United Nations Capital Development Fund
Outline of the input of intergovernmental bodies to the HLPF

1. Key policies and measures to ensure "accelerated action and transformative pathways" for realizing the decade of action and delivery for sustainable development

> ***a. Critical gaps in implementing the 2030 Agenda within the area of responsibility of the intergovernmental body (bearing in mind interrelations with other goals and targets)***

The United Nations Capital Development Fund (UNCDF) makes public and private finance work for the poor in the world's 47 least developed countries. With its capital mandate and instruments, UNCDF offers "last mile" finance models that unlock public and private resources, especially at the domestic level, to reduce poverty and support local economic development.

1. Average GDP growth in LDCs has remained higher than global growth, but below the 7 per cent annual rate called for by the 2030 Agenda (SDG 8.1). Research indicates that falling below the target of 7 per cent growth means that up to 35 per cent of LDC populations risk remaining in extreme poverty by 2030[1] (SDG 1).

2. LDCs continue to face low levels of per capita income, domestic savings and investments, and small tax bases; they remain heavily dependent on external finance, including official development assistance, foreign direct investment, remittances, and external debt. These resources are insufficient to meet LDC needs and, as a result, development progress has been uneven, leaving significant gaps towards the achievement of the Istanbul Programme of Action and the Sustainable Development Goals. LDCs thus face a significant SDG financing gap and are struggling to make progress on SDG targets 17.1 – 17.5.

3. A key reason for the slow progress is the lack of structural transformation and diversification of LDC economies (SDG 8) to build sustained inclusive economic growth. Investment in developing productive capacities, especially at local levels beyond capital cities — including in entrepreneurship, climate resilient infrastructure (SDG9, 13), energy (SDG7), agriculture (SDG2), science and technology and digitalization (SDG17) etc. — is insufficient, hindering attempts at transformation.

4. LDCs face challenges in mobilizing commercial and other capital for investments that can drive their economic transformation. Official Development Assistance (ODA) as a component to blended finance solutions will continue to be critical to driving finance to LDCs in the coming decade. But despite a growing focus on blended finance approaches, according to the UNCDF/OECD publication Blended Finance in the LDCs[2], between 2012–2018 only 6 per cent of private capital mobilized for all developing countries reached LDCs. This figure was highly concentrated in a small number of sectors, countries, and transactions.

5. Small and medium-sized enterprises (SMEs) face special challenges in accessing finance in LDCs. The unmet credit need for formal SMEs in the developing world is estimated at $4.5 trillion[3]. The issue is even more acute in LDCs, where the percentage of firms identifying access to finance as a major constraint is higher than in the rest of the developing world[4]. Growth SMEs with financing needs between $50,000 to $1,000,000 face particular challenges. Their needs are too large to be met by

[1] https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/WESP_2018_Mid-year_Update.pdf

[2] Blended Finance in the Least Developed Countries 2019, UNCDF

[3] Source: "MSME Finance Gap" report, 2017 published by IFC and SME finance forum. https://www.ifc.org/wps/wcm/connect/03522e90-a13d-4a02-87cd-9ee9a297b311/121264-WP-PUBLIC-MSMEReportFINAL.pdf?MOD=AJPERES&CVID=m5SwAQA

[4] *The percentage is about 35 per cent in LDCs, while it is 24 per cent in other developing countries. See https://www.enterprisesurveys.org/*

microfinance institutions and too small or too risky for local banks or Development Finance Institutions (DFIs), which seek large ticket sizes and need to meet their AAA credit ratings.

6. LDCs continue to be extremely vulnerable to climate change (SDG 13), as their economic growth is dependent on climate-sensitive sectors and they lack resilient infrastructure. As climate change accelerates, there is growing recognition that local governments must play a key role in adaptation and building resilience. Access to climate finance to fund infrastructure for climate resilience and adaptation and strengthened capacities for LDC governments in general, and sub-national governments in particular, must be scaled up significantly and at a faster rate.

