supported targeted social goals such as improving standards and linking financial access to improvements in social or human rights safeguards (Epstein 2005; Romero 2017).

Lastly, from the earliest experiences with industrialization strategies, developmental states such as those in the UK, the U.S., Europe, Japan, the 4 Tigers of East Asia and China had all learned through trial and error that waiting for private entrepreneurs to establish critical industries when the private sector was either unwilling or unable to do so was not a winning strategy. It became clear that in some sectors, the state would need to step in as the "entrepreneur of last resort" with state-owned enterprises supported with state financing and subsidies, particularly because they are able to take on extreme risks, independent of the business cycles (Evans 1995; Johnson 1996; Woo-Cummings 1999; Amsden 2001; Wade 2003). Or sometimes the state would need to step in as the "entrepreneur of first resort" in order to finance the large, long-term research and development for innovations that the private sector could not (Mazzucato 2015).

However, many of these strategic uses of state-regulated finance by developmental states have been increasingly outlawed over the last few decades through MDB loan conditions, WTO rules and international trade and investment agreements as guided by the Washington Consensus approach to free market development strategies that became popular in the 1980s and 1990s (Gallagher, Sklar and Thrasher 2019). Under such liberalization policies, the role of the state in the national economic development process has been sharply curtailed and financial sectors have been increasingly deregulated, particularly in the emerging market economies. As a consequence, many developing countries, particularly emerging market economies, have already been deregulating their financial sectors in recent years (Bishop et al 2018; Rowden 2018).

Therefore, the policies of the Washington Consensus approach to development over the last few decades have been nearly the opposite of those historically used by successful developmental states. These changes have made it difficult for developing countries to still use an effective role for the state in national economic development strategies, and in regulating finance to support national economic development.

Despite these trends, developing countries have resisted pressures to fully liberalize their financial sectors. In many countries, the financial sectors remain relatively small, and in many cases various financial regulations remain intact. While some financial regulations are allowed under WTO rules, they are increasingly curtailed by bilateral free trade agreements FTAs and international investment agreements. However, the new G20-DFI initiative for the financialization of development operations reflects a newer and more expansive type of pressure that goes even further than WTO rules and other trade and investment treaties in pushing developing countries to deregulate their financial sectors and deepen their integration into global capital markets. Proponents of the G20-DFI initiative view such deregulation as "preconditions" for being eligible to access the new forms of market-based development finance.

Prof. Daniela Gabor of the University of West England, Bristol, calls this new push for even deeper financialization the *Wall Street Consensus*: adopting financial liberalization on a new order of magnitude that will involve a wholesale reorganization and creation of new financial markets that would accommodate the investment practices of global institutional investors (Gabor 2019).

Today, if developing countries were to fully implement the policy reforms outlined in the IMF and World Bank's "Guidelines for Public Debt Management" and the World Bank Group's "Government Bond Market Development Program," the financial deregulation involved would present significant constraints and limits on the ability of developing countries to regulate finance in ways that were historically used successfully by developmental states (Alves 2019; Gallagher, Sklar, and Thrasher 2019). Consequently, the policy reforms articulated in the G20-DFI initiative would necessarily result in developing countries losing their monetary policy autonomy and their ability actively manage capital flows and influence domestic credit conditions. Adopting such reforms would amount to countries surrendering control over their autonomous national development strategies (Kwame Sundaram and Lim Mah Hui 2019).

Therefore, a major concern with the initiative is the developmental factor: without a strong state capable of effectively regulating its domestic financial sector to support domestic manufacturing and other long-term national economic development goals, it will become very difficult for countries to meet the SDGs and develop successfully. Ironically, the G20 and DFI drive to raise private financing to fund the SDGs would appear to be on a collision course with the ability of developing countries to adopt the developmental states they need to achieve the SDGs, particularly SDG number 8: "Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all" and SDG number 9: "Build resilient infrastructure, promote inclusive and sustainable industrialization, and foster innovation."

In jeopardy is the traditional project for "national economic development" that has characterized the successful economic development of industrialized economies, which appears set to be abandoned in favor of a new project for "global integration" through financialization. The new project is based on de-linking domestic financial sectors from their national economies, national development goals and national accountability mechanisms. Whereas the Washington Consensus constrained the ability of developmental states to regulate finance, the *Wall Street Consensus* now threatens to finish them off completely.

The G20-DFI initiative seeks to engineer a shift from traditional bank-based systems to market-based financial systems by getting developing countries to adopt the architecture of the US and European securities markets and the accommodating shadow banking institutions – repurchase markets and derivative markets (Gabor 2018a; Gabor 2019). Given that even the most sophisticated economies in the world have thus far proven either incapable or unwilling to adequately regulate their shadow banking institutions, let alone structure PPP contracts that are equitable to taxpayers, it is difficult to imagine how developing countries could be expected to have the capacity to do so.

