TRANSITION FINANCE COMPENDIUM: CHALLENGES AND RECOMMENDATIONS FOR THE DEVELOPMENT ASSISTANCE COMMITTEE

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Abstract

Official development assistance (ODA) promotes the long-term sustainability and inclusiveness of growth and development. At certain stages of development, in certain contexts or sectors, ODA remains the main source of financing for development partners. This comes with exit and phasing out risks: how to reduce dependence on ODA and ensure a smooth transition to other forms of financing,[1] in particular domestic and private, without creating financing gaps or development setbacks? While the focus in the literature and policy discussions has been placed on the specific milestone of ODA graduation, our analysis suggests that those risks arise much earlier in developing countries' transition from low to high income. It also suggests that ODA trends should not be observed in isolation of other sources of financing for sustainable development since transition finance is about the progressive substitution of external financing by domestic public resources and the mobilisation of private investment.

This Transition Finance Compendium concludes that more could be done to build the resilience of ODA, particularly relating to efforts to help domestic resource mobilisation and market creation (private sector development and investment), quantitatively as well as qualitatively, i.e. maintaining the development footprint in all of its dimensions (e.g. efficiency of public spending, quality of foreign direct investment, boosting local productivity).

Foreword

In the communiqué issued at its 2017 High Level Meeting, the Development Assistance Committee (DAC) set an objective for itself "to better understand the broad catalytic effect of official support and other resources by understanding the interlinkages among official development assistance (ODA), partner countries' domestic resources, private investment, remittances, philanthropy, trade finance and export credits, and other sources of finance", and to "continue to collaborate with other experts within the OECD and beyond in order to have a global overview and outlook on financing for development" (§15).

Responding to this call, the OECD Development Co-operation Directorate launched a new line of work called "transition finance", first presented to the DAC at its February 2018 formal meeting, and since then updated at several formal and informal DAC meetings and international events. Applying a novel approach, the transition finance work stream has produced a methodological working paper that outlined the analytical basis of this new framework and carried out seven pilot studies over the course of 2018-19 on countries facing different transition challenges: Cabo Verde, Chile, Lebanon, Solomon Islands, Uganda, Viet Nam and Zambia.

The Transition Finance Compendium closes this series, addressing the lessons learnt over the two years during which this work has been undertaken. It highlights the main findings and recommendations, which have implications for the DAC's future, while offering some strategic guidance on how the DAC can itself transition to a better adapted approach to development co-operation.

This Compendium was supplemented by a website, the Transition Finance Toolkit, which offers further methodological guidance for undertaking country diagnostics, online tools for development partners to conduct their own analysis and fact sheets covering different transition milestones.

This working paper is the result of a study commissioned by the government of Spain in order to compile the lessons learnt from the seven country pilots carried out by the Development Co-operation Directorate Secretariat under the transition finance work stream between 2018 and 2020. Special thanks for their support go to AECID, Cooperación Española.

We also reiterate our gratitude to the international cooperation agencies of Ireland, Japan, New Zealand and Portugal who cooperated throughout the development of the transition finance work stream.

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Abbreviations and acronyms

DAC	Development Assistance Committee
DCD	Development Co-operation Directorate
DRM	Domestic resource mobilisation
EU	European Union
GDP	Gross domestic product
GNI	Gross national income
GVC	Global value chain
IDA	International Development Association
IMF	International Monetary Fund
LDC	Least developed country
LIC	Low-income country
LMIC	Lower middle-income country
MIC	Middle-income country
ODA	Official development assistance
ODF	Official development flow
OOF	Other official flows
R&D	Research and development
SDG	Sustainable Development Goal
SIDS	Small island developing states
UMIC	Upper middle-income country

Executive summary

Managing risks or transition more broadly is key to aid effectiveness and resilience. Building on the evidence collected through seven country pilots, it appears that the Development Assistance Committee (DAC) could do better at managing transition by conducting systematic and dynamic diagnostics of partner countries' needs and better co-ordinating responses to the challenges they face.

Further planning and co-ordination of DAC members' exit and phasing out strategies or decisions could generate official development assistance efficiency gains and resilience. First, better transition management could help reduce observed risks of socio-economic setbacks or development traps, financing gaps, and increased pressure on developing countries left behind. Second, it would help optimise the catalytic role of official development assistance (ODA)[2] and ensure a smooth transition to other sources of financing while preserving the long-term prospects of inclusive and sustainable development. For example, it appears as a paradox that efforts to create markets are lacking in sectors that are highly dependent on ODA, such as social sectors, creating significant financing gaps as countries transition (when the highest potential transformational effects of creating markets are precisely in those sectors).

The increasing complexity of the financing for sustainable development landscape creates opportunities but also risks for access to additional sources of financing. The long-term benefits of DAC efforts might be lost if transition is unprepared and ODA is substituted by other sources of financing that do not have similar levels of quality. Not all financing for sustainable development actors have the same standards, e.g. in terms of debt sustainability. Not all financing for sustainable development actors have the same interests: for example, the People's Republic of China's management of transition looks different from the DAC's, with less interest in financing social sectors but a faster and more efficient mobilisation of private resources. In addition, evidence points at aid trade-offs linked to portfolio management strategies that change as countries transition, creating a disconnect between countries' financing needs and external financing supply.

Finally, an increasing amount of available financing for sustainable development diagnostics creates further segmentation of the financing for sustainable development landscape and strategies. Different actors (including across the DAC) have different incentives and strategies and, in the absence of alignment mechanisms, DAC resource allocations may become suboptimal. There is a strong case for integrating those diagnostics into national development financing strategies.

Recommendations

To better prepare for transition, the DAC could:

- Adopt guiding principles and put mechanisms in place for better planning and co-ordinating transition (e.g. of budget support groups).
- Introduce transition management into discussions revamping the effectiveness agenda, and integrate key benchmarks into peer reviews or other forms of monitoring.
- Explore the idea of transition management of grants or loans.
- Establish a “transition club”, that could be of particular relevance to small island developing states and monitor co-operation beyond ODA.

To build the resilience of external assistance, the DAC could:

- Discuss and plan phasing out mechanisms. DAC members could further explore the question of domestic resource mobilisation and increase related efforts to ensure a better connection between intentions and actions.
- Boost efforts to create markets and increase the development footprint of private finance and investment.
- Work on strengthening the development co-operation/investment nexus through institutional reforms in DAC countries (continuity of action across ministries) and renewed dialogue of the DAC and the OECD Investment Committee (through regular meetings, joint work streams, joint country assessments and provision of solutions).
- Improve dialogue with the private sector to build the resilience of ODA, identifying financing risks and opportunities.
- Review the role of aid for trade as a key element of the development co-operation/investment nexus.
- Scale-up collaboration and joint work across OECD committees and directorates to optimise the management of transition.

To address risks and trade-offs, the DAC could:

- Introduce multidimensional development indicators to manage transition, heeding the “warning signals” in financing for sustainable development strategies.
- Create a mechanism for financing for sustainable development technical assistance and capacity building.
- Identify and promote core DAC principles on financing for sustainable development that should include transparency of financing at all levels of governance (to be articulated with other principles such as those of the Paris Club’s).

To move from diagnostics to implementation, the DAC could:

- Undertake mapping exercises to identify financing opportunities, both at the DAC level and at the country level.
- Ensure country ownership and better align with country strategies and financing needs, including, when appropriate, through the integration of the DAC perspective into integrated national financing frameworks.

1 Introduction

The Addis Ababa Action Agenda underscored the need for a holistic approach to financing the 2030 Agenda: it called on all available resources, domestic and foreign, public and private, in support of the Sustainable Development Goals. With a view to helping its implementation, the transition finance work undertaken by the Development Co-operation Directorate (DCD) has attempted to explore the evolution of the availability and interactions of different sources of financing for sustainable development as countries develop and reach higher levels of income.

The underlying objective under the transition finance work is to design strategies for optimising financing mixes in specific country contexts – with a particular focus on the role and catalytic effects of official development assistance (ODA). In order to secure a smooth and resilient phasing out from ODA, a situation that all developing countries should address one day or another, the transition finance work looks to provide the OECD DAC with recommendations on how to make the best use of scarce public resources, leveraging other sources of financing for sustainable development, and avoiding country- or sector-specific financing gaps as countries transition.

This work developed new concepts and methodological tools for assessing the capacity of developing countries to finance sustainable development, and the performance of DAC members in managing the transition of their development partners – i.e. building the resilience of their efforts and avoiding financing gaps or socio-economic setbacks as ODA progressively phases out until the country reaches a high-income level.

Box 1.1. The OECD/DCD Transition Finance Roadmap

The DCD Transition Finance Roadmap sets the scene with the concept note "Transition finance: Introducing a new concept" (Piemonte et al., 2019[1]), which provided the analytical basis of this framework. Additionally, seven country pilots (Cabo Verde, Chile, Lebanon, Solomon Islands, Uganda, Viet Nam and Zambia)[1] carried out in 2018-19 applied further evidence to the theoretical basis and helped develop concrete knowledge on policy issues. Lastly, the Transition Finance Toolkit website provided the Development Assistance Committee (DAC) with online interactive tools to reproduce portfolio management exercises using the ABC methodology (assessment, benchmarking and counselling) (Kim and Poensgen, 2019[2]) (Chiofalo, Poensgen and Rockenfeller, 2019[3]); (Cattaneo, Piemonte and Poensgen, 2020[4]) (Piemonte and Fabregas, 2020[5]) (Thompson, forthcoming[6]) (Morris and Cattaneo, 2018[7]); (Kim et al., 2019[8]).[2]

Notes: 1. The selection of this group of pilot countries was done in consultation with DAC members, who provided financial and logistical support for their completion. All country pilot studies are available at: www.oecd.org/dac/transition-finance-toolkit. 2. More details are available at: www.oecd.org/dac/transition-finance-toolkit.

The following chapters summarise some of the key challenges of transition finance and, building on the evidence collected through seven country pilots (Cabo Verde, Chile, Lebanon, Solomon Islands, Uganda, Viet Nam and Zambia – representative of different stages of transition, geographies and specific

vulnerability contexts), provides recommendations and concrete solutions for their implementation by the DAC.

Two main conclusions from the country pilots

1. Each transition milestone needs to be equally prepared: no single milestone is more important than the others.

- Nevertheless, focus on ODA graduation has over-shadowed the challenges of other milestones (e.g. graduation from low-income country or least developed country [LDC] status; see Box 1.2).
- On average, the DAC's management of transition has been suboptimal.

Box 1.2. Graduation from low-income country and least developed country status, what does the evidence tell us?

Zambia's transition from low-income to lower middle-income country status could have been better managed

Up until the early 2000s, Zambia's reliance on official development flows was significant. However, with growing income levels, the importance of official development finance from Development Assistance Committee (DAC) providers decreased: as a share of gross national income, from 23.0% in 2000 to 12.7% in 2006 and further to 4.9% in 2010. Several DAC providers decided to exit or scale down their operations as the country joined the lower middle-income group in 2011. Denmark and the Netherlands announced a phase-out in 2011, Norway closed its embassy in 2016. This happened without any co-ordination or securing the transitioning of important co-operation activities, as the domestic tax reform technical co-operation project led by Norway of helping to build the capacities of the Zambia Revenue Authority to ensure its long-term sustainable financing of development stopped from one day to the next.