7. Recent years have seen a rapid acceleration in the application of digital technology for providing financial and other services in LDCs. In Sub-Saharan Africa, 45 per cent of adults reported having a mobile money account in 2018, the highest rate of any region in the world. These advances have the potential to benefit women, youth, refugees and migrants as well as SMEs and show promise for the development of wider inclusive digital economies and financial inclusion (SDG 8.10). However, LDCs especially face difficulties in ensuring that the digital infrastructure, regulatory environment and viable business models that can drive financial inclusion and development of digital economies, as well as provide opportunities to increase domestic resource mobilization, are in place.

b**. *Priority measures to:***
i. accelerate action, and
ii. ensure transformative pathways to realize the decade of action for achieving the 2030 Agenda

Addressing the SDG financing gap in LDCs is of critical importance in order to achieve the 2030 Agenda. It is especially important to improve how finance works for the poor and those at risk of being left behind in LDCs, including individuals and households, small and medium-sized enterprise and local governments and municipalities. A number of priority measures can be proposed in this regard:

1. ***Scale up support for building inclusive digital economies:*** Wider adoption of financial technology (fintech) solutions will help further deepen financial inclusion and help build broader inclusive digital markets and economies, including in areas such as clean energy access, agriculture productivity, and transport. Useful actions to drive such development, especially in LDCs, include: i) develop a shared vision and framework for inclusive digital economies that leave no one behind and contribute to the SDGs; ii) mobilize investment capital and technical support to build inclusive digital economies; iii) create tools to measure inclusiveness of digital economies; iv) promote new financial instruments that harness the potential of digital innovations for the financing of the SDGs, including e.g. digital financing platforms, innovative digital services, MSME digitization and domestic resource mobilization.

2. ***Scale up finance solutions for climate-resilient infrastructure and economic development at local level***: Investment in small but transformational infrastructure projects at the local level - feeder roads, bridges, micro hydro, and climate adaptation – will be key to meeting the SDGs, as they create substantial development dividends for food security, women's economic empowerment, clean energy access, climate resilience, local economic development, and domestic resource mobilization.

    a. Unlocking public and private financing for subnational climate resilient infrastructure and local economic development is therefore essential. This will require effective local development policy that expands local fiscal space— including by nurturing domestic municipal bond markets and establishing sub national development banks, — promotes effective sub-national development policies, encourages PPPs, and stimulates the banking sector to invest in local productive infrastructure.

b. In addition, innovative financing instruments are needed, such as blended finance funds that invest in urban and municipal sustainable infrastructure projects, or local currency-denominated guarantee funds to guarantee debt to sub-sovereign entities for SDG-aligned projects.

c. Improved access to various sources and pools of global and regional climate finance for subnational governments and municipalities are also urgently needed. Support for capacity building alongside policy and regulatory reforms to enable sub-sovereign authorities to access such resources need to be scaled up.

3. ***Make blended finance work better for SMEs in the LDCs:*** Scalable blended finance approaches that address currency exchange risk, ticket size, and risk tolerance, among others, will be critical. These solutions are possible within the existing development finance architecture but require innovations, including, ring-fencing of LDC/last mile finance windows, aggregation of smaller investments in order to increase ticket size and diversify risk, amplification of technical assistance facilities to identify and support pipeline and credit scoring processes on the ground in LDCs, and the creation of integrated guarantee facilities in domestic finance institutions to help drive more domestic capital into local development. This could also include greater use of grants and concessional capital for early stage growth SMEs (the "missing middle") in LDCs, to enable them to demonstrate credit worthiness which will allow for greater access to blended finance and commercial capital. Stronger structural linkages between the existing development finance institutions and such "hybrid" entities as the UN Capital Development Fund can help fill such gaps.

2. Contribution of the intergovernmental body to accelerated action and transformative pathways and realizing the decade of action and delivery for achieving the 2030 Agenda within its area of responsibility (including its cooperation with ECOSOC and other intergovernmental bodies)

1. UNCDF's focus on "last mile" finance in LDCs occupies a unique niche in the United Nations system and broader development space. UNCDF is the only United Nations entity with a capital mandate and the ability to deploy loans and guarantees across sectors. Its focus on smaller and riskier last mile investments in LDCs, including for SMEs and local infrastructure, fills a critical gap currently left by the international development finance architecture.

2. Financing for sustainable development will be key to realizing the Decade of Action and in the context of UNDS reform, UNCDF with its unique capital mandate, is well positioned to offer its expertise and solutions to the wider United Nations system.