3.5 The loss of national autonomy

The G20-DFI initiative would more deeply integrate developing countries into global financial markets – with all the attendant volatility this implies. This shift could subject the financial stability of developing countries to the impulses of short-term financial market fluctuations and undermine the ability of states to pursue long-term national economic development goals.

As developing countries adopt the proposed reforms and further integrate their economies into global financial markets, they would become much more vulnerable to the vicissitudes of global markets and to the decisions of those well beyond their national economy, such as large institutional investors, global banks and asset managers (Kwame Sundaram and Lim Mah Hui 2019). For such decision makers in far off financial centers, who are guided by their balance sheets, the long-term national economic development and financial well-being of distant developing countries are not typically factors guiding their decisions.

This issue of the impact of global finance on developing countries has been a topic of increasing research in the last two decades. Cambridge University Research Fellow Carolina Alves (2018) provided a comprehensive overview of the many recent strands of research that are exploring these concerns. Today's research on financialization in developing countries is rooted in earlier discussions about the risks highlighted by the Latin American structuralist literature on the hegemonic role of the US dollar and its financial and monetary implications for developing economies; the Minsky-inspired currency and boom bust dynamics of financial crises in developing economies; and more recently, in research on the national-international dimension of financialization within developing countries (Alves 2018).

However, because these dynamics are relatively recent, there are many unknown aspects to the integration of developing economies into global financial markets that require much more research. For example, the degree to which financialization is being driven by international factors or in some cases by autonomous domestic political economy processes or by some combination is unclear (Alves 2018).

As it relates to the process being driven by international actors, a final concern is the plan to coordinate MDB lending operations. As stated above, the G20's Eminent Persons Group (EPG) on Global Financial Governance called for the establishment of a coordinated system of new country and regional "platforms" through which DFIs, including MDBs and bilateral aid donors, could work together as a group to coordinate future development financing for projects and work through a new set of core standards for joint project preparation, procurement, transparency, etc. (EPG 2018). The added sovereignty concern is that the combined lending firepower and leverage jointly exercised by this much larger group of DFIs could in some cases begin to overwhelm borrowing country ownership and autonomous decision making about financing, and also override the voices of domestic civil society groups and public interest organizations engaged in development efforts within developing countries (Alexander and Rowden 2018).

3.6 Who would be accountable for the environmental, social and governance standards currently fixed to Multilateral Development Banks development project loans?

Another major concern with the G20-DFI initiative is about how it will affect the already weak accountability mechanisms at the World Bank and other MDBs and DFIs, and specifically, who would be accountable for enforcing Environmental, Social and Governance (ESG) standards for the underlying development projects under the new system.

Civil society organizations, including human rights, labor and environmental organizations around the world have spent the last several decades demanding and securing the establishment of a range of social and environmental safeguards with which MDB investment projects must comply. Despite their many weaknesses and shortcomings, the current ESG safeguards can sometimes offer project-affected communities some degree of recourse for redressing grievances in the event that an MDB operation violates its own policies (Huijstee et al. 2016; CHRD 2019). But many of these efforts are losing relevance and not keeping up with the swiftly-developing new realities of financialization.

For instance, there is growing concern among civil society organizations that DFIs are deliberately using more program loans (rather than project investments) and financial intermediaries to circumvent their environmental and social safeguard policies. With rare exceptions, DFI-backed private equity funds are often left to apply their own standards – or standards they have agreed with their DFI backers – to monitor and self-certify their implementation (Hildyard 2012b). The concern is that such types of ESG enforcement will continue to be inadequate under the new initiative for greater financialization.

As stated above, it is not yet clear if the G20-DFI initiative envisions having MDBs sell-off the securities to other investors and traders (true sale securitization) or if they would retain ownership of the loans on their balance sheets and just transfer the credit risk (synthetic securitization) or use them as collateral for additional financing. Officially, MDBs are mandated by their shareholders to oversee the implementation of their loans to ensure quality control, development impact and environmental, social, procurement and other ESG-related safeguards. However, as the MDBs increasingly engage in originate-to-distribute loans that they subsequently sell off their balance sheets to revolving sets of external investors, this traditional model for ESG implementation and lines of accountability could start to break down (Humphrey 2018a).

These developments raise many unanswered questions about the implications of the G20-DFI initiative for accountability. For example, it is unclear what would happen in the event of a default of an underlying asset. Would the investor have the option of taking title to the underlying asset? If such a transfer is possible, will all project covenants run to the investor? What would the lines of accountability be between the new owner of the asset and the impacted communities on the ground? Who would have the responsibility for safeguarding environmental and social risks after a change in ownership or a default?

