IFFEd NOTE:
DEBT SUSTAINABILITY

The International Finance Facility for Education

the Education Commission

The International Finance Facility for Education

Improving education finance to achieve SDG 4

Today there are 260 million children not going to school. On current trends, by 2030, 400 million will leave education early and more than 800 million young people – half the world's children – will not be on track to have even the most basic skills needed for the workforce. This is truly a global tragedy as education is essential to development: human capital represents 70 percent of all wealth in high-income countries and no country can ever develop its full potential without investments in education.

To achieve the Sustainable Development Goal for education (SDG 4), countries and the international community will need to mobilize nearly three times the amount of current resources for education by 2030. The massive financing gap for education is holding back growth, stunting poverty reduction, and undermining many of the other development objectives from health and climate to gender equality and peace.

The International Commission on Financing Global Education Opportunity has put forward a bold plan to mobilize the needed resources for education in low- and middle-income countries to achieve SDG 4.

1. **The scale of the education financing challenge cannot be met by ordinary measures.**

The overall external financing needed to achieve the Sustainable Development Goals is estimated at $30 trillion over 12 years.

For education, a scaling up from $1.2 trillion to nearly $3 trillion annually by 2030 – through a combination of domestic and international resources – will be needed to ensure education is fully financed. Even with countries' optimal efforts to improve their tax base, increase spending on education, and improve value for money, an external funding gap for education will persist, rising to almost $40 billion by 2020 and $90 billion by 2030.

As recognized when the Sustainable Development Goals were formulated in 2015 and in the Addis Ababa "billions to trillions" strategy was adopted, developing countries cannot solve the education financing challenge on their own. The international community has an important role to play, which will require both increased commitments and new ways of leveraging additional finance.

2. **The Commission has proposed extensive domestic resource mobilization, including action to bring an end to tax avoidance. But even with maximum efforts on this front, international support for SDG 4, as recognized by the United Nations, is vital.**

Domestic resource mobilization is the main vehicle by which we will bridge the education funding gap, but it cannot achieve everything. The Commission called on countries to increase their own investment in education through increased public spending, giving greater priority to education and tackling tax evasion.

The Commission specifically called for low- and middle-income countries to increase domestic public expenditures on education from an estimated $1 trillion in 2015 to $2.7 trillion by 2030, or from 4 to 5.8 percent of GDP. It also recommended that countries "leverage the dividend from growth by increasing spending on education, through reallocating spending, raising more revenues, or both," highlighting that "there are significant amounts of potential tax revenues that could be collected from reducing current tax avoidance and evasion." And where taxes can be raised, the Commission recommended it be done in an equitable and sustainable manner.

The Commission's Chair has launched an initiative to stop tax havens following the release of the Panama Papers and other revelations about wrongdoing. The petition, directed at G20 leaders, has already been signed by over 1.1 million people. It highlights that "trillions are still being siphoned off to dodge tax in the most shadowy places in the global economy" and that "it's one of today's greatest injustices, allowing the richest to stand aside while the rest of us pay for health, education, and protecting the most vulnerable." It calls for the G20 to take action on an international agreement that outlaws tax havens and imposes penalties and prison sentences on tax evaders.

The Commission has also sent high-level delegations to meet with leaders in over 20 countries, calling for greater domestic resource mobilization and more effective domestic spending on education.

3. **The agreed Addis Ababa "billions to trillions" strategy acknowledges that traditional aid, even when increased substantially, cannot do enough to bridge the financing gap and makes a call for innovative financing solutions.**

International aid will need to increase from today's $12 billion to nearly $90 billion by 2030 to achieve SDG 4. Therefore, it is not possible to achieve the scale of financing needed through ordinary means.

To reach this level of finance, donors must increase their overall aid portfolio to reach 0.7% and in doing so, ensure 15% is directed to education. The plan also calls for a larger share of financing to be directed to multilateral organizations, such as the Global Partnership for Education, the Education Cannot Wait fund, the MDBs, UNICEF, and other UN organizations such as UNRWA which provides education for 500,000 Palestinian children.

Generosity of donors will be essential to close this gap, but even with the most optimistic assumptions to expand grant aid, the financing gap cannot be filled with traditional aid alone. Therefore, additional innovations are needed if we aspire to achieve SDG 4.

4. **Within the "billions to trillions" strategy, the Commission has examined every option exhaustively. The Commission concluded one way to deliver substantial extra resources to education is by mobilizing finance through a judicious mix of grant aid and responsible lending.**

The International Finance Facility for Education is an example of the "billions to trillions" strategy which resulted from the Addis Ababa Action Agenda of the Third International Conference on Financing for Development. It is at the heart of the United Nations approach to securing the funding needed for the broader Sustainable Development Goals agenda.