3. UNCDF's financing models work through three channels:

i) Inclusive digital economies, connecting individuals, households, and small businesses with financial eco-systems that catalyze participation in the local economy, and provide tools to climb out of poverty and manage financial lives;

ii) Local development finance that capacitates localities through fiscal decentralization, innovative municipal finance, and structured project finance to drive local economic expansion and sustainable development; and

iii) Investment finance, that provides catalytic financial structuring, de-risking, and capital deployment, both on and off UNCDF's balance sheet, to drive SDG impact and domestic resource mobilization.

4. By strengthening how finance works for poor people at the household, small enterprise, and local infrastructure levels, UNCDF contributes to Sustainable Development Goal-SDG 1 on eradicating poverty and SDG 17. By identifying and supporting "real economy" sectors where innovative financing models can have transformational impact in helping to reach the last mile and address exclusion and inequalities of access, UNCDF also contributes to a broad diversity of SDGs (SDG 6, 7, 8, 9, 10, 11, 13).

5. The preparatory process for the Fifth United Nations Conference on the LDCs (UNLDC-V) in 2021 also provides a unique opportunity to renew the global partnership for LDCs and highlight the need for new approaches to finance sustainable development in the LDCs. UNCDF is engaging closely to support the preparatory process for UNLDC-V and will continue to support LDCs under the new agenda, including for smooth transition of graduating countries.

6. Based on this, UNCDF will continue to scale up SDG financing solutions that work for LDCs, with a focus on the following areas:

Digital transformation in inclusive finance and the wider economy

7. The digital transformation is reshaping the financial landscape and the wider economy in the Global South. UNCDF has supported digitalization in inclusive finance across Africa, Asia and the Pacific for over a decade. In 2019 alone, UNCDF reached 2.3 million people, most of them previously unbanked and underbanked, to access and use digital financial services in the last mile. To advance inclusive digital finance and digital economies, UNCDF launched a 2019 strategy on "leaving no one behind in the digital era".

8. UNCDF increasingly leverages financial technology ('fintech') innovations to target previously hard-to-reach populations with tailored digital financial services and to provide poor households with access to off-grid energy solutions and health services, strengthen sustainable value chains and empower women and young people.

9. To create a positive enabling environment, UNCDF has supported financial regulators in over 30 countries to incentivize inclusive innovations in digital financing. UNCDF recognizes the digital divide for the poor, women and migrants, and is devising tailored services and products to address inequalities and exclusions. It is also creating a tool to help countries measure inclusiveness of digital economies. UNCDF also supports other UN agencies to apply digital financial innovation in their service delivery and project implementation.

10. UNCDF hosts the secretariat for the Better Than Cash Alliance, which is a global advocacy effort focused on accelerating the transition from cash to digital payments. The Alliance has a membership of 30 national governments, 34 international organizations and eight businesses. UNCDF also hosts the secretariat of the UN Secretary-General's Task Force on Digital Financing for the SDGs, chaired by the UNDP Administrator and former CEO of ABSA Bank. UNCDF is developing an integrated implementation platform with UNDP to take relevant recommendations of the Task Force forward.

Sub-national finance for Agenda 2030 and the Paris Agreement

11. Achieving sustainable development requires local action; however, subnational governments in LDCs face challenges in mobilizing resources and building capacity to accelerate progress towards the Global Goals. In local development finance, UNCDF provides support for fiscal decentralization and other decentralized finance models for inclusive local economic development and climate resilient infrastructure.

12. UNCDF supports local governments in LDCs and low-income countries to enhance their planning, mobilization, allocation, and transparency in financing local sustainable development. It demonstrates the effectiveness of the localized financing system through specific investments supporting local needs in climate adaptation, food security, women's empowerment, and local economic development. In 2019, UNCDF supported 443 local governments in 22 LDCs and low-income countries in these areas.

13. UNCDF's decentralized climate financing mechanism was recognized by the United Nations Framework Convention on Climate Change (UNFCCC) in 2019 as a standard for local government implementation of the Paris Agreement. UNCDF is also a pioneer in supporting local government-focused entities to become accredited to receive international climate financing from the Green Climate Fund (GCF), helping such national entities in Cambodia and Benin to become accredited to the GCF in 2019.

14. In 2020, UNCDF will launch a third-party managed fund for municipal infrastructure (the International Municipal Investment Fund) in partnership with a global asset manager specializing in long-term public infrastructure projects. The targeted capitalization for this Fund is US$350m. UNCDF will help prepare a pipeline of viable projects for this fund and continue to provide policy advice and capacity support to municipalities.