According to Oxfam, the recent increase in the use of private financial intermediaries by DFIs, including MDBs, for carrying out development projects in developing countries has already been causing problems with traditional ESG safeguards on accountability and transparency. As increasing amounts of development finance are delivered via private financial intermediaries such as banks, private equity funds, venture capital, microfinance institutions, and leasing and insurance companies – ostensibly because this expands the reach of development finance – the confidentiality concerns of these intermediaries has come into direct conflict with ESG transparency requirements (Oxfam 2018). If such worrisome developments are already underway with MDB funding through financial intermediaries, what would the full implementation of the G20-DFI initiative mean for ESG accountability going forward?

3.7 Too much finance

The G20-DFI initiative would draw developing countries increasingly into global capital markets and deepen their domestic financial sectors despite the warnings being raised by a growing body of evidence that identifies a danger point in the growth of the financial sector relative to the real sector within economies. Research suggests that once the growth of the financial sector reaches a certain size, it begins to undermine GDP growth for the economy as a whole.

A major factor in the trend is that, in the context of financial sector liberalization and deregulation, many investors tend to shift capital into short-term, higher risk/reward opportunities in the financial sector that can provide higher returns than other types of traditional investments in the real sector, where jobs are created and goods and services are produced. While this may be reasonable from the perspective of a single investor, it becomes a problem over time as the growth of the financial sector and increased availability of speculative opportunities ends up drawing disproportionate amounts of needed investment capital away from the real sector, ultimately harming economic growth rates and employment and exacerbating inequality. When this point is reached, it is no longer about the prerogatives of individual investors to make decisions for themselves and instead becomes a public interest issue.

When the financial sector gets too big within an economy, it begins to warp decision-making on spending and investments at a systemic level so that movements in the production and pricing of goods and services are increasingly conditioned not only by actual supply and demand in the real economy but by movements in financial markets. In the process, the original function of the financial sector – to channel money from those who have it (savers) to those who need it in order to invest in production (investors) – becomes delinked as financial speculation increasingly becomes an end in itself (Bello 2019).

The fact that financial sectors that get too big can develop these deleterious effects on their host economies had long been understood in previous eras. Economists such as Adam Smith, Karl Marx, John Maynard Keynes, Hyman Minsky and Charles Kindleberger had all warned about the phenomenon. More recent decades included warnings by Charles Tobin and Raghuram Rajan.

But particularly in the last decade following the 2008 global financial crisis, multiple new studies have consistently found what Nicholas Shaxon called "the finance curse" – an inverted U-shape line on the graph between finance and growth, i.e. at first the growth of the finance sector helps the economy grow over time, but eventually, as it gets bigger, it starts to become a drag on GDP growth as the real sector becomes starved of investment capital (Shaxon 2018a, 2018b; Baker et al 2018; Law et al 2018; Panizza 2017; Christensen et al 2016; Epstein and Montecino 2016; Cecchetti and Kharroubi 2015; Cournède and Denk 2015; Law and Singh 2014; Cecchetti and Kharroubi 2012; Arcand et al 2012; and Haldane 2010).

This growing body of literature has led some major international financial institutions such as the Bank for International Settlements (BIS), the Organization for Economic Cooperation and Development (OECD) and the IMF, all of which generally favor the financial sector, to issue warnings about the dangers of letting finance get too big (Kvangraven 2019).

For example, in 2015, a study by the IMF warned of the same inverted U-curve by noting that, while a finance sector can assist in a country's economic growth, it only does so up to a point: there is a critical threshold after which the size of the financial sector can begin to cause countries to suffer from "too much finance as financial resources are used less efficiently overall because investments are increasingly diverted into speculation and away from productive activities." Using data for 128 countries collected between 1980 and 2013, the IMF found that economies such as those of Japan, the US and Ireland had already crossed this threshold when financial sector expansion starts to provide fewer benefits to growth and eventually leads to diminishing returns (the study did not publish the data on China, Germany or the United Kingdom, where finance also plays a significant role) (IMF 2015b; Sayhay et al 2015).

Similar research by the BIS also found the same inverted U-shaped relationship between finance and growth as did that by the IMF and others (Brei et al 2018). Other research on the role of securitization in particular similarly found a relationship between securitization and economic growth, finding that securities based on certain types of underlying collateral can divert resources away from productive economic activities (Bertay et al 2015).

In describing how the large size of the financial sector has harmed the real sector in the United Kingdom, Shaxon (2018) noted the broad trends towards financial sector liberalization over the last few decades:

> And our businesses began to undergo a dramatic transformation: their core purposes were whittled down, through ideological shifts and changes in laws and rules, to little more than a single-minded focus on maximising the wealth of shareholders, the owners of those companies. Managers often found that the best way to maximise the owners' wealth was not to make better widgets and sprockets or to find new cures for malaria, but to indulge in the sugar rush of financial engineering, to tease out more profits from businesses that are already doing well. Social purpose be damned. As all this happened, inequality rose, financial crises became more common and economic growth fell, as managers started focusing their attentions in all the wrong places. This was misallocation, again, but the more precise term for this transformation of business and the rise of finance is "financialisation".... In other words, it is not just that financial institutions and credit have puffed up spectacularly in size since the 1970s, but also that more normal companies such as beer makers, media groups or online rail ticket services, are being "financialised", to extract maximum wealth for their owners."
>
> (Shaxon 2018)

United States Senators Chuck Schumer and Bernie Sanders have described similar deleterious trends that the rise of finance has had on the US economy (Schumer and Sanders 2019).