Graduating from least developed country status, Solomon Islands' encouraging experience

Solomon Islands is expected to graduate from the least developed country (LDC) category in 2024. However, the direct implications of its graduation from the LDC category are expected to be largely manageable. The country's main development partners (Australia, Japan, New Zealand and the United Kingdom)* do not anticipate a decline of their official development assistance flows following Solomon Islands' graduation. In addition, one of the main effects anticipated by the government and its development partners – the loss of European Union (EU) trade preferences for the country's exports of fish and agricultural products – has been mitigated through the signing of an Interim Economic Partnership Agreement with the EU in late 2019.

* Note that such ODA allocation decisions also respond to geostrategic concerns and historical ties.
Sources: Piemonte, C. and Fabregas, A. (2020[5]), "Transition finance in Solomon Islands: Preparing for graduation from least developed country (LDC) status", https://doi.org/10.1787/a4739684-en; Kim, J. et al. (2019[8]), "Transition finance challenges for commodity-based least developed countries: the case of Zambia", https://doi.org/10.1787/feb640fe-en.

2. More efforts could be made to build the resilience of ODA.

- Support for domestic resource mobilisation and market creation (private sector development and investment promotion) could be increased, in particular in sectors that are the most dependent on ODA and at early stages of development.

- Some sectors still have transition finance gaps (e.g. social sectors), while others have surpluses (e.g. infrastructure), suggesting that country/context approaches should be supplemented by sector-specific strategies and an overall balance of financing (Box 1.3).

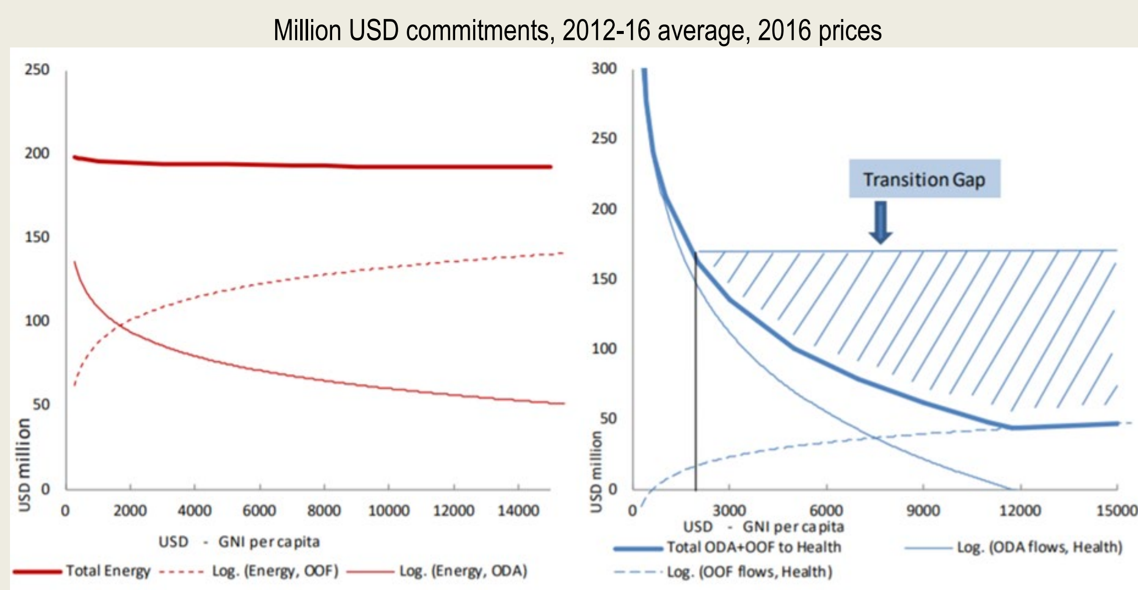
These efforts could result in further efficiency gains benefiting both the DAC and its development partners: for the DAC, an optimal management of transition results in efficient resource allocations, greater impact and resilience of efforts; for countries in transition, it would result in avoiding gaps, less exposure to debt sustainability risks, and avoiding socio-economic setbacks or development "traps" at different stages of transition.

Box 1.3. Transition gaps: What is different in productive and social sectors?

Illustrating how official development flows (official development assistance [ODA] and other official flows [OOF] financing) is deployed along the development continuum can help identify if there are any different behaviours among sectors; that is, if there are specific sectoral financial specificities as countries become richer. As sketched in Figure 1.1, transition (or the substitution between ODA and OOF) can result in either a financing surplus or a financing gap.

Figure 1.1. There is no financial gap in energy, while the transition gap in the health sector seems deep and permanent

Million USD commitments, 2012-16 average, 2016 prices



Source: Piemonte, C. et al. (2019[1]), "Transition finance: Introducing a new concept", https://doi.org/10.1787/2dad64fb-en.

In the energy sector (Figure 1.1, left panel), there is a perfect substitution between ODA and OOF, with a constant level of financing throughout the transition spectrum, from low- to high-income levels. In the case of the health sector, however (Figure 1.1, right panel), an extremely wide transition gap results from the sum of both flows. Development Assistance Committee members should be particularly vigilant when such a picture emerges, because it could translate into a situation of "everything to nothing". Indeed, high dependence on ODA increases the acuteness of transition finance challenges and the need to deploy resilience measures.

Source: Piemonte, C. et al. (2019[1]), "Transition finance: Introducing a new concept", https://doi.org/10.1787/2dad64fb-en.

The following also calls for a greater emphasis on the qualitative dimensions of financing for sustainable development rather than a plain “accounting approach”. This places the DAC in a role not only as a global financier, but also as a global shaper and standards setter. Indeed, as ODA phases out, certain objectives and values espoused by the DAC need to be adopted by other financing for development actors – whether domestic or foreign, public or private. Building the resilience of ODA would ensure that a country’s growth remains inclusive and sustainable as ODA phases out. This requires anticipating substituting ODA by other sources of financing, and building capacities or an environment conducive to certain virtuous behaviours of private investors (e.g. responsible business conduct) and public institutions (e.g. public spending efficiency). It also highlights the opportunity for DAC members to modernise their understanding of existing effectiveness principles and commitments in transition contexts, reinforcing country ownership, transparency and inclusive partnerships in such settings.

The concept of “resilience of ODA” refers to the long-lasting effects of ODA, implying no development setbacks, even after phasing out.

2 Planning for transition

A proper planning of transition is needed to build the resilience of the Development Assistance Committee's (DAC) efforts as they are phased out and to encourage other actors to step in to avoid financing gaps and development setbacks.

Developing dedicated principles and instruments

Observing – What are the issues?

From covering least developed country (LDC) to official development assistance (ODA) graduation, and spanning several regions (Africa, Asia, Pacific, Latin America and the Caribbean) and country conditions (small island developing states [SIDS]/land-locked developing countries), the sample of pilots reveals some of the key challenges of transition finance. Table 2.1 showcases, very succinctly, the evidence collected through the pilots.

Table 2.1. Has the Development Assistance Committee adequately reacted to different phase-out stages of assistance?

Country studies	Stage of transition	Actions undertaken by the DAC	Actions still needed
Cabo Verde	Least developed country (LDC) graduation	Tariff exceptions lost because of LDC graduation were renegotiated to adapt for transition. However, debt levels skyrocketed and official development assistance (ODA) was tied and did not focus on the main needs.	Focus on country priorities and adapt adequate ODA grant vs. loan assistance; untied aid; advise and help the country negotiate appropriate and sustainable debt levels and conditions.
Chile	ODA graduation	Essential technical co-operation projects funded by donors disappeared as donors left (were not locally budgeted).	Focus on sustainable growth (leverage domestic resource mobilisation, fight inequalities, build capacity) to prevent setbacks; avoid portfolio management loan allocation that can be contracted by the market.
Lebanon	Upper middle-income country facing migration challenges	Risk of pernicious dependence on aid; donors intensively financing social sectors.	Focus on improving local capacity to absorb aid projects; focus on helping develop an adequate tax system, leveraging domestic resource mobilisation; co-ordinate with multilaterals to provide safety nets to ensure continuity.
Solomon Islands	LDC graduation	Some efforts were made to envisage renegotiations on lost tariff exemption; nevertheless, transition should be addressed more broadly.	Advise and help the country negotiate appropriate and sustainable debt levels and conditions; improve regulation to allow private sector development; focus on domestic resource mobilisation.
Uganda	Low-income country (LIC)-LDC-land-locked developing country facing migration challenges	Some efforts have been made by the DAC community to reduce Uganda's humanitarian burden (BRAER from the United Kingdom, the CRRF model).	Focus on increasing domestic resources (currently as low as 13.8% of GDP); prevent an increase of non-concessional loan levels (from DAC but also China); contribute to decreasing the high youth unemployment rate.
Viet Nam	LDC graduation, highest growth rate in the world	Some members like the United Kingdom and the United States have shifted their support to build private sector ecosystems.	Better address the move from donor-financed to private-financed solutions; focus on sustainability of growth (quality of investments, debt issues); focus on derisking the possibility of a middle-income trap (productivity losses in view).
Zambia	LIC to lower	No programmed exit strategy when the	Better address existing strategies; help to monitor

	middle-income country (LMIC)	country surpassed the LMIC threshold.	indebtedness levels; diversify DAC presence in other sectors (not only health); encourage domestic resource mobilisation; help engage the private sector.

Notes: In the case of Cabo Verde, the Development Co-operation Directorate conducted an *ex post* study in 2018 of its LDC graduation (2007); in the case of Solomon Islands, the Development Co-operation Directorate focused on its LDC graduation as an *ex ante* exercise (scheduled in 2024).

Coherence and co-ordination of the solutions proposed to manage the transition may fall short of the challenges faced by partner countries. DAC members' decisions to exit, phase-out or re-enter a country do not necessarily respond to any predictable patterns, in spite of existing transition milestones. This created difficulties for both DAC members (co-ordination gaps) and partner countries (financing gaps), affecting the effectiveness of aid.

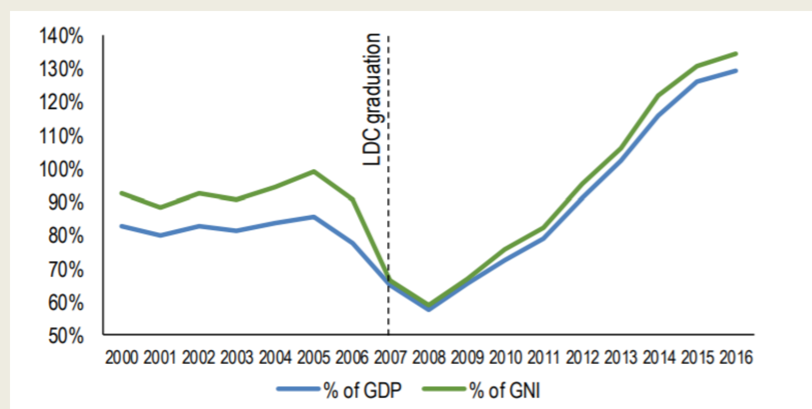
For example, the phasing out from Cabo Verde did not coincide with the country's LDC graduation (on the contrary, ODA, especially loans, increased after LDC graduation; see Box 2.1); however, the country subsequently faced limitations in its borrowing capacities set by the International Monetary Fund. In Chile, for decades before graduation from ODA, the government did not rely on ODA, but rather on foreign direct investment and domestic private investment.

