



INFF

Integrated National  
Financing Frameworks

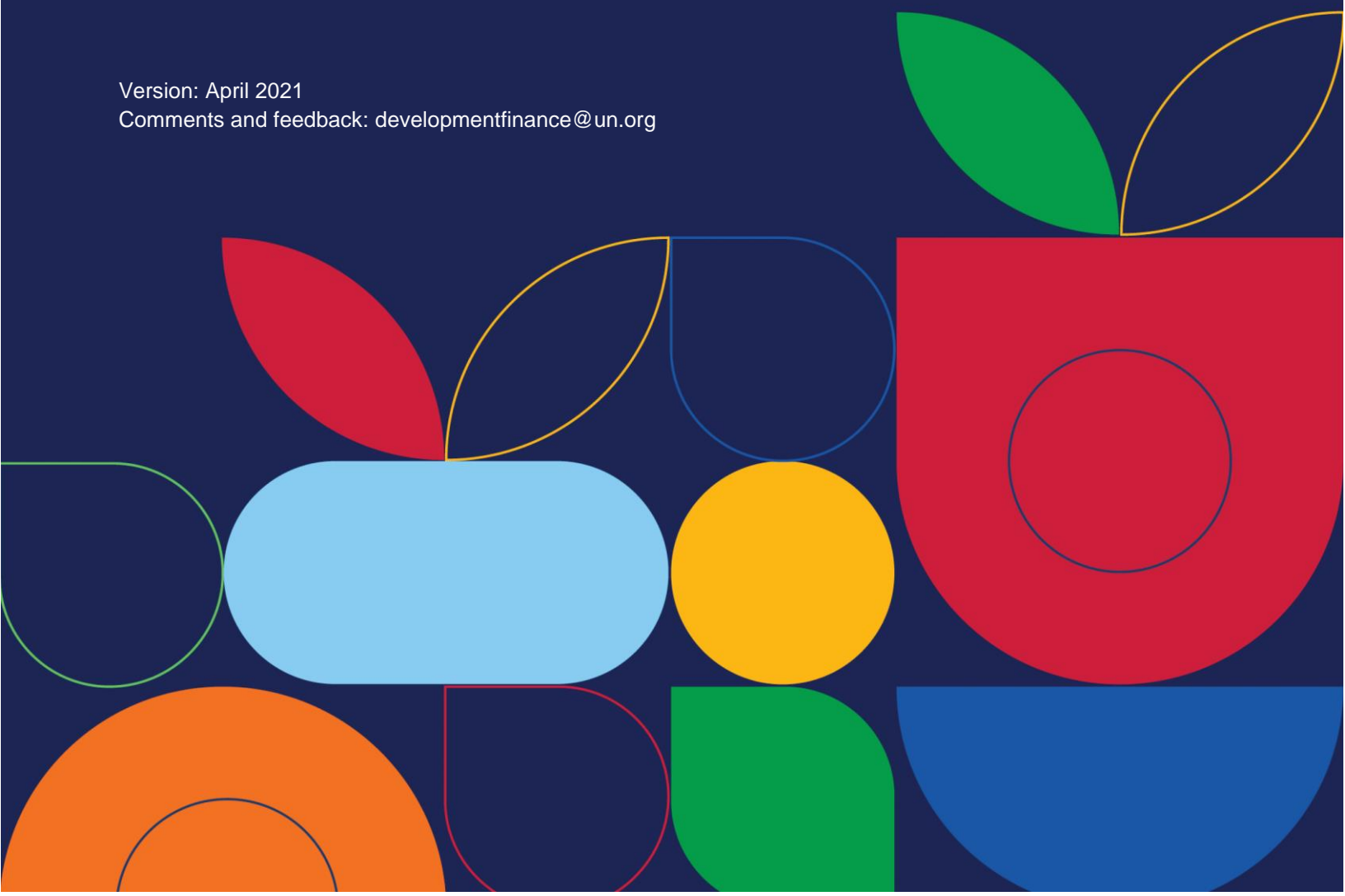


## BUILDING BLOCK 2

# Financing strategy

Version: April 2021

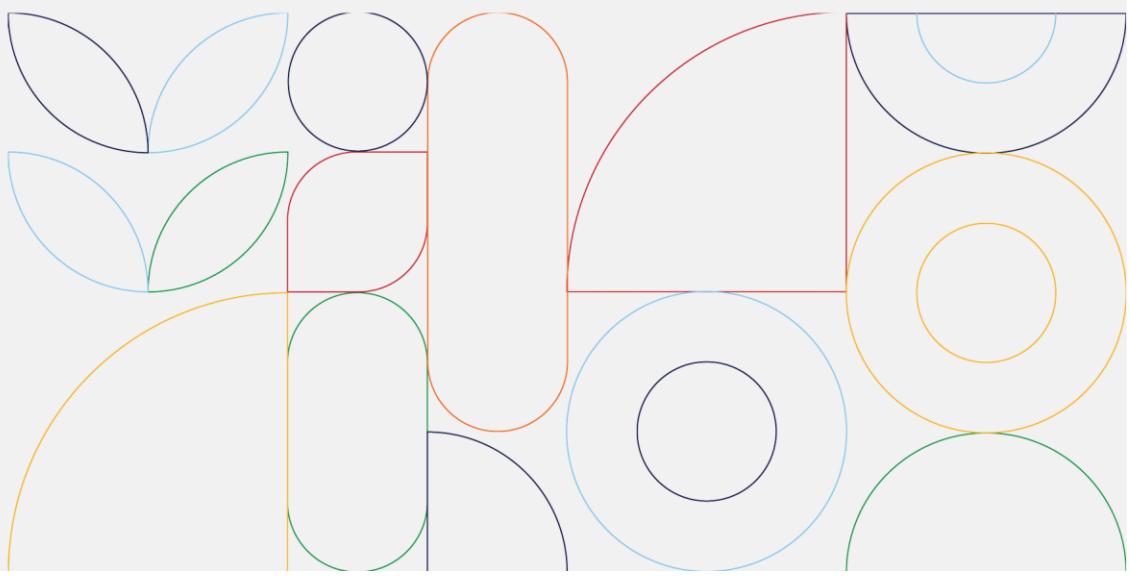
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# 1. Brief overview

A financing strategy is at the core of an integrated national financing framework. It provides a path for financing national development strategies and plans, building on findings from Building Block 1 “[Assessment and Diagnostics](#)”, as laid out in the [INFF Roadmap](#). It brings together existing policies and institutional structures in support of financing national development strategies and plans. In the current context, financing strategies can also be used to support COVID-19 recovery plans.

In most countries, a wide range of national financing policies are already in place. However, these policies are often fragmented in that they are sectoral or thematic, and were developed over time autonomously from each other. They may also not fully align with a country’s sustainable development strategy. An integrated financing strategy seeks to bring these policies and instruments together, promoting coherence both with sustainable development objectives and between different financing policy areas (public and private financing and macro-systemic issues). The financing strategy can support the prioritization of financing policy actions that best respond to national goals, needs, and constraints.

This document puts forward operational guidance to design an integrated financing strategy, drawing on countries’ experiences from different country contexts. It also provides an overview of a range of tools offered by the international community to support national efforts, while ensuring government leadership.

National and local government officials are the primary audience for this material, but it can also be

useful for international development partners and other stakeholders supporting governments in their efforts.