Countries with liberalized financial sectors can also suffer high costs when they are hit with a financial crisis. The IMF noted that, as the financial sector grows in size, "the positive effect on economic growth begins to decline, *while costs in terms of economic and financial volatility begin to rise*" (Emphasis added).

Also of concern are the correlations identified between large financial sectors and economic inequality. The BIS research also found essentially the same inverted U-shaped relationship present between finance and economic inequality, i.e., up to a point, more finance is associated with lower income inequality, but beyond that point, further financial development is correlated with higher income inequality (Brei et al 2018). Notably, this BIS research found differences for bank- vs. market-based financing: the higher inequality was primarily associated with market-based financial development and not significantly to bank finance (Brei et al 2018; Piketty, 2014).

Yet, despite the awareness generated by this literature in economics and the pronounced warnings by the IMF, OECD and BIS about letting finance get too big, the entire G20-DFI initiative is based on growing the size of the financial sectors in developing countries and deepening their integration into global financial markets.

The G20-DFI initiative has neglected the concerns raised by such research, leaving many important questions unanswered: In particular, if the world's largest and most powerful economies have thus far proven either incapable or unwilling to rein in the growth of their financial sectors (because of regulatory capture), despite having their sizes cross the critical thresholds identified, then how could developing countries ever be expected to do so?

3.8 The G20-DFI initiative neglects hard lessons: Poor people are too poor to pay a reasonable return on investment to private shareholders

The G20-DFI initiative would necessitate the further privatization and commercialization of public services over time, and thereby neglects many critical lessons that have been learned the hard way. For example, the World Bank's attempts to privatize water and other public utilities and public services in developing countries in the 2000s produced a major backlash because the effort ignored the same ultimate realities that had led to the establishment of the modern European welfare state in the 19th century: poor people are simply too poor to pay the market prices needed to provide an adequate return on investment for private investors.

Policy approaches that pursue the commercialization or privatization of public services in poor societies by skimming off and segregating the small middle class of consumers who can afford to pay higher market rates end up leaving too many poor people behind and holding back progress on overall national economic development. To address this problem, the European welfare state was established on the premise that large, long-term public investments in financing public health, public education, and public transportation systems and utilities that are universally accessible best enables the whole society to move forward with national economic development.

During 30 years of efforts to privatize public services in developing countries, the deeper economic inequality that often followed resulted in a backlash of tear gas-filled protests from Cochabamba, Bolivia to Nairobi, Kenya, to activists systematically dismantling private water meters from entire neighborhoods in South Africa. *Ultimately, these efforts have led to a counter wave of over 800 cases of "remunicipalizations" of public services involving more than 1,600 cities in 45 countries over the last 30 years* (Kishimoto 2018; McDonald 2018). For example, Cumbers and Becker (2018) documented a global trend since 2000 in which cities take formerly privatized assets, infrastructure and services back into public ownership as "a reaction to the problems and contradictions arising from four decades of privatization and marketization of public services" and described the remunicipalization trend as "a compelling contemporary phenomenon of urban politics and governance."

Despite these basic lessons of history, both distant and recent, the G20-DFI initiative still calls for the further privatization of infrastructure as a way to finance development. The securitization process in the G20-DFI initiative would enable long-term revenue streams from infrastructure investments to be bought, sold and traded or used as collateral for private investors who will want an adequate return on investment. For example, as former World Bank President Kim stated, the initiative envisions that consumers who pay to access toll roads in Tanzania would provide the future revenue streams for financing pension funds in the UK who have invested directly or indirectly in the asset. By definition, this would require the road to be privatized rather than be a public investment by the Tanzanian taxpayers; and by definition a portion of the proceeds from the toll road would go out of the country for decades or even in perpetuity and not be recycled within the domestic tax base for use in other public investments in Tanzania. In these ways, the G20-DFI initiative for securitization of development finance requires the privatization of infrastructure and thereby contributes to a form of wealth extraction from developing countries to asset holders in global markets. In so doing, the initiative turns the historical purpose of public investment on its head.

As noted, overseas development assistance has been increasingly funneled through private channels in recent years through blended finance instruments and PPPs and the growing use of financial intermediaries by the MDBs and DFIs. The G20-DFI initiative represents the natural next step in this trajectory: expanding the broad-based use securitization markets.