Box 2.1. External debt increased substantially after Cabo Verde's least developing country graduation

In 2016, Cabo Verde was classified at "high risk" of debt distress for the first time by the International Monetary Fund. Figure 2.1 shows that that year, debt reached 134% of GNI. Debt levels of public enterprises including Cabo Verde Airlines and the social housing company IFH were close to 20% of GDP. The largest share of the total debt composition (45%) was provided by multilateral actors.

Figure 2.1. Government debt increased quickly following Cabo Verde's graducation from least developed country

General government debt over time



Source: Morris, R. and O. Cattaneo (2018[7]), "Cabo Verde transition finance country pilot", https://doi.org/10.1787/1affcac6-en.

Moreover, some DAC members providing grants leave earlier, when loan providers step in, and those leaving sometimes compete among themselves or with the private sector as concessionality declines. Each DAC member seems to focus on its core business. Co-ordination takes place in some circumstances

(e.g. budget support group, debt sustainability group), but not throughout the whole transition spectrum or as part of an integrated financing strategy (e.g. to achieve the Sustainable Development Goals [SDGs]) (Box 2.2).

Box 2.2. Concessional flows to investment projects in Chile previous to its official development assistance graduation

In the period 2010-17 (Chile graduated from the List of ODA Recipients in 2018), official development assistance (ODA) was mainly allocated in the form of loans, and provided by the German development bank (KfW) and the European Investment Bank, and focused on investment projects in the energy sector. However, some of the credits were finally cancelled due to better financial conditions offered by a private creditor, meaning that the country was able to get credit at competitive conditions to provide this kind of financing, and that ODA was not essential to finance, at least, this kind of investment. The latter case raises questions on the indispensability of ODA loans to Chile at its stage of development, instead of allocating ODA resources to more demanded objectives, such as the fight against inequalities and environmental problems.

Source: Cattaneo, O., C. Piemonte and K. Poensgen (2020[4]), "Transition finance country study of Chile: Better managing graduation from ODA eligibility", https://doi.org/10.1787/608cbf6d-en.

This kind of "divergence of interests" across the DAC is sometimes replicated with multilateral organisations. For example, in Viet Nam, some DAC members criticised the fact that, after IDA (International Development Association) graduation, demand for grants dried out as the country was guided towards other types of instruments. It also appeared that multilateral and national development banks sometimes have diverging interests.

Last but not least, the studies highlight the need to focus especially on indebtedness as an overarching challenge, and the imperative to acknowledge the presence of new actors in the development co-operation landscape. The following sections suggest how the DAC could react and better prepare the phasing out of their ODA.

Proposing: What are the possible solutions?

Transition management strategies need to be implemented. In order to avoid development setbacks and to build the resilience of ODA as DAC members phase-out their contributions, they could better prepare and co-ordinate exit/re-entry among themselves and with partner countries.

A set of guiding principles could be developed to guide the DAC in managing transition. These could be elaborated around two pillars: 1) *vis-à-vis* other DAC members: early warning co-ordination mechanisms could help avoid financing gaps and bolster the effectiveness of other DAC members' operations (e.g. ensure as Norway exits Zambia that another DAC member continues its work; see Box 1.2); and 2) *vis-à-vis* partner countries: an early warning mechanism and capacity building to avoid financing gaps and development setbacks, i.e. to ensure the sustainability of financing key sectors such as health or education (for example, ensure proper funding of vaccination efforts in Viet Nam after graduation from GAVI, The Vaccine Alliance.

The management of transition finance could be mainstreamed in peer reviews and help the revision of effectiveness principles. DAC delegates' occasional participation in transition finance country diagnostics could link capitals and field representations, contributing to a better assessment of the co-ordination and alignment challenges.

Beyond the sum of the individual interests and priorities of its members, the DAC could further work on building more coherent, holistic approaches to financing strategies. Guiding principles would include the necessity for members to discuss and plan their phasing out.

Box 2.3. Highlighting Development Assistance Committee members' good transition practices in Solomon Islands

The major donors in Solomon Islands (Australia, Japan, New Zealand and the United Kingdom, as well as multilateral actors such as the Asian Development Bank) currently meet once a month to share information and co-ordinate action in the field. Their information exchange helps them anticipate and co-ordinate their interventions, avoiding duplication of effort. Moreover, thanks to this co-ordination, it appears that the Solomon Islands' least developed country (LDC) graduation (scheduled for 2024) will not have any major, direct financial implications for the country as no Development Assistance Committee (DAC) member plans to change its mostly grant-ODA assistance in the coming years.

Furthermore, all DAC providers interviewed during a Development Co-operation Division's technical mission to Solomon Islands confirmed that LDC graduation is not an eligibility criteria for their ODA support. However, some providers, such as Australia, do have a long-term transition strategy to progressively transfer additional responsibilities to the Solomon Islands government in sectors such as health, with a view to ensure government ownership and prepare the country for a smooth transition.

Source: Piemonte, C. and A. Fabregas (2020[5]), "Transition finance in Solomon Islands: Preparing for graduation from least developed country (LDC) status", https://doi.org/10.1787/a4739684-en.

The use of transition finance country diagnostics such as, for example, the Transition Finance Toolkit,[3] to assess the performance in managing transition and designing effective holistic financing strategies could be of special interest to better co-ordinate phasing out. It could be used by both donors and partner countries, informing transition finance assessments and helping each developing country position itself in the transition continuum, thereby helping it to better anticipate the substitution of different sources of financing (including in specific contexts, for example SIDS, LDCs and countries in fragile contexts). Furthermore, the transition finance fact sheets also developed under this toolkit foster a better understanding of the criteria, impact and challenges associated with key transition milestones (e.g. from low-income to lower middle-income countries, or graduation from the least developed country category) and thereby better prepare all parties.

Finally, the idea of transition management grants or loans could be usefully explored. With a view to locking in resilience building in the phasing out of ODA or planning the exit of specific DAC members, such mechanisms already in use in multilaterals or global funds for specific graduation milestones could be of interest in addressing specific transition finance challenges. Such targeted instruments could have the following components:[4]

- Identify risks associated with transition and raise awareness with the government, including through a better preparation of substitution by other sources of financing of key sectors or activities.
- Mobilise domestic resources and create markets to secure a smooth financing transition without adverse impacts on growth or redistribution.
- Include quantitative and qualitative dimensions (i.e. preserving the level and quality of financing) on the basis of transition finance country diagnostics.

Better handling transition beyond official development assistance graduation

Observing: What are the issues?

From a DAC perspective, ODA graduation is a key transition milestone that has long monopolised the attention of the development community and its observers. It used to be a “point of no return”, without provisions on the possible scenario of reinstatement on the DAC List of ODA eligible countries, even in case of serious adverse shocks. The 2018 dramatic hurricane season shed new light on the issue, prompting the DAC to reconsider the reinstatement under certain conditions (see §21 in OECD (2017[9])) and later agree to a mechanism to operationalise it.

Evidence collected in transition finance diagnostics helps to de-dramatise this debate. Focusing on the resilience of ODA and the preservation of mutually beneficial relationships beyond graduation rather than just accounting considerations, it appears that:

1. Graduation from ODA is just one of the many milestones of the transition journey, and often not the hardest hurdle to overcome.
2. When handled poorly, graduation results in missed opportunities for deepened technical co-operation and smooth transition in some areas of priority of the DAC.
3. There is a strong case for the DAC to pay attention to “warning signals”, beyond GDP per capita, to better prepare for ODA graduation.
4. There is space for mechanisms to be put in place to build the resilience of ODA and provide mutual benefits in relationships beyond ODA.
5. Solidarity does not end with ODA graduation, and a return of the DAC in case of serious adverse shocks as well as continued co-operation in areas such as global public goods should be possible.

Transparency should be increased to get a more accurate picture of co-operation after graduation. A main issue is one of data – or lack thereof – about post-graduation co-operation. The collection of data on aid stops with graduation, sending the wrong signal that co-operation itself comes to an end. As observed in the country pilots, co-operation might actually increase after graduation and take new forms (e.g. linked to regional integration or peer-to-peer technical co-operation).[5]

Sometimes, the scope of partnership may actually broaden after graduation, but is not monitored or measured. Hence, there are common misperceptions about the impact of ODA graduation. The example of Chile shows that the phasing out of ODA and the DAC’s presence starts well ahead of the formal graduation process. The “soft” part of DAC projects (i.e. technical assistance, knowledge transfer) is actually more essential to partner countries as they reach high-income status than the “hard” part (i.e. the financing). At the time of graduation, only some rare technical assistance and infrastructure projects at above-market rates remained in Chile. Thus, the main challenges observed in the case of Chile were related to changes in communication and co-operation channels, as well as in responsibilities across government parts. Better managing transition would require learning about those changes and adapting the forms of dialogue and co-operation.

The discontinuation of DAC-sponsored technical assistance projects raises questions of country ownership and alignment of DAC and partner country priorities. For example, if transition to renewable energy is a priority for the DAC, and the DAC is still involved in its financing up to graduation, it would be important to ensure that investment in renewable energy remains a commitment and is budgeted accordingly.

ODA is often channelled through ministries of foreign affairs and development co-operation agencies. After graduation, peer-to-peer technical assistance is more likely to take place directly among technical ministries. In the case of Chile, all requests for support had to be channelled through the regular budget (i.e. Ministry of Finance) instead of through the Ministry of Foreign Affairs as it was done previously, creating tensions after graduation by not being budgeted.

ODA graduates have to make the most of peer-to-peer technical assistance opportunities through triangular co-operation. Indeed, ODA graduates can grow into development co-operation providers in their own right and engage in South-South co-operation. Also, regional integration, mainly through regional organisations, should be further and more systematically explored. For instance, for Chile, it is currently also possible through its OECD membership.

All of this points to an ecosystem of aid delivery. This raises the questions once again of DAC members returning to a country that had reached high-income status but who then experienced a significant drop in GDP as a result of an adverse shock (e.g. natural disaster or conflict; see Box 2.4). Thus, as development partners leave a country, those involved in the "business of aid" tend to leave as well (e.g. non-governmental organisations or contractors) and returning can be difficult if the aid ecosystem is no longer in place. For example, in Lebanon, the return of donors and massive commitments raised the question of the local governments' absorption capacity and good governance practices. It also raises the question of greater international dependency and persistent inequalities (e.g. in the case of national social security schemes).

Box 2.4. Will the COVID-19 crisis result in the first official development assistance graduates to be reinstated on the Development Assistance Committee's List of ODA Recipients?