## 2. Value of a financing strategy

Integrated financing strategies can help countries:

- i. Raise financing for sustainable development, and better align existing financing policies with, medium- and long-term national sustainable development priorities;
- ii. Prioritise policies to take advantage of opportunities in the near-term, and identify financing policy areas for the medium- and long-term;
- iii. Ensure that financing policies, instruments, and regulatory frameworks from across different areas are coherent, sustainable, and risk-informed;
- iv. Identify opportunities to access technical assistance and capacity building support from development partners, as well as highlighting areas for peer-to-peer exchanges and learning.

seeks to avoid fragmented decision-making, better align efforts, and identify gaps and opportunities for resource mobilisation.

By centralizing the otherwise sectoral debate around financing approaches into one overarching policy framework and setting incentives for greater collaboration, integrated strategies can promote coherence. The process of formulating a financing strategy also provides opportunities for enhanced coordination and engagement across ministries and agencies; and can be an anchor for non-state stakeholders, especially development partners, to coordinate and align their support.

The financing strategy aims to foster creative approaches to mobilize finance, and combine financing policies to increase their impact. The novelty of this approach lies in its integrated nature. Its aim is not to replace the many existing methodologies and tools that countries may already make use of, such as medium-term expenditure frameworks, public investment management, revenue strategies, or financial sector development strategies. Rather, it provides a framework to align specific tools with the broader financing strategy,

## 3. Scope and limitations