The Addis Agenda concluded that domestic resource mobilization would need to be complemented by using aid budgets to make money go further and bring in additional sources of finance. While the total $160 billion in aid cannot possibly bridge the development funding gap, it is possible to do more by making the available aid money as productive as possible and encouraging new finance.

The International Finance Facility for Education aims to ensure additional grants are mobilized alongside an increasing availability of affordable finance adhering to responsible lending and borrowing practices. The Facility will make funding available for eligible lower-middle-income (LMIC) countries by working with donor countries to provide $2 billion in financial guarantees which will underwrite newly leveraged financing. It will also request $2 billion in grants to provide additional funds to countries which would act as interest subsidies. Together, this could mobilize approximately $10 billion in new finance.

Without the Facility, it will be impossible to mobilize new and additional resources at the scale necessary and within the timeline put forward for the 2030 education goals.

For the education sector, the International Finance Facility for Education is the breakthrough solution in innovative finance, following on similar approaches already applied in health, climate, anti-poverty programs, and infrastructure. Ignoring its potential for education would be a disservice to the sector and the millions of girls and boys who deserve the right to a quality education. The Commission deemed there is no feasible alternative to address the external financing gap in education, in particular for LMICs. Put simply, education cannot be the sector left behind in the new wave of innovative global development finance.

5. **Low-income countries are better able to secure grant funding in the international education architecture, and the International Finance Facility for Education fixes a structural issue for lower-middle-income countries.**

Low-income countries can secure grant financing through enhanced International Development Association (IDA) resources – which has risen from $50 billion to $75 billion over three years – and the Global Partnership for Education. There may be additional needs for grants to buy down IDA to convert the available funding to even more concessional levels.

<u>But lower-middle-income countries face a structural problem.</u> After thorough analysis, the Commission found that lower-middle-income countries have the largest external finance gap. Lower-middle-income countries are home to the vast majority of out-of-school children and are experiencing growth but no longer have access to affordable finance in the international financial architecture for education.

There is limited concessional financing for education available for these countries and as they transition to middle-income status, they are forced to borrow at rates of 4% (IBRD/non-concessional) or resort to commercial lending (at rates of approximately 6% or more) if they would like to bridge the gap between domestic resources and aid to provide education for their citizens.

Increased and more affordable support for lower-middle-income countries is essential if we are to bridge the financing gap.

6. **The International Finance Facility for Education adheres to best practices and agreed principles of responsible lending. The beneficiaries will have lower debt levels than America and Europe.**

   Currently, with few exceptions, these countries are in a position to use a sustainable mix of grants and responsible lending – aligned with UNCTAD principles – which prevent excessive debt or excessive interest payments. This makes it possible for substantial increases in education investment.

At the heart of the Facility is improving the terms at which lower-middle-income countries can finance education so they are more affordable, fair, and help governments better prioritize education. With support from the Facility, the multilateral development banks could significantly scale up their engagement in education. At present, a small fraction of non-concessional financing is allocated to education – and only 1% of all non-concessional finance is directed to education in the whole of Africa and Asia.

The Facility will use guarantees to multiply donor resources and create a new and additional pool of subsidized finance available at reasonable rates. The Facility will offer carefully considered and responsible financing, which will have a grant element of at least 50% (much higher than the required 25% to be classified as ODA).

The mobilization of finance for the Facility reflects the spirit of the *"billions to trillions"* strategy resulting from the Addis Ababa Action Agenda. The Addis Ababa agenda also noted the UNCTAD principles on responsible lending and borrowing, the requirements of IMF debt limits policy and/or the World Bank's non-concessional borrowing policy, and the OECD Development Assistance Committee statistical systems safeguards to enhance the debt sustainability of recipient countries.

Currently, the median public and publicly guaranteed debt in lower-middle-income countries is 25% of GDP (2016), down from 51% in 2000. The Facility also aims to counter an over-reliance on commercial debt through its grant component, which is introduced alongside responsible and affordable lending.

A recent analysis by the Center for Global Development (CGD) of the eight low- or lower-middle-income African countries with the highest debt-to-GDP ratios today illustrates the "commercialization" of debt, due to rising finance from private banks and bondholders. CGD and others argue that that an increase in lending by multilateral institutions could satisfy demand for borrowing by countries and stave off a new period of debt distress as countries turn to more expensive commercial loans. Concessional funding for low-income countries from the (largely OECD) members of the DAC fell by

20 percent between 2013–16, precisely the period in which liabilities to commercial lenders increased dramatically.