In light of the results obtained when analysing the exposure to the economic consequences of the COVID-19 crisis in small island developing states (SIDS), it could be expected that middle-/upper-income SIDS, relatively less ODA-dependent, will be those suffering the most from the crisis. Furthermore, and depending on the duration of the crisis, it could be possible to see the first (economic) reinstatements back onto the DAC List of ODA Recipients in the coming years: a country such as Antigua and Barbuda, candidate to graduate* from the DAC List of ODA Recipients at the time of its 2020 revision, could, shortly after having graduated from the list, be reintegrated onto it.

* According to World Bank data from 10 July 2019, Antigua and Barbuda exceeded the high-income threshold in 2017 and 2018. In accordance with the DAC rules for revision of the List of ODA Recipients, if it remains a high-income country until 2019, it will be proposed for graduation from the List of ODA Recipients in the 2020 review.

Source: Piemonte, C. (2020[10]), *Mapping the Economic Consequences of COVID-19 in Small Island Developing States* (SIDS), https://one.oecd.org/document/DCD/DAC(2020)35/FINAL/en/pdf.

Graduation from ODA does not mean the end of solidarity, in particular in regard to global public goods.[6] The 2030 Agenda and the SDGs are shared objectives for humanity, and the capacity of each country to reach the goals is linked to the capacity of others to reach them as well. The recent COVID-19 pandemic is the most blatant example of this. This raises questions about the justification for return after graduation from specific milestones (e.g. International Development Association or ODA) and the mixture of assistance after specific transition milestones. The World Bank is exploring the possibility to expand the type of facility used in Lebanon to address other crises (e.g. neighbouring countries affected by the crisis in Venezuela) and more broadly respond to global public bads.[7]

The underlying question is the role and definition of ODA. Is ODA serving development as an end or as a means to serve other purposes (e.g. security, health, export-led growth)? How can ODA be articulated with other foreign or domestic policy tools, such as peace-keeping interventions, migration policies, etc.? What are the technical assistance tools before and after ODA? What other tools can be used after ODA graduation that serve similar purposes (e.g. trade or co-operation agreements)? Graduation is not an end, but the beginning of new forms of co-operation.

Proposing: What are the solutions?

The lack of preparation and information as well as the management of the consequences of ODA graduation can be remedied. A "transition club" for ODA graduates could be part of the solution.[8] Such a club could also help facilitate a smooth transition for countries and maintain continuity of relations between DAC and partner countries.

The objectives of a transition club could include:

- the collection of information and data about co-operation after graduation
- the exchange of experiences among recent graduates to ensure a smooth transition, helping identify new channels and instruments of co-operation
- "mentoring" future graduates by sharing recent graduates' experience
- prolonging the development co-operation continuum beyond ODA graduation by providing guidance for technical assistance and other forms of co-operation and funding (including regional or global funds), triangular and South-South co-operation
- monitoring the risk of setbacks and identifying solutions to avoid them
- analysing the conditions of return of donors or re-enlisting on the DAC List of ODA Recipients after adverse shocks of significant magnitude
- creating a link with non-OECD member countries and providing advice about application for membership.

The graduates club could be backed by a budget or a multi-donor trust fund for the DAC to channel its support to recent graduates or accompany this transition (see the previous section on transition finance grants or loans).

A "transition club" could facilitate a smooth transition for graduated countries and maintain continuity of relations between DAC and partner countries.

Box 2.5. Triangular co-operation beyond graduation: The case of Chile

Currently, through the Fondo mixto de cooperación triangular Chile-España, Spain continues to co-operate with Chile as a pivotal partner post-ODA graduation. Similarly, the German Regional Fund for Triangular Co-operation in Latin America and the Caribbean, based in Santiago, Chile, regularly co-operates with Chile in the individual projects of the fund. Both funds operate through co-financing models with Chile and at times the beneficiary countries, so that official development assistance provided by Development Assistance Committee members is leveraged with contributions from the Latin America and Caribbean region. The US-Chile Trilateral Development Cooperation initiative promotes projects focusing on areas such as citizen security, social inclusion, improving agricultural standards and export promotion.

A formal "graduates club" could help Chile and other countries (scheduled to graduate or having already graduated) formally meet and benefit from peer learning. Through such a club, Chile could continue its engagement with DAC members as a pivotal partner in triangular co-operation, sharing its experiences and lessons learnt from its recent development path, and benefiting from the triangular partnership itself.

Source: Cattaneo, O., C. Piemonte and K. Poensgen (2020[4]), "Transition finance country study of Chile: Better managing graduation from ODA eligibility", https://doi.org/10.1787/608cbf6d-en.

3 Building resilience

Planning transition and phasing out/substitution of official development assistance (ODA) by other sources of financing should aim to build the resilience of Development Assistance Committee (DAC) members' efforts. This objective could be summarised as "No gap, no trap":

- No gap – the quantitative dimension: substitution of ODA by other sources of financing is secured so the country or specific sector or activity is not short of resources. This involves domestic resources mobilisation and the creation of market/promotion of private investment.
- No trap – the qualitative dimension: not all types of financing have the same qualities from a development perspective. It is not enough to preserve the level of financing; planning transition means securing its qualities and maintaining the inclusiveness and sustainability of growth (i.e. no development setbacks). ODA has a key role to play in building an environment conducive to a certain behaviour of government (e.g. capacity building, public spending efficiency) and business (e.g. business environment, investment climate, private sector development, responsible business conduct as they become main financiers of the economy).

Building resilience of efforts and preparing substitution/avoiding financing gaps should be at the centre of the DAC's ODA phasing out initiatives. In order to do so, the DAC could draw more broadly on OECD expertise. Four fronts are of special interest for the DAC: 1) the ODA environment (currently exploited by the DAC through its Secretariat's work on analysis/strategy); 2) the investment context through the OECD's Directorate of Financial and Enterprise Affairs; 3) the role of domestic resource mobilisation and taxes, through the OECD Centre for Tax Policy and Administration; and 4) together with the OECD Economics Department, the Development Co-operation Directorate could add the impact analysis of growth and redistribution to its intervention choices.

Supporting domestic resource mobilisation: Shared responsibility and efficiency of public spending

Observing: What are the issues?

No gap. Domestic resources are, by far, the largest source of financing for development. The DAC has repeatedly referred to the need for ODA to better support country-led domestic resource mobilisation as well as public financial management. Domestic resource mobilisation should be part of transition strategies and always built into DAC members' phasing out plans: domestic resource mobilisation is a guarantee of ODA resilience. Recognised in the Addis Ababa Action Agenda, domestic resource mobilisation was also elevated as a development priority by the Addis Tax Initiative, initiated by DAC members with over 30 countries and international development organisations. The Addis Tax Initiative pledged to double total technical assistance for domestic resource mobilisation and taxation initiatives by 2020. Also, numerous individual DAC members have initiatives to support this pledge and domestic resource mobilisation (DRM) or public financial management projects (Box 3.1).

Box 3.1. Learning from Norway's "tax for development" approach

Norway's tax for development programmes aim to help developing countries improve their tax systems and increase their tax revenues. The programmes focus on four areas: 1) capacity building to improve tax systems and strengthen tax authorities; 2) knowledge generation and dissemination of research findings in the areas of taxation and capital flight; 3) international co-operation efforts related to issues of taxation and capital flight; and 4) support to civil society to strengthen public engagement in taxation and capital flight issues.

Examples include: co-operation between the Norwegian Tax Administration and tax authorities in Mozambique, the United Republic of Tanzania and Zambia on improving effectiveness and increasing the countries' tax revenues. It also includes research programmes on taxation, development and capital flight. Norway is an active supporter of the OECD's work on taxation and development and also supports other international and local organisations working on tax issues in partner countries.*

* Other DAC members have also been active in developing domestic resource mobilisation programmes and initiatives. See, for example, the Irish approach at: https://www.irishaid.ie/media/irishaid/publications/DRM-Brochure.pdf.

Source: Chiofalo, E., K. Poensgen and Y. Rockenfeller (2019[3]), "Transition finance country study Lebanon: Global public goods and the response to adverse shocks", https://doi.org/10.1787/25aa14e0-en.

No trap. It is not only about quantity, but also about the quality of funding and DRM projects need to be carefully crafted to include public financial management considerations (i.e. collect more, spend better approach). In the case of Viet Nam, while the graduation from the Global Fund was compensated by budgetisation of the same amounts and domestic resource mobilisation built into the phasing out, the government shifted resources away from research and development of new vaccines and encouraged local sourcing to the detriment of innovation and cost-efficiency.

This raises a number of questions about the conditions necessary for domestic resource mobilisation to be successful:

- How to bolster the efficiency of public spending? Less could be more. There seems to be a need for the DAC to increase its focus on building institutions and capacities as part of transition planning (e.g. Zambia Revenue Authority; see Box 1.2).
- How to reduce corruption and government inefficiency? For example, in Zambia, the lack of transparency for some procurement in infrastructure exacerbated the risk of debt crisis. There seems to be a need to secure substitution of sources of financing through governance improvements so as to not increase debt problems as the country transitions (see the section below on warning signals).

Proposing: What are the solutions?

DRM efforts need to be increased, and DAC members could more systematically include DRM and public financial management as part of their transition strategies and planning. Transition finance grants or loans could have a built-in DRM and/or public financial management component.

Transition finance diagnostics could be improved to better assess the respective roles and synergy of external and domestic resources, as well as the impact on growth and redistribution of transition from one source of financing to another. Financing strategies could identify optimal financing mixes, including measuring the impact on growth and redistribution. Transition strategies should include both domestic resource mobilisation and public financial management and private investment mobilisation or market creation. All three types of expertise (ODA, tax, investment) need to be combined in one assessment. For

example, together with the Centre of Tax Policy and Administration, the Development Co-operation Directorate explored the consequences of graduation from the Global Fund in Morocco – and it appears that before the Global Fund left the country, the staff in the Ministry of Health could have benefited from being trained to maintain technical discussions with the Ministry of Finance and other counterparts in order to anticipate future adequate budgeting (OECD, 2020[11]).

Fostering private sector finance: Creating markets

Observing: What are the issues?

No gap. ODA efforts to create markets and promote investment should be increased. Private investment is driven by market, portfolio and production strategies, and transition finance analysis confirms that attracting foreign direct investment[9] could be challenging for countries in the early stages of development and/or in specific contexts (e.g. least developed countries [LDCs], small island developing states, fragile contexts) or sectors (Box 3.2).

Box 3.2. Looking to increase private investment in developing countries: The example of the EU External Investment Plan

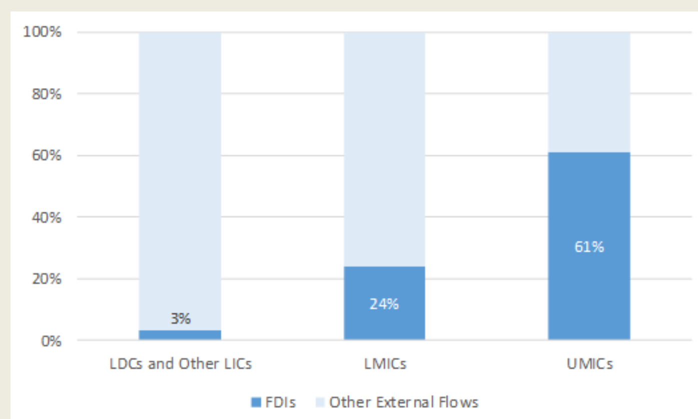
The External Investment Plan was adopted in September 2017 to help boost investment in Africa and the European neighbourhood. Its aim is to contribute to the Sustainable Development Goals while tackling some of the root causes of migration, and to mobilise/leverage sustainable public and private investments to improve economic and social development (with a special focus on job creation).