It should be perfectly clear, however, that private equity funds do not invest in projects in order to provide public goods, but to generate above-market returns on investment for investors. According to Nicholas Hildyard (2012b) of the UK-based research and advocacy group, The Corner House, "[E]entirely absent from the portfolios of all but a few philanthropically-financed infrastructure funds are projects that respond to the demands of poorer people." So while there may be investment in privatized water utilities servicing those who can afford it, "there are no investments in rainwater harvesting that, once installed, provides water for free" (Hildyard 2012b). While such opportunities to invest in privatized water utilities in a developing country may be good for investors and institutions on an individual level, at the macro level this process facilitates the very exclusion and economic inequality in society that the European welfare states sought to undo.

As the DFIs and MDBs have advanced efforts to privatize development finance in recent years, one of the results has been a retooling of the role of the state: the policy decisions become less about a choice between the private sector and the state. Rather, according to Hildyard (2012b), there is a new state-private nexus emerging, in which a realigned state serves as the lynchpin in creating new highly profitable investment opportunities through blended finance mechanisms, PPPs or the outright selling off of public assets at bargain prices. Rather than directly providing its own public infrastructure, the state's role under the G20-DFI initiative would advance this new state-private nexus mode and redefine the role of states in terms of their capacity to create assets, manage private sector risks and protect the rate of return of global infrastructure investment funds (Fine and Hall 2012; Farmer 2014; Van Waeyenberge 2016). In other words, states would become more attuned to meeting the needs of foreign investors and less attuned to the needs of their own citizens or long-term national development goals.

Under such conditions, infrastructure is likely to be built only where it might be most profitable for investors and not necessarily where it can be accessible and affordable for poor people or where it is most needed according to national economic development strategies (O'Neill 2013; Hebb and Sharma 2014; Fine and Hall 2012).

Despite the lessons and warnings highlighted above, the G20-DFI initiative suggests that the process of the financialization of development finance is set to continue (Van Waeyenberge 2016).

4. ADVOCACY FOR PUBLIC FINANCING

In response to these concerns, there is a need for greater advocacy by civil society organizations, social movements and policy experts around the world to both challenge the efficacy of private development financing and call for moving in the opposite direction– to scale up traditional public investment and bank-based financing systems.

Experts note that there are considerable untapped pools of public money in many developing countries, especially in public pension funds for state employees, which could be used for public sector investment in infrastructure. Governments could also restore their depleted coffers by abandoning low tax regimes or clamping down on tax evasion and capital flight.

The G20-DFI initiative would likely have very limited application in low-income countries (LICs), most of which are located in Africa. Such countries are unable to provide the necessary financial infrastructure and technical and administrative skills required to adopt the G20's proposed approach. For example, according to the World Bank's private sector arm, the International Finance Corporation (IFC), LICs accounted for only about 5 percent of blended financing mobilized in 2018 (World Bank 2018). This suggests the initiative would only be applicable in larger, middle-income countries (MICs) and emerging market economies – yet, ironically, the need for infrastructure lending and other development finance is arguably greatest in African countries (Moore 2018). This lack of capacity in LICs to adopt the G20-DFI securitization approach has not deterred the New Partnership for Africa's Development from launching its "5 % Agenda" – a campaign to increase the allocations of African asset owners to African infrastructure from its current level of 1.5 percent of their assets under management to 5 percent (PIDA 2018).

The multiple initiatives by the DFIs in recent years have so far failed to attract the large levels of private investors from global capital markets that they predicted, not just in LICs, but across the board. For example, according to the Inter-Agency Task Force on Financing for Development (FfD), in 2017 MDBs directly mobilized only USD 52 billion in long-term private co-financing, with only USD 2 billion mobilized for the least developed and other LICs. Similarly, between 2012 and 2017, the OECD's Development Assistance Committee donors only mobilized USD 152.1 billion from private capital sources, with most going to MICs and only 8 percent mobilized for LICs (MDBs 2018; IAFT 2019); And data from the Blended Finance Task Force found similar outcomes of securitization efforts by the MDBs thus far, noting that from 2008 to 2014 such efforts only mobilized an average of USD 37 billion annually (BFT 2018). In 2019, the Overseas Development Institute found that, on average, for every USD 1 of MDB and DFI resources invested, private finance mobilized amounts of just USD 0.37 in LICs, USD 1.06 in lower-middle-income countries and USD 0.65 in upper-middle income countries (Attridge and Engen

2019; Edwards 2019). This is quite far from the "trillions" that were promised.

Judith Tyson of the Overseas Development Institute explained that realizing the promised higher levels of private capital is "likely to require higher subsidies" because, "[A]s the volumes of finance mobilized rise, marginal projects and investors will need to be engaged. This is likely to result in ever riskier projects and the engagement of increasingly risk-averse investors, requiring higher subsidy levels" (2018). And in striking similarity to observations about the outcomes of PPPs, Tyson cautioned, "[H]however, there is a point at which the cost of the subsidy becomes so large, that more could be achieved by direct public investment" or in other words, by simply using public financing in the first place (Tyson 2018).