Acknowledging this context, the realities of particular countries, and global norms, the Facility will adhere to best practice and will work with MDBs to put processes in place to assess debt sustainability risks based on comprehensive, objective, and reliable data prior to any financing. This would be a core requirement for participation.

Countries in debt distress or at high risk would not be eligible. Of the 27 LMICs assessed by the IMF for their debt sustainability, nine are at a high risk of distress. When the debt-to-GDP ratios of the entire group of approximately 50 lower-middle-income countries with available data are reviewed, only two have debt levels above 80 percent, near current levels of the US or high-income countries in Europe.

Table: The Facility's Impact on Debt Sustainability

	2020	**2025**	**2030**
Delta Outstanding (% GDP)	Negligible	0.3	1.9
Source: Commission Estimates			

It is important to note that all financing would be made available based on the Paris Declaration on Aid Effectiveness, the 2008 Accra Agenda for Action, and align with human rights standards as a matter of principle. The Commission has also reviewed the UNCTAD principles and see no contradictions to what we hope to achieve for education finance through the Facility. Moreover, by using the existing MDBs we can safeguard against events and dramatic circumstances (e.g. natural disaster, a shock, etc.). Working through other entities would make it much more difficult to make any changes in the terms if deemed necessary.

Education merits increased investment

Education is an investment and should be financed by responsible, long-term financing. Evidence is now overwhelming that investments in human capital can be equally, and in many cases more, productive than physical capital, and the central source of long-term sustainable poverty reduction. This is being recognized increasingly by finance and planning ministries around the world.

As one example of this emerging recognition, the World Bank's most recent *Global Economic Prospects* paper (January 2018) concluded that while the global outlook had deteriorated by 0.5 percentage points, 0.2 percentage points could be offset with stronger investments in education and health. Investing in education – and preserving spending on the social sectors during times of crisis – is absolutely essential and warrants responsible financing.

Education is an investment in the future – an investment with intertemporal benefits. It will generate economic growth and tax revenue which could help repay the concessional finance taken up for education today which represent only a fraction of the total cost in LMICs.

By solely relying on current tax revenue, which is in and of itself insufficient, today's working population in developing countries, who are much poorer than the next generation will be, would be asked to pay for the massive expansion of education called for in the SDGs. This expansion will only generate benefits once this generation reaches working age. Education, perhaps more so than most social services, generates benefits into the future which warrants a delayed payment scheme.

Ensuring impact of investment and the right to education

In the effort to expand educational opportunity at significant scale, it is essential to pay close attention to the quality of sector planning and the programs that are implemented using domestic and international finance. To ensure a sustainable and lasting impact, the education sector must ensure that investments generate results and are measured in terms of learning, not just access. Efforts for international finance are not mutually exclusive from domestic financing. Countries must be encouraged to improve their tax revenue and prioritization of education to enable continued investment in education into the future. International financing through aid and concessional lending should go hand-in-hand with fiscal reforms – including tax reform, the introduction of stabilization funds, ending tax havens, and lengthening the maturity of public debt.

The International Finance Facility for Education is an innovation which holds itself to the highest levels of sustainable financing, ensures that terms and conditions of the finance are as reasonable and favorable as possible, includes the proper safeguards, and helps countries achieve long-term growth and prosperity.

7. **The United Nations system, the World Bank, and the regional development banks support this initiative. We need civil society organizations to help us secure donors and guarantors for the new Facility.**

As the Commission points out, SDG 4 will be possible only through increased domestic finance, increased aid, and innovative financing through the MDBs. All are essential and by leaving one aspect out of the equation, we risk locking countries into much higher-cost debt or consigning them to not educating their children.

The UN Secretary-General, Deputy Secretary-General, and the UN family of agencies have fully backed the creation of the International Finance Facility for Education. A petition signed by more than 1.5 million young people was delivered to the UN on May 11th calling for the creation of the Facility and in turn, the World Bank, Inter-American Development Bank, African Development Bank, Asian Development Bank, and European Bank for Reconstruction and Development issued statements in support of its establishment.

We now need the support of civil society organizations to help persuade donors to provide financial guarantees and funding to the Facility as part of their increasing contribution to global education so we can ensure adequate financing for countries willing to make education and SDG 4 a priority.

#MakeImpossiblePossible

the
Education
Commission

The International
Commission
on Financing Global
Education Opportunity

@educommission
info@educationcommission.org
educationcommission.org