Over a two-year period (2018 to January 2020), the External Investment Plan signed 34 agreements for EUR 4.6 billion that is expected to mobilise ten times this amount (EUR 47 billion). These agreements consist of EUR 3.1 billion from existing investment facilities from the European Fund for Sustainable Development (EFSD) budget, combined with additional EFSD guarantees totalling EUR 1.54 billion.

Such initiatives are important to boost private investment in the more needed contexts. Indeed, private investment is almost inexistent in least developed countries (LDCs): foreign direct investment represents only 3% of all total external inflows (24% in lower middle-income countries and 61% in upper middle-income countries) (Figure 3.1).

Figure 3.1. As countries transition to higher gross national income per capita, foreign direct investment inflows become more prominent over all external inflows

2015-17 average, USD disbursements



Notes: LDCs: least developed countries. LICs: low-income countries. LMICs: lower middle-income countries. UMICs: upper middle-income countries. FDI: foreign direct investment. All external flows are official development assistance (ODA) inflows, export credits, non-concessional flows (other official flows, OOF), foreign direct investments, remittances, portfolio investments and private grants.
Sources: Authors' calculations based on OECD (2020[12]), *Creditor Reporting System* (database), https://stats.oecd.org/Index.aspx?DataSetCode=CRS1 for ODA and OOF flows; and World Bank (2020[13]), *World Development Indicators* (database), https://data.worldbank.org/indicator.

Source: European Commission (2020[14]), "The EU External Investment Plan", https://ec.europa.eu/eu-external-investment-plan/about-plan_en.

Sectors such as health and education that are the most dependent on ODA in the early stages of transition also experience the sharpest and fastest decline in ODA, and major financing gaps appear in the absence of sufficient domestic resources or private investment. Planning transition means attempting to exploit this potential in the early stages with the assistance of development finance institutions. Indeed, paradoxically,

these sectors are precisely those that would benefit the most from early market creation. As mentioned above, domestic resource mobilisation has to be planned in order to anticipate budgeting needs, and the private sector can also be engaged earlier in the development continuum in order to jump in with business opportunities and allow consumers to benefit from their services (Box 3.3).

Box 3.3. Private insurance can be critical in financing specialised treatment for high-income segments of the population in low-income and lower middle-income countries

While the problem of non-communicable diseases continues to increase in all regions of the world, it disproportionally affects low- and lower middle-income countries (LICs and LMICs). As remarked in OECD (2021[15]), the global disease burden is shifting towards non-communicable diseases. However, this shift is especially burdensome for LICs and LMICs. Health systems in these countries often lack adequate funding and were not designed to manage chronic conditions, with the financial burden of healthcare costs falling on individuals, families and communities.

However, even in LICs and LMICs, private insurance business opportunities exist, and can cater to the needs of middle classes that are among the most likely affected. Although private insurance remains underdeveloped in most low-income and lower middle-income contexts, its role can be critical in financing specialised treatment for high-income segments of the population. Due to their relatively high income levels and affluent lifestyles (e.g. higher consumption of meat and dairy products and high sugar-containing food, less physical activity), these populations are often more susceptible to non-communicable diseases than the rest of the population. This would allow rational targeting for scarce tax-based and government-supported scheme resources for low-income households.

Source: OECD (2021[15]), “Financing transition in the health sector: What can DAC providers do?”, https://doi.org/10.1787/0d16fad8-en.

No trap. In alignment with partners’ development strategies, the DAC should help mobilise additional private finance and reduce dependence on ODA. As countries reach higher levels of income, private investment plays an increasing role in financing their development, and the need and demand for ODA decline. Again, transition and substitution should be better prepared to build the resilience of ODA and ensure that both the quantity and the quality of financing remain sufficient to avoid development setbacks.

In the example of Viet Nam, in a context of surging private investment, the government had frozen borrowing because of an internal debt ceiling and stricter debt level control. This created, for some DAC members, a backlog of undisbursed projects. At the same time, after graduation from IDA (International Development Association) assistance, multilateral development banks offered the government technical assistance to access financial markets. While this transition is to be expected, and could create new avenues of co-operation for the DAC, a few DAC members did not adjust in time. From an ODA resilience perspective, the question is how to ensure that this change in the type of financing does not curve Viet Nam’s growth path towards a less sustainable one (e.g. with no respect for environmental standards) and does not lead to a middle-income trap (e.g. low wages and poor labour conditions, productivity losses).

The Viet Nam pilot study underscores the issue of DAC members adapting their instruments and projects as countries transition and their needs change. While this adjustment might be difficult at the individual DAC member level, it could be done more easily at the collective DAC level (e.g. among development agencies and banks). It appears, however, that the development co-operation/investment nexus can lag behind. In Viet Nam, only a few DAC members had shifted their support to build a private sector ecosystem conducive to sustainable growth (Box 3.4).

This example shows at the same time the importance of the role of ODA in creating the conditions that private sector-led financing remains sustainable and inclusive and does not result in socio-economic

setbacks. Again, this should be part of transition management, to avoid the DAC from losing its influence before the country can embark on a virtuous sustainable growth path.

Box 3.4. The enabling environment for private sector investment in Viet Nam needs to be strengthened

Despite the dramatic increase in volumes, foreign direct investment does not seem to have acted as a broader catalyst for growth with spillover effects on the domestic private sector – in the form of increased demand for local supplies and the transfer of technology and managerial techniques. The contribution of the domestic private sector to gross domestic product and to exports is low. Indeed, with the exception of a handful of emerging domestic conglomerates such as VIN group,* the domestic private sector mainly consists of small household enterprises.

Some of the consequences are social: in light of demographic pressures and structural imbalances between the foreign direct investment sector and the domestic private sector, it is likely that there will be a continued need to address social vulnerabilities.

To realise a transition towards a more balanced financing mix, the private sector enabling environment needs to be strengthened: the Regulatory Quality Index ranks Viet Nam 121st out of 193 countries. For example, the absence of clear guidance on land ownership rights and usage, as well as a lack of clarity on procedures for land transfers, are named to be one of the key concerns of investors. An enabling environment for the private sector in Viet Nam will allow for more opportunities for local value creation.

Development partners can help to promote financial sector development and support the creation of an enabling legal and regulatory framework for an increased sustainable development footprint of private sector investments.

* https://vingroup.net/en/about.
Source: Kim, J. and K. Poensgen (2019[2]), "Transition finance country study Viet Nam: On the threshold of transition", https://doi.org/10.1787/3cb86a6c-en.

Proposing: What are the solutions?

The nexus between development co-operation and investment – or development policy and economic diplomacy – needs to be strengthened. The DAC could help to do this through additional work on substance and institutional arrangements.

On substance, the DAC has a major role to play in building an eco-system for private sector-led development supportive of sustainability and inclusiveness. This means investing in private sector development, investment climate, the business environment; creating markets and building local capacities to attract the "right" investors (i.e. renounce the race to the bottom and now-criticised tax incentives and raise local standards to join higher value-added supply chains) and improving access to credit. It also means revamping aid for trade, taking into account the new geopolitical context. Additionally, it means the DAC should work together with the private sector to increase the development footprint of trade and investment, e.g. through the work on qualities of foreign direct investment or the development dimensions of global value chains (GVCs), promoting certain standards embedded in DAC members' core values (environment, labour, intellectual property rights, etc.). Finally, it means using transition finance and other diagnostics to design country/sector/GVC strategies assessing the respective roles of private and public financing (e.g. cascade approach)[10] and optimising financing mixes accordingly. This would help move from diagnostics to implementation.

Box 3.5. Towards quality investment: Showcasing Japanese and US initiatives

In recent years, Japan has strongly promoted quality infrastructure investment through concrete global and regional commitments. These include: the development of the *APEC Guidebook on Quality of Infrastructure Development and Investment* (from 2014 and subsequently revised in 2018); the 2016 G7 agreement of the Ise Shima Principles for Promoting Quality Infrastructure Investment; the achievement of the G20 Compendium of Good Practices for Promoting Integrity and Transparency in Infrastructure Development; and in 2019, the G20 agreement on Principles for Quality Infrastructure Investment.

More recently, and based, among others, on the Japanese experience, the US has launched the idea of the "Blue Dot Network".* This network is defined as a "multi-stakeholder initiative that aims to bring together governments, the private sector, and civil society to encourage adoption of trusted standards for quality, global infrastructure development in an open and inclusive framework". Its mission is to promote high-quality, market-driven and private sector-led investment.

* Also endorsed by Australia and Japan's Bank for International Cooperation. See Hartman (2020[16]).

Concerning institutional arrangements, the DAC could benefit from scaling up its dialogue and co-operation with other committees, such as the Investment Committee. Joint meetings could be organised around the topics of Sustainable Development Goal financing and sustainability/quality of investment (e.g. the existing OECD/Roundtable on Sustainable Investment).[11] Furthermore, the DAC could better leverage existing partnerships such as the Sustainable Development Investment Partnership[12] with the World Economic Forum. This would supplement the work of the new Private Finance for Sustainable Development Community of Practice that is initially focused on joint financing instruments, and could benefit from the work and network of the Global Partnership for Effective Development Co-operation. Last but not least, the DAC could analyse and draw conclusions from institutional settings aimed at ensuring the continuity between development policy and economic diplomacy (e.g. between the Swiss Agency for Development and Cooperation and the State Secretariat for Economic Affairs in Switzerland).[13] Such an analysis could also be introduced as part of the peer reviews, since it is an essential element of ODA resilience and long-term effectiveness.

A prosperous business environment and clear trade and investment promotion are key to mitigate risks and to incentivise private sector participation and competition.

4 Addressing risks and trade-offs

The Addis Ababa Action Agenda has created a number of opportunities for financing the 2030 Agenda with new actors and instruments put forward. At the same time, this complexification of the financing for sustainable development landscape has created new risks and increasing difficulties for partner countries to navigate this landscape and design optimal financing strategies. The transition finance work points at critical stages of transition where those risks peak, with financing decisions potentially affecting the growth path of countries.

The DAC could lead efforts to adapt to this new financing for sustainable landscape to better align portfolio management strategies with development co-operation objectives, and prevent contributing, for example, to another debt crisis. It also calls for further technical assistance and capacity building in financing for sustainable development to help partner countries benefit the most and avoid the traps of the rapidly evolving financing for sustainable development landscape.

Providing financing for sustainable development technical assistance and capacity building and managing debt

Observing: What are the issues?