This inability of the G20-DFI initiative to mobilize the trillions of dollars promised also suggests that there is still a critical role for publicly financed infrastructure and other types of development in the world's poorest countries. In fact, most infrastructure financing has traditionally been based on public financing and it is imperative that civil society and other advocates find ways to strengthen and expand public finance (Eurodad 2018). This also implies there is a major need to support the scaling-up of public development banks that have historically played an important role in successfully financing public infrastructure (Griffith-Jones and Ocampo 2018; Chandrasekhar 2016; Griffith-Jones 2016; TNI 2016; McDonald and Ruiters 2012).

After three decades of free markets ideology in the political ascendency, in which public institutions and public finance have been broadly disparaged, advocates must work to reinvigorate debates about the beneficial role and value of public investment and public financing. For example, Prof. Mariana Mazzucato has recently launched a new Institute for Innovation and Public Purpose at University College London which describes its mission as "to rethink how public value is created, nurtured and evaluated and in particular how the public sector and public finance can drive innovation and actively co-create and shape the markets of the future" (and not simply to fix market failures or de-risk business ventures). Mazzucato (2015) documents the extensive history of successful state support in fostering some of the most important technological innovations we now take for granted, such as vaccines, the internet and GPS, and many others.

Many civil society organizations, academics, and research institutions around the world have been producing research that highlighted the failures, dangers and consequences of various PPP projects. As a result of this work, in 2017 the European Network on Debt and Development (Eurodad) published an international sign-on letter by 149 national, regional, and international civil society organizations, trade unions and citizens' organizations from 45 countries that openly called on the World Bank to halt its promotion of PPPs for social and economic infrastructure financing, and to acknowledge publicly the financial and other significant risks that PPPs entail (Eurodad 2017).

Given that the G20-DFI initiative seeks to greatly scale up PPPs to a whole new level using securitization markets, a similar international sign-on letter by over 130 economists published in 2018 raised the alarm about the G20 proposal for the financialization of development lending. The letter stated:

> We call on the World Bank Group to recognize that the preference for the private sector should not be automatic, but rather chosen only when it can demonstrably serve the public good. When it meets this test, we call for the WBG to develop an analytical framework that clearly sets out the costs of de-risking and subsidies embedded in the MFD agenda in a way that allows a broad range of stakeholders, including civil society organizations and other public interest actors, to closely monitor results as well as fiscal costs in order to ensure transparency and accountability. Should the MDBs adopt the proposals for securitization of development-related loans, it should first develop a credible framework that protects the SDG goals from the systemic fragilities of shadow banking. But this will not be enough. To ensure that it does not shrink developmental spaces and that it advances sustainable development, the MFD agenda should only be adopted in conjunction with (a) a well-designed framework for project selection that is aligned with the global sustainable development goals and the Paris Agreement; (b) a careful framework for managing volatile portfolio flows into local securities markets and (c) a resilient global safety net.
>
> (CMF 2018)

In response to the financialization trend, many civil society organizations are calling on the World Bank and other MDBs to instead formally adopt or facilitate compliance with national commitments to: reduce carbon emissions as set out in the Paris Agreement; enact labor rights embodied in International Labor Organization conventions; and respect international human rights (e.g., International Covenant of Economic, Social and Cultural Rights) by designing their development policies with such goals in mind. Such commitments include prioritizing the public interest over the rights of private investors and strengthening the capacities for financial regulation and increased public financing.

The Office of the United Nations High Commissioner for Human Rights has also weighed in on the issue, warning that, despite the rush towards financialization, the human rights implications of infrastructure investment have not yet been adequately studied. It noted that the United Nations human rights treaties, along with core International Labor Organization conventions that governments have committed to, are relevant to infrastructure policy-making, investment, and the management of the environmental, social and governance risks (OHCHR 2017).

Box 7. Questions for Civil Society Advocates to Ask

- Whose infrastructure should be developed? And how should this be decided?
- Is public financing more efficient than private financing?
- If the public sector is to guarantee the private sector, which private sector should be supported? Multinationals? Major domestic conglomerates? Small and medium-sized enterprises? Community based co-operatives?
- What are the structural risks posed to the global financial system by the new forms of finance being devised by the infrastructure industry to fund private sector infrastructure development?
- If public debts are to be incurred for infrastructure development, how should their repayment be apportioned within society? Should poorer users pay through higher service charges? Or should wealthier sections of society contribute more through taxes?
- Are comprehensive public services possible where governments opt for low tax/ low public investment economic regimes?
- What forms of infrastructure delivery best serve the public interest? And how might consensus on what constitutes "the public interest" best be reached?
- What decision-making processes need to be constructed to ensure that infrastructure programs reflect real public needs? If the state is to take a greater role in delivery infrastructure services, what institutional forms ensure greatest accountability?
- What experience can be gained from the many initiatives already undertaken by citizens to reclaim municipal and other services from the private sector?
- What are alternative forms of financing for desirable infrastructure? For example, if communities determine that renewable energy is needed, how can stable, sustainable financing be developed as alternatives to constantly shifting private sector financing markets?
- How might the current state-private combination be reassembled to better serve the public interest?