Blended finance for SME development in LDCs

15. In 2017, UNCDF established its **LDC Investment Platform** to scale up efforts to mobilize investments in local economies through the use of catalytic loans and guarantees that mitigate risks for public and private investors. Through this Platform, UNCDF provides capital to the "missing middle" segment of SMEs, i.e. early and growth stage enterprises that are too big for microfinance and too small for banks and development finance institutions. In doing so, UNCDF adopts a blended finance approach, using concessional finance to catalyse commercial investments. Over the past two years, UNCDF has made 15 concessional loans and guarantees to enterprises in the energy, agriculture and financial sectors, enabling many of them to access additional commercial finance. UNCDF is one of very few development institutions that provide financing for this important segment of growth enterprises. To expand this type of early stage financing for enterprises and small revenue generating infrastructure projects, the agency has established the **UNCDF managed LDC Investment Fund** (on- balance sheet fund) to be capitalized in the amount of US$ 50m, as outlined in its Strategic Framework 2018-2021.

16. UNCDF is also enhancing its capacity to develop a pipeline of investable enterprises, especially in Africa, and facilitate access for them to commercial investments, including through the recently announced BUILD Fund, a third-party managed blended finance fund to scale up investments in LDC-based SMEs.

17. UNCDF plays a key role in raising global awareness about blended finance in LDCs. Together with the Organisation for Economic Co-operation and Development (OECD) and other partners, it issued highly lauded reports on this topic in 2018 and 2019[5]. The reports showed that where blended finance approaches are appropriate, there is a need for more innovation and experimentation to make them work for the missing middle and local economies in LDCs. A third report on this topic is planned for 2020.

Women's Economic Empowerment

18. UNCDF integrates women's economic empowerment across all its work. It works to remove the structural barriers to women's economic empowerment by tailoring financial services and training to

[5] Blended finance in the least developed countries, 2018; Blended finance in the least developed countries, 2019

women and investing in gender-responsive local infrastructure. Over 52.7 per cent of UNCDF programme expenditures in 2019 provided a significant or a principled contribution to women's empowerment.

Partnerships

19. As a small organization, UNCDF seeks to enhance its impact through partnerships. In the context of UN reform, this means deepening collaboration with UNDP and other UN agencies where UNCDF's unique capital mandate can be leveraged to accelerate progress towards the Global Goals. UNCDF also continues to work with impact investors and financial institutions, including through initiatives such as the UN-led Global Investors for Sustainable Development (GISD), to create innovative ways to attract public and private finance to LDC markets.

3. Selected recommendations for accelerating progress and moving on transformative pathways for realizing the decade of action, for possible use in drafting the HLPF declaration.

1. Put ODA and public finance to more strategic use as an instrument of leverage for all sources of finance—public and private, domestic and international – to catalyze a higher quantity and quality of finance towards the implementation of the SDGs in LDCs, especially at the local level.

2. Employ blended finance instruments to provide capital to smaller and riskier projects and contexts that face challenges in accessing financing, especially in LDCs. This includes instruments that address currency exchange risk, ticket size, market failure, and risk tolerance.

3. Provide seed capital to de-risk local SDG positive SMEs and revenue generating infrastructure projects, and support the development of a pipeline of bankable projects. This demonstrates to private and public sector investors how financing local businesses, infrastructure and essential services can generate both financial and social returns and helps crowd-in additional resources that exist in the economy – such as pension funds and local capital - to invest in local productive sectors.

4. Help public and private capital investments reach all geographic areas - including secondary cities, growing peri-urban areas and rural regions - and contribute to inclusive growth that retain value within local economies, avoiding patterns of high growth and low poverty reduction. This especially includes a focus on increasing capacity and fiscal space of subnational authorities.

5. Enhance support for building inclusive digital economies especially in LDCs. This includes putting in place policies, regulations, infrastructure and associated capacities, as well as encouraging and supporting banks, cooperatives, microfinance institutions, money transfer companies, mobile network operators and others to extend the reach of digital financial services to unbanked and underbanked individuals and enterprises at a reasonable cost, and on a sustainable basis.

6. Promote women's economic empowerment by tailoring financial services and training to women and their businesses and by investing in gender-responsive local infrastructure. Improved access to savings and insurance for women leads to broader positive economic outcomes for their households and communities and improved infrastructure and access to credit for women businesses help increase productivity, profits and greater investment in their businesses.