Debt was uniformly observed as a major transition issue. For example, in Cabo Verde, graduation from least developed country (LDC) status has resulted in a surge of the debt-to-GDP ratio to reach 130%. This was related to the issuance of Eurobonds and the government's financing of large-scale social housing programmes. Following warnings from the International Monetary Fund (IMF) and the withdrawal of Development Assistance Committee (DAC) funding, the country turned to the People's Republic of China (hereafter "China") to finance the infrastructure needed to diversify its economy and sustain growth. With low levels of debt, Solomon Islands also turned to China for the diversification of its economy and the exploration of its mining resources. In the case of Viet Nam, the country blocked a number of DAC projects to control its debt level. Zambia is again at risk, turning to non-DAC actors for the financing of its infrastructure after tapping into DAC resources to fight the AIDS pandemic.

There is a need to further explore the debt sustainability issue, ensuring that the DAC will not contribute to the next debt crisis. In particular, there is a need to better understand existing systemic risks. For example, in Zambia – a main benefactor of the Heavily Indebted Poor Countries initiative in 2009 – the current debt-to-GDP ratio at 60% is much lower and seemingly not worrisome compared to 2009. However, the service of the debt is much higher than in 2009. Debt to the private sector has shorter maturity, flexible rates and is more exposed to currency fluctuation risks. Also, while DAC members respect the principles adopted by the Paris Club, such as the absence of collateralisation of debt, it is not the case of all actors now on the financing for sustainable development market. The example of Sri Lanka and the loss of the port concession for 90 years is a troubling example (Abi-Habib, n.d.[17]).

Box 4.1. China's investment planning in Solomon Islands

The People's Republic of China (hereafter "China") is rapidly emerging as a new provider of development finance in Solomon Islands since the establishment of diplomatic ties between the two countries in September 2019. Since then, Solomon Islands has formally joined China's Belt and Road Initiative and announced a first series of China-backed projects, in particular in areas related to infrastructure development.

One of China's "early harvests" from the new diplomatic ties is the takeover of the country's main mining site, Gold Ridge mine, by the Chinese mining group Wanguo International. At the official launch of the mine in October 2019, Wanguo announced that it had contracted the state-owned enterprise China State Railway Group in a USD 825 million deal to complete the infrastructure works. According to the project terms presented during the official launch, Wanguo International will own all of the infrastructure developed as part of the project, including power and port facilities, roads, rail, and bridges.

The experience of other small island developing states shows that new financing opportunities need to be managed carefully. Several small island developing states, such as Cabo Verde and Samoa, have experienced a quick surge of their debt levels following least developed country graduation, and moved from a moderate to a high risk of debt distress in a relatively short period of time. In the case of Cabo Verde, the rapid deterioration of its debt sustainability was mainly driven by a surge in public non-concessional debt and increased contingent financial liabilities related to state-owned enterprises.

Source: Piemonte, C. and A. Fabregas (2020[5]), "Transition finance in Solomon Islands: Preparing for graduation from least developed country (LDC) status", https://doi.org/10.1787/a4739684-en.

The evidence collected points at this systemic risk and major geopolitical considerations for the DAC. The role of DAC and non-DAC actors differs as countries transition. Three major differences in financing patterns appear: 1) non-DAC actors intervene at a later transition stage than DAC members; 2) they focus less on social sectors and more on infrastructure; and 3) the frontier between public and private funding is less clear. This confirms the uniqueness of the DAC and official development assistance (ODA) as a supporter of early development and provider of access to basic services such as health and education (Box 4.2). However, it also raises questions as to the strategic breakdown of the roles among financing for sustainable development actors. For example, in Cabo Verde, China arrived after the country had reached a high level of debt and the DAC mainly financed social sectors; thus, China could invest in productive sectors (infrastructure, tourism, the blue economy) with the perspective of reaping long-term benefits and leaning from the initial incursions of the DAC.

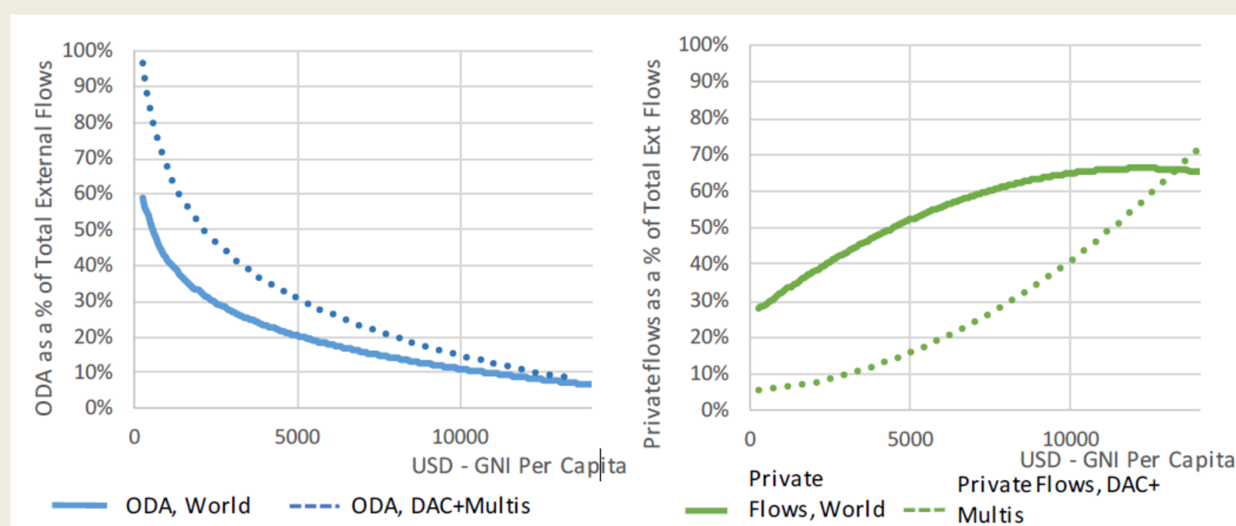
Discussions have revealed a blame game between China and the DAC. China points to the absence of accountability of DAC members' assistance (e.g. budget support) and the effectiveness of tied aid and value-for-money infrastructure, while the DAC points to transparency requirements, the quality of infrastructure and principles that exclude, for example, tied aid or debt collateralisation.

Box 4.2. The role of DAC and non-DAC actors differs as countries transition

At any point in transition, the share of official development assistance (ODA) in external finance is significantly greater when considering the Development Assistance Committee (DAC) community only. The share of ODA drops twice as fast for the DAC than for the world as a whole. Indeed, ODA is mostly a DAC instrument, and other countries provide comparatively less ODA-like support (Figure 4.1, left panel).

Figure 4.1 (right panel) shows, however, that the curves of private sector finance are reversed (one convex, one concave), meaning that the DAC is much slower at mobilising private finance than other actors. This could be explained by differences in levels of development, and the higher reluctance of investors in DAC member countries to enter less sophisticated and riskier markets. For countries with more comparable levels of development, on the contrary, the risk perception is different.

Figure 4.1. Traditional donors are in a unique position to finance underinvested sectors with official development finance; non-DAC financiers trigger faster and earlier their private flows as countries develop



Source: Piemonte, C. et al. (2019[1]), "Transition finance: Introducing a new concept", https://doi.org/10.1787/2dad64fb-en.

Proposing: What are the solutions?

The DAC could help developing countries better navigate the complex financing for sustainable development landscape that emerged from the Addis Ababa Action Agenda with a Tax Inspectors Without Borders initiative type of mechanism.[14] Its objective should be to help partner countries navigate the complex financing for sustainable development landscape and identify the partners and instruments that are best fit for purpose at different stages of transition. This would also prevent the risks associated with key transition milestones from translating into financing gaps or debt traps.

Such a mechanism would supplement existing debt management efforts carried out by, among others, the IMF and the World Bank, and rely on the following principles:

- Technical expertise: in practice, some DAC members already fly experts to partner countries to provide such assistance (e.g. the United Kingdom in Zambia), but more widely, such experts could

be co-ordinated and teamed up to represent DAC and non-DAC countries, as well as institutions such as the IMF.

- Neutrality: the mechanism should be hosted by a neutral actor/honest broker to avoid conflicts of interest (such as the OECD/UNDP for Tax Inspectors Without Borders); teams should be representative of different types of donors and relevant organisations.
- Country and demand-driven responses: the success of Tax Inspectors Without Borders partially relies on country ownership and the fact that partner countries see an interest in raising their fiscal revenue as a result of their participation in the programme. In the case of external financing, a number of governance issues could affect the demand for participation in the programme. On the other hand, it could also be a tool for governments and development partners to increase transparency and fight corruption.
- Early interventions: debt sustainability management programmes often start too late. Sometimes governments sign deals without even fully understanding their terms and conditions. Financing for sustainable development technical assistance should take place as early as possible.
- Long-term capacity building: the World Bank and the IMF are scaling up their efforts to build the capacity of partner countries to access financial markets and negotiate/manage debt. DAC members should also invest in supporting partner countries to build capacity to navigate the financing for sustainable development landscape, identifying the best partners and instruments, and avoiding risks associated with key transition milestones. Specific needs were identified for capacity building in the small island developing states and access to climate funds.
- Multi-levels of governance: a major challenge of debt sustainability is related to the multitude of actors having the ability to contract debt within each partner country (ministries, subnational and non-sovereign entities, state-owned enterprises, etc.). Beyond debt, the Development Co-operation Directorate’s work on decentralised development co-operation revealed opportunities for subnational entities to actively participate in financing and achieving the Sustainable Development Goals. Assistance could be provided to assess risks and opportunities and strike the right balance of financing.

  Guidelines: the DAC should define a number of guidelines or standards for financing for sustainable development that would be promoted through these technical assistance and capacity building efforts. These guidelines would be useful to engage in a more constructive dialogue on emerging financing for sustainable development with non-DAC actors and end the blame game that was earlier identified.

Box 4.3. COVID-19 and the debt crisis

Where do we stand?

The COVID-19 pandemic has thrust many of the world's economies into extreme indebtedness. Most countries have been forced to resort to new debt issuances to finance extraordinary health expenses as well as measures that seek to reduce the crisis' catastrophic economic and welfare consequences. In particular, many developing countries have reached unprecedented high debt-to-GDP ratios and face extremely worrying debt liquidity, and even solvency, concerns.

In order to alleviate the current debt crisis, the international community has already arranged for certain emergency relief initiatives (e.g. the Debt Service Suspension Initiative (G20-Paris Club, n.d.[18])[1], the IMF's rapid financing mechanisms[2]). However, and depending on how long the COVID-19 crisis will last and how long will it take for a return to "normality", other measures should certainly be considered in the very near future.[3] Indeed, the current global debt crisis is just at its beginnings.

Notes: 1. This initiative was initially approved until December 2020, but has been extended until June 2021. It allows eligible countries to freeze, between May 2020 and June 2021, the public and publicly guaranteed-related debt service. Moreover, because the standstill is offered on a net-present value-neutral basis (meaning that creditors will be fully repaid), multilateral creditors should be able to consider participating without significantly impacting their ratings, with support from their shareholders. 2. The Rapid Credit Facility, the Rapid Financing Instrument, the Catastrophe Containment and Relief Trust, and the augmentation of the Extended Credit Facility. 3. A recent World Bank green/blue debt swap initiative is currently under study; however, some questions remain: Is it fair to ask developing countries to "finance" global public goods when what they really need is to finance their own sustainable development and invest in poverty reduction, social services, etc.?

Sources: Based on OECD (2020[19]), "A debt standstill for the poorest countries: How much is at stake?' https://www.oecd.org/coronavirus/policy-responses/a-debt-standstill-for-the-poorest-countries-how-much-is-at-stake-462eabd8; Piemonte, C. (forthcoming[20]), "External debt in SIDS: One-year into the COVID-19 crisis, where do we stand?", forthcoming

Managing aid portfolios, trade-offs and foreign policy strategies

Observing: What are the issues?

The DAC could improve its development co-operation offer all along its partner countries' transition journey. As countries transition, their needs for financing evolve in terms of volumes as well as quality (e.g. instruments, sectors). However, there is often a division within the DAC between those members primarily offering grants and those primarily offering loans, which also overlaps with income category segmentation (see Annex A). The transition finance approach allows reconciling the views with a strategic collective distribution of the roles along the development continuum.

There is a need for advisory services to be neutral and financing strategies to be country owned, but also for DAC members to define their development co-operation strategies and prioritisation coherently as a group. Indeed, their actions are, individually, based on political objectives, impact (i.e. optimise the allocation of scarce public resources) and portfolio management considerations. However, there is also a need to reconcile collectively all of those objectives to obtain efficient results, aligned with the partner countries' priorities.

The transition finance country pilots pointed at some trade-offs encountered in individual portfolio management strategies. For example, in Chile, most DAC members had already phased-out their support before graduation – beyond technical assistance – and the only remaining sizeable projects were in renewable energy (with the German development bank; see Box 2.2). From Chile's perspective, the "soft" dimensions (i.e. technical expertise, knowledge and technology transfers) of the German projects were

more important than the "hard" ones (i.e. the financing) because Chile had access to other cheaper sources of financing. This raises questions about DAC portfolio and transition management strategies. First, why was Germany still present in Chile in the area of renewables? This is clearly in line with Germany's (and the DAC's at large) priorities and engagement in favour of environment and climate. It also makes sense from a portfolio management perspective with low-risk/high-return projects that could generate resources for high-risk/low-return projects in countries most in need. Second, from a transition finance perspective, two pieces of the puzzle are still missing: how could Germany (or the DAC) support the government of Chile to ensure investment in renewable energies is properly budgeted for and remains a priority after graduation? How can one ensure that portfolio management strategies do not overshadow development impact objectives? (In that case, how can infrastructure projects be supplemented with other social or governance projects that would tackle the issue of inequalities in Chile that are the main hurdle on the country's development path?)

The work of development agencies and development banks or development finance institutions within each DAC member (where both are available) and across DAC members could be better articulated and co-ordinated. As countries transition and their borrowing capacities increase at the same time as their infrastructure needs, development banks and development finance institutions see their potential business opportunities increase. However, rapid growth might coincide with growing social challenges (e.g. regional and social inequalities, quality of jobs). Therefore, it is not satisfactory for DAC members to capitalise on investment opportunities (phasing in of infrastructure) while phasing out social or governance/institutions' capacity building programmes. In Zambia, for instance, progress in health and rapid growth should not divert from geographical disparities and the growing poverty in rural areas or in populations at risk. In Viet Nam, the strong economic growth and opportunities for infrastructure financing should not divert from environmental and labour/productivity challenges.

Neutrality of advice for financing strategies calls for a better understanding of the comparative advantages of the different actors – including bilateral versus multilateral institutions. Co-ordinated action in specific contexts (partner countries) can deliver better results than the sum of individual interventions. From a financial point of view, the DAC could usefully plan joint actions and help define the role of multilateral actors.

Proposing: What are the solutions?

The DAC could further integrate the multidimensionality of development into its financing strategies. So far, this topic has been contentious and associated with the definition of ODA and graduation criteria. The transition finance approach offers a different perspective, focusing on the trade-offs between portfolio management and development impact, as well as aid effectiveness and prioritisation for impact.

The observation of "warning signals" could be part of the preparation for graduation. Inequalities and environmental vulnerability are examples. In addition to gross national income per capita, the DAC could track some indicators that could help respond to some of the following questions:

- What should be the DAC's priorities when a country grows fast and will graduate in the near future while it still observes strong inequalities?
- Should the focus be on governance? On mobilising domestic resources for building strong institutions, national economic and social solidarity mechanisms?
- What environmental vulnerability indicators should the DAC use in order to better allocate resources? (Small island developing states should be closely involved and their needs better targeted when considering such variables.)

In light of development's multidimensionality, co-operation providers could usefully deploy, for example, special technical assistance funds/methods and produce principles/recommendations on how to execute

this kind of assistance. Indeed, the Chilean inequality problem and the challenges surrounding Lebanese governance and solidarity could have been prevented, or at least mitigated.

Furthermore, the use of such a multidimensional vision could also send signals to the DAC on when international solidarity could pull back. The Lebanon pilot demonstrated the adverse effects of aid, or a broken humanitarian/development nexus, when massive flows to finance infrastructure and real estate projects resulted in greater inequalities (benefiting a small elite, using a low-cost refugee workforce), instead of improving governance and establishing solid safety nets (Box 4.3).

The DAC could further integrate the multidimensionality of development into its financing strategies. The observation of "warning signals" as inequalities and environmental vulnerability could be some of them.

Box 4.4. The economic trajectory of Lebanon towards upper middle-income country status left the socio-economic and political fragilities of the country unaddressed

Fragilities arise from socio-political fragmentation, political instability in the country – including civil wars and conflicts with neighbouring countries, as well as knock-on effects from conflicts in the region, such as drops in external finance and large refugee inflows. They also arise from high exposure to external financing and a narrow fiscal space for public investment.

Lebanon has struggled with widespread poverty, unequal income distribution, disparities across regions and difficulties in generating inclusive growth. According to the 2007 national survey, the most commonly used for a pre-Syria conflict poverty profile, 28.5% of the population was considered poor and 8% extremely poor in 2005. The bottom 20% of the population accounted for 7% of all consumption, while the richest 20% accounted for 43%. Around 65% of the total poor in Lebanon is estimated to live in the North and Mount Lebanon governorates. Around four in ten workers lack formal work contracts and the same share did not benefit from any type of health insurance in 2015. Pension and health service coverage among Lebanese older than 65 years of age was very low, with only two in ten people covered.

Source: Chiofalo, E., K. Poensgen and Y. Rockenfeller (2019[3]), "Transition finance country study Lebanon: Global public goods and the response to adverse shocks", https://doi.org/10.1787/22220518.

5 Moving from diagnostics to implementation

The multiplication of actors in charge of the implementation of the Addis Ababa Action Agenda creates a co-ordination challenge at all levels, from diagnostics to implementation. Financing strategies need to be integrated/holistic and dynamic. As the transition finance work shows, there is no point designing financing strategies that do not take into consideration the respective roles of different actors at different stages of transition. There is also no point doing so without taking into consideration the dynamics of transition, i.e. without planning for the evolution of the respective roles of different actors as countries transition.

Mapping priorities and opportunities

Observing: What are the issues?

Different donors, including within the Development Assistance Committee (DAC), have different priorities and use different instruments (e.g. grants versus loans), implying that they intervene at different stages of transition with a focus on different issues, groups of countries or sectors. There is no model that is better than the others, and each donor has good reasons to opt for one model rather than the others. Diversity of portfolio management strategies should also allow for more complementarity and leaving no one behind. Building on this simple observation, the question is whether the value of the DAC as a whole could be greater than the sum of its parts, i.e. whether there could be an integrated DAC financing strategy beyond the sum of individual DAC members' strategies.

In the absence of co-ordination and (collective as well as individual) management of transition, the DAC's efforts could be insufficiently resilient and fade away in the long term. Restoring the development co-operation/investment nexus, for example, also means creating a continuity of action across agencies within individual DAC members and across DAC membership, with some members focusing on social issues while others focus on private sector development. The DAC as a whole should determine:

- at any stage of transition, which of its members have a comparative advantage in specific areas and types of financing
- as partner countries transition, how to avoid financing gaps and development traps by planning the exit and entry of different DAC members or the use of different instruments all along the journey.

In other terms, could there be a better distribution of the roles among DAC members in a country taking into account the dynamics of transition? The objective would be to avoid, for example, that a set of DAC members does increasingly well at sponsoring infrastructure when at the same time inequalities persist and DAC members or agencies most interested in social aspects have already left the country.

Proposing: What are the solutions?

In order to make the value of the DAC as a whole greater than the sum of its parts at any stage of transition, and to build the resilience of official development assistance (ODA) as countries transition and new DAC

actors phase in and out, the DAC could map its members' priorities, comparative advantages, expertise and instruments. The objective of such a mapping exercise would be to better understand and potentially more strategically distribute the roles and responsibilities of individual DAC members (or entities), taking into consideration the transition factor, i.e. the fact that these roles evolve as partner countries transition.

Such a mapping could be part of transition finance country diagnostics, at country or sector level, helping DAC members better prepare and manage transition and build ODA resilience. This mapping would identify financing opportunities for DAC members. If articulated with other diagnostics, it could also help better align DAC and partner countries' financing strategies. For example, in Viet Nam, the Development Co-operation Directorate's contribution to the OECD Development Centre's *Multidimensional Country Review*[15] could result in recommendations for economic and policy reforms to the government supported by a financing plan (transition finance diagnostics), including an analysis of the optimal financing mix to support the reforms. An analysis of impact on growth and redistribution of this financing strategy could also be included.

Further reflection could be made on the alignment of multilateral/bilateral actors along the development continuum. Their interests and incentives should be better investigated, and their behaviour better handled (competition, complementarity). Indeed, as shareholders, DAC members should have a clearer distribution of the roles in mind, e.g. for crisis management and global public goods.

Moving from diagnostics to implementation will be essential. Observation suggests that co-ordination among DAC members, and with other financing actors, could be improved. Co-ordination is greater where the DAC is less in competition with other actors (e.g. budget support groups, or when the country does not have access to capital markets). Building on diagnostics, the DAC, together with other actors, could implement financing strategies with a better distribution of the roles among external/local and public/private actors. For example, using the "cascade approach": what the private sector can do alone – market-driven; what the private sector can do with support from donors – creating markets, fixing the regulatory environment, etc.

Co-ordination could be achieved through partnerships and country road maps or along value chains (e.g. Sustainable Development Investment Partnership with the World Economic Forum and the International Chamber of Commerce's Sustainable Development Goals [SDG] Action Labs,[16] respectively). It could also build on an improved private sector engagement of the DAC and the Global Partnership for Effective Development Co-operation.

Reconciling perspectives into integrated national financing frameworks and country ownership

Observing: What are the issues?

Alignment of various Addis Ababa Action Agenda actors' strategies among themselves and with partner countries' SDG financing plans is a major challenge. The profusion of diagnostics, often aimed at serving individual interests and priorities, does not help to maximise synergies and catalytic effects. Some actors do not want to release those diagnostics, as they are the basis of their "business strategy" and want to preserve the confidentiality of their investment plans. All diagnostics should rather feed into integrated national financing strategies that would allow for local governments to plan the allocation of resources and adequately budget SDG financing. Predictability is essential to successful SDG financing strategies.