Source: Adapted from Hildyard (2012a)

In 2018, Philip Alston, the United Nations special rapporteur on extreme poverty and human rights, criticized the prioritization for private financing built in to the World Bank's Cascade line of questioning when developing countries are deciding about public or private provision of financing for infrastructure. Alston called the Cascade's presumption that privatization is the default setting and that the role of the public sector is that of a last-resort actor an "entirely one-sided solution to development financing". He claimed that the Cascade guidelines neglect the concerns that widespread privatization of public goods in many societies is "systematically eliminating human rights protections and further marginalizing those living in poverty" (UN 2018).

In 2019, the United Nations Human Rights Council will address the need for establishing "Guiding principles on human rights impact assessments of economic reforms." These United Nations guidelines will address specifically the "obligations of States, international financial institutions and private actors" and the impact of their external influence on domestic policy space. Also at issue is the establishment of principles related to the obligations of public creditors and donors, specifically on international financial institutions, bilateral lenders and public donors to "ensure that the terms of their transactions and their proposals for reform policies and conditionalities for financial support do not undermine the borrower/recipient State's ability to respect, protect and fulfil its human rights obligations." Ensuring this would require regular human rights impact assessments and including rights as a mandatory element in the design of all economic reform and adjustment programs to avoid human rights violations.

To assist advocacy organizations in efforts to support and engage in this United Nations process, the European Network on Debt and Development produced an "Advocacy Guide for CSOs: UN Guiding Principles on human rights impact assessments for economic reform policies" (Eurodad 2018).

There is a major need for civil society actors to step up their learning about the financialization of development finance that is underway. In many cases, civil society organizations are ill-prepared to address these complexities because many have traditionally been focused on Environmental, Social and Governance safeguard-based approaches that are far "downstream" in the project cycle. The immediate task ahead is to bring together diverse parties to build a knowledge base and enhance learning regarding the development of the complex financial instruments involved, including how they operate and the implications for human rights-based approaches to development and accountability for public institutions.

Civil society advocates can deepen their activities in supporting countries to find the best financing method for public services in social and economic infrastructure, which are responsible, transparent, environmentally and fiscally sustainable, and in line with their human rights obligations. There are many viable options to prioritize tax revenues that can be augmented with long-term external, and domestic, concessional and non-concessional finance, where appropriate. For example, Boston University's Global Development Policy Center and the United Nations Conference on Trade and Development identified a set of goals and principles for forming the foundations for a new multilateral trade and investment regime that has shared prosperity and sustainable development as its core goals (Gallagher and Kozul-Wright 2019a; 2019b). Boston University's Global Development Policy Center also worked with the Brookings Institution to outline a guide for better aligning the G20's infrastructure investment initiatives with climate goals and the 2030 Agenda (Bhattacharya, et al 2019).

But advocates must take further steps to ensure good and democratic governance is in place before states pursue large-scale infrastructure or service development projects. Accountability can be improved through informed consultation and broad civil society participation and monitoring, including by local communities, trade unions, and independent media and other stakeholders. These efforts must also ensure that the right to free, prior and informed consent, and the right to redress for any affected communities, are much more meaningfully enforced in project-affected communities.

More rigorous transparency standards are needed, particularly with regard to accounting for public funds – the contract value of a proposed PPP and its long-term fiscal implications must be included in national accounts, which would require that all contracts and performance reports of social and economic infrastructure projects be proactively disclosed. Public funds used by public institutions in PPPs should be structured to ensure that the public interest is not subordinated to individual private investors.

Furthermore, critical steps are needed to address the problems with the growing role of private finance in development lending. As noted, capital markets are driven by short-termism. Civil society and others must advocate for policies that enable states to shift investors from short-term toward long-term investments in national development strategy priorities, including sustainable economic, social, and environmental goals. However, because the private sector will not make this transition by itself, states must be able to make such policy changes through appropriate financial regulation (Zhenmin 2018).