Alignment of DAC and partner country strategies remains a challenge, even if country ownership is a core principle of the DAC and development co-operation. This was revealed, for instance, in the Viet Nam country diagnostic, where some DAC members had stalled projects due to a fast growth that resulted in late adjustments and a misalignment of financing supply and demand.

Country ownership is a factor of ODA resilience. In the absence of country ownership, the partner country's government is less likely to continue funding programmes using domestic resources or to call upon private finance as ODA phases out. In Chile, for example, DAC members still present at the time of ODA graduation should have ensured that the programmes they supported would be adequately budgeted or supported by other sources of financing: abandoning programmes in a context where access to finance is not a severe issue raises questions about aligning donors' and partner countries' priorities.

In the absence of integrated financing strategies, resources can be channelled through different ministries or agencies, sometimes without much transparency, resulting in difficulties to centrally plan SDG financing or even manage debt levels. This was observed, for instance, in Zambia, with an independent administrative agency in charge of infrastructure; in Chile with aid transitioning through the Ministry of Foreign Affairs; or in Viet Nam with the problematic of non-sovereign borrowing.

Proposing: What are the solutions?

As per the Addis Ababa Action Agenda, the integrated national financing frameworks could be the primary tool to address those issues. The United Nations Secretary-General's Roadmap called for support for the adoption and implementation of the integrated national financing frameworks through:

- Development of required methodologies and tools to develop high-quality and action-oriented integrated national financing frameworks (including assessment of needs, financial flows, risks and binding constraints; a financing strategy that identifies required public and private financing policy actions; monitoring and review frameworks; and governance and co-ordination mechanisms to provide political backing and ownership).
- Promotion of multi-stakeholder national dialogues involving government, social partners, development partners, international financial institutions, civil society and other stakeholders in order to develop quality and action-oriented integrated national financing frameworks.

The DAC, as a main actor of the Addis Ababa Action Agenda, could respond to this call for support and contribute to the integrated national financing frameworks. This could be done through:

- Active participation in the definition of the integrated national financing frameworks modules – the Development Co-operation Directorate contributes with other stakeholders in the consultation process led by the United Nations Department of Economic and Social Affairs.
- The inclusion of transition finance country diagnostics into the integrated national financing frameworks toolbox – the DAC perspective could supplement the development finance assessments[17] to help align various donors' and partner countries' financing strategies; transition finance country diagnostics could be undertaken in integrated national financing frameworks in pioneer countries upon partner countries' request jointly with DAC members. This could include cross-OECD expertise (aid/tax/investment) as unique value-added and be articulated with other OECD reviews, such as Multidimensional Country Reviews or Investment Policy Reviews.[18] Such an approach would facilitate DAC co-ordination and build ODA resilience into national financing frameworks.
- The DAC could further improve its co-ordination with multilateral actors and engage with the private sector (e.g. through the Sustainable Development Investment Partnership) to implement the integrated national financing frameworks. As integrated national financing frameworks increase country ownership, the DAC's contribution would ensure mutual responsibility.
- The DAC could build on the Global Partnership for Effective Development Co-operation to implement those strategies.

Annex A. DAC members' portfolios of official development finance

Each DAC member uses a particular combination of financial instruments to target the specific region/categories of countries of its choice. Such combinations result in diverse portfolio management strategies, as mapped in Table A.1.

Table A.1. Summary of DAC members' portfolios of official development finance to specific country groupings

	More than 20% of ODF is ODA loan focused (1)	More than 5% of ODF is OOF focused (2)	More than 25% of ODF targets LDCs (3)	More than 25% of ODF targets non-LDC MICs (4)	More than 25% of ODF is concentrated in SIDS (5)
Australia		Yes	Yes	Yes	Yes
Austria		Yes		Yes	
Belgium		Yes	Yes		
Canada			Yes	Yes	
Czech Republic				Yes	
Denmark					
EU institutions	Yes			Yes	
Finland		Yes	Yes		
France	Yes	Yes		Yes	
Germany	Yes	Yes		Yes	
Greece					
Hungary				Yes	
Iceland			Yes		
Ireland			Yes		
Italy					
Japan	Yes		Yes	Yes	
Korea		Yes		Yes	
Luxembourg			Yes	Yes	
Netherlands					
New Zealand			Yes	Yes	Yes
Norway					
Poland	Yes		Yes	Yes	
Portugal	Yes		Yes	Yes	Yes
Slovak Republic				Yes	
Slovenia				Yes	
Spain		Yes		Yes	Yes
Sweden		Yes			
Switzerland		Yes		Yes	
United Kingdom		Yes	Yes	Yes	
United States		Yes	Yes	Yes	
Total	6	12	13	19	4

Notes: ODF: official development flows. ODA: official development assistance. OOF: other official flows. LDC: least developed country. MIC: middle-income country. SIDS: small island developing state. How to read this table? For example, in Column (1), "yes" in the case of the EU institutions means that in the period 2012-17, more than 20% of its official assistance (ODA and OOF) was allocated in the form of concessional loans, and from column (4) it can be said that in the same period, its principal target was MIC countries that are not LDCs.

Table A.1 showcases a major diversity in individual portfolio priorities, or “niches”. Indeed, only two “groups” formed by two countries each can be highlighted as having similar behaviours. This is the case for France and Germany on the one hand (both providing more than 20% of their official development flows in the form of ODA loans and more than 5% as other official flows loans, and targeting more than one-fourth of their portfolio to middle-income [MIC] non-LDC countries); and the United Kingdom and the United States on the other hand (both allocating more than 5% of their official development flows in the form of non-concessional loans, targeting one-quarter of their assistance to non-MIC least developed countries and another quarter to other MICs). It is also worth highlighting that even if they use different financial modalities to reach their target, only four countries focused more than one-quarter of their aid portfolios on small island developing states countries (Australia, New Zealand, Portugal and Spain[19]).

The diversity of the portfolios reflects the intrinsic diversity of each of the DAC members. Indeed, each portfolio is the result of different preferences, choices and expertise, e.g. the United Kingdom will naturally focus on countries in the Commonwealth, France its African ex-colonies, and Japan countries in the Asian neighbourhood. Other DAC members will prioritise sectors or groupings of countries following comparative advantages (e.g. health for the United States, small island developing states in the case of Australia) and use specific instruments (e.g. only grants in the case of Ireland; ODA loans in the case of Japan). The composition of each of these portfolios responds therefore to a well-founded reasoning and country-specific policies. However, when considering the DAC portfolio as a whole, because of poor or non-existent co-ordination, there remains much room for improvement.

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Notes

[1] Major transition milestones facing developing countries as they move along the development continuum are described in Table 1.1 "Understanding the full spectrum of financing opportunities developing countries face when transitioning" in Piemonte et al. (2019[1]). Fact sheets on individual milestones are also available in the Transition Finance Toolkit at: www.oecd.org/dac/transition-finance-toolkit.

[2] ODA can be used to mobilise other financing flows, such as private finance, tax revenues, etc.

[3] Developed by the OECD. See: www.oecd.org/dac/transition-finance-toolkit.

[4] For example, the transition finance management of grants or loans for a DAC member with a vaccination programme could include the financing of capacity building in the partner country's health administration (to manage and administer vaccines), research and development, market creation and price pooling mechanisms (private investment and distribution channels), insurance, or budgeting, etc. Viet Nam's experience in this area shows that such targeted instruments should focus on maintaining not only the level of financing, but also the quality of outputs and outcomes (defaulting in this case, absent new R&D and with a policy of import substitution).

[5] Similar observations have been made by the Overseas Development Institute in "Moving away from aid" (ODI, 2019[22]) and the German Corporation for International Co-operation publication *Transforming International Cooperation: Thoughts and Perspectives on Moving Beyond Aid* (Kolsdorf and Müller, 2020[21]).

[6] Global public goods are collectively shared and should be collectively financed, regardless of a country's stage of development.

[7] A new World Bank initiative also explores the possibility to create a platform for debt restructuration or reduction in support of biodiversity and climate.

[8] Such a concept could also be explored in the case of LDCs, or other groupings of countries transitioning towards a major milestone. For example, in preparation of graduation from the LDC category, consultative mechanisms such as those envisaged by the United Nations General Assembly are also available: upon request, LDCs are invited to establish such a mechanism in co-operation with their developing and trading partners and with the support of the UN resident co-ordinator. This mechanism could also be integrated with other consultative processes.

[9] Note that this refers to creating markets and investment opportunities, boosting productivity and entrepreneurship, not to taxing exemptions.

[10] The World Bank introduced the cascade approach to "create markets and leverage more private financing" (World Bank, 2017[24]). The cascade approach seeks to first mobilise commercial finance and use official and public resources only when market solutions are not feasible or within reach only through upstream reforms.

[11] www.oecd.org/fr/investissement/fdi-qualities-indicators.htm.

[12] https://www.oecd.org/development/sdip.htm.

[13] Two agencies within the Swiss government engaged in overseas development, working towards shared overall objectives and goals.

[14] The Tax Inspectors Without Borders initiative is a joint UNDP/OECD initiative that aims to support developing countries in building tax audit capacity, giving the host administrations of developing countries the lead role in their country programmes. It allows, for example, developing countries to specify their needs and the scope of the technical assistance they require on specific tax audit issues. A dedicated central unit (the Tax Inspectors Without Borders Secretariat) operates as a clearing house to match the demand for auditing assistance with appropriate expertise. As of 30 April 2020, with 45 ongoing programmes, 33 completed programmes and an additional 19 upcoming ones, the initiative has helped raise more than USD 532 million in additional tax revenue and USD 1.75 billion tax assessments in developing countries **(OECD, 2020[23])**, with a return estimated at USD 60 of raised revenue for every USD spent by donors.

[15] The OECD's *Multidimensional Country Reviews* aim to design policies and strategies that promote development in a holistic sense, and not to simply promote growth. This takes into account the complementarities and interactions across policies and, in doing so, helps to identify the sequencing of policies needed to remove binding constraints to sustainable development and well-being improvements. See: https://www.oecd.org/development/mdcr.

[16] The International Chamber of Commerce's Action Labs aim to provide business leaders and policy makers with a platform to establish a co-operative approach toward the implementation of the 2030 Agenda. See: https://iccwbo.org/media-wall/news-speeches/icc-convenes-business-leaders-take-meaningful-action-sdg-action-labs.

[17] The development finance assessments are a tool for countries to finance the SDGs. They help identify opportunities to mobilise additional sources of finance and use existing financial resources more efficiently. See: https://sdgintegration.undp.org/DFA.

[18] The *OECD Investment Policy Reviews* present an overview of investment trends and policies in the countries reviewed. See: https://www.oecd.org/investment/countryreviews.htm.

[19] Note that in the case of Spain, the figures respond to an extraordinary debt relief to Cuba in the period, so strictly, it cannot be classified as a purely SIDS-focused donor.