Because markets do not operate fairly or in the public interest without well-considered and well-enforced rules set by governments, it is critical that new policies and rules are established that can transform global finance by reducing its dangerous size and strengthening its beneficial roles. Such policies must include changes in prudential regulations, capital requirements, investment-firm culture and executive compensation, which will require new and more appropriate longer-term benchmarks. Reforms to accounting practices, especially for illiquid investments, will also be necessary, for example, to reduce the short-term bias introduced by mark-to-market accounting; and institutional investors must adopt a broader interpretation of fiduciary duty, which should focus on the long term and incorporate all factors that have a material impact on returns, be they financial, environmental, social, or governance-related (Zhenmin 2018).

The fact that the securitization initiative is being promoted in such a high profile way by the G20 and leading DFIs despite all of the concerns listed above suggests that the current conjuncture reflects an intensified contest between those supporting the public interest and those supporting the private interest.

Four decades ago, President Ronald Reagan in the United States and Prime Minister Margaret Thatcher in the United Kingdom promised their respective financial sectors they would be "freed" from "financial repression" – or the high levels of regulation that had prevailed in the 1950s, 1960s and 1970s. Under free market policies, the financial markets were set free and have expanded in size and scope ever since, bringing greater financial instability and recurrent financial crises ever since. Today advocacy organizations focused on the public interest and issues such as poverty reduction, economic development, accountability in public finance, employment and financial stability must focus their mobilization efforts on reigning in the size and scope of private finance through new financial regulations at the local, national and international levels – including in the realms of development finance and the public resources made available to public lending institutions.

5. CONCLUSION

Rather than adopting the G20-DFI initiative for the financialization of development lending, new efforts must instead be focused on regulating finance and strengthening and expanding the role of public development finance, both at the international and national levels.

At the international level, the discussion in the United Nations Financing for Development conference in Addis Ababa in 2015, at which the mechanisms for financing the SDGs were established, was too quick to dispense with the role of public sector financing for development. The idea that public taxpayer-funded overseas development assistance (ODA) and other international public finance flows could play a prominent role in financing international development efforts was downplayed. There was a presumption that the current levels of public ODA – at about USD 150 billion annually – is the only level of aid possible. However, only a small fraction of countries is currently meeting the officially pledged international commitments to provide 0.7 percent of gross national income in ODA and public aid levels could be increased considerably if others would fully comply with their official commitments and if donor countries would walk the talk on the SDGs by mobilizing a massive "SDGs capital increase" for DFIs and MDBs using public ODA resources.

Additionally, new sources of international aid financing could be mobilized from the establishment of international financial transaction taxes. There are also a host of other new forms of global public taxes that could be established and expanded, such as on corporate incomes, offshore accounts, billionaires' net wealth, and polluting activities (Sachs 2018).

At a time when greater participation is required in more robust public debates about the best mechanisms for development finance, including public financing options, many civil society organizations and independent media are facing mounting constraints on their activities. All donors could do much more to support, defend and strengthen the role of civil society organizations generally, and of investigative reporters and human rights defenders in particular, in the face of an ongoing and unprecedented rollback of rights and freedoms in many countries where they lend and provide financing (Barat 2017; TAI 2019). Donors should use their influence in constructive ways to ensure civic space is strengthened and defended and debates about policy options are widened.

Despite all the massive numbers thrown around in terms of projected trillions of dollars needed to fill in the "infrastructure financing gap" needed to meet the SDGs, Griffiths and Romero (2018) showed there is actually little evidence that "traditional" public funding sources cannot fill the gap. While the big numbers tossed around seem overwhelming, when measured in terms of investment as a percentage of gross domestic product (GDP), analyses by the McKinsey Global Institute showed the world requires a relatively modest increase from 3.8 to 4.2 percent of global GDP, and similar estimates by the United Nations Conference on Trade and Development showed that the increase needed is from

3.8 to 5.0 percent of global GDP (Griffiths and Romero 2018). Thus, the order of magnitude involved with donor countries using public resources for mobilizing a "SDGs capital increase" for MDBs is not as farfetched as is often claimed.

Additionally, much more can be done at the national level in developing countries to mobilize more resources domestically. The scaled-up use of public development banks, the adoption of more progressive income tax and wealth tax systems, and efforts to crack down on tax evasion, tax avoidance and trade misinvoicing can all become important new sources of domestic capital for development financing in countries that demonstrate the political will.

Lastly, it is also critical that lessons are learned from the history of successful developmental states on the importance of using industrial policies to support long-term structural transformation of national economies towards the development of manufacturing sectors and manufacturing-related services that pay higher wages, reduce poverty and build up the national tax base. In this context, national infrastructure development must be about supporting national development strategies, and about supporting the health, education and mobility of the workforce and the general population over the long-term; It must not only be about the ability of individual users to pay market rates high enough to attract private investors in the short-term.

This makes infrastructure development a public policy imperative which is clearly rooted in the long-term public interest. Doing so requires the ability of states to adequately regulate the domestic financial sector and direct flows of credit to productive economic activities that support structural transformation – something that cannot be achieved under the financialization of development finance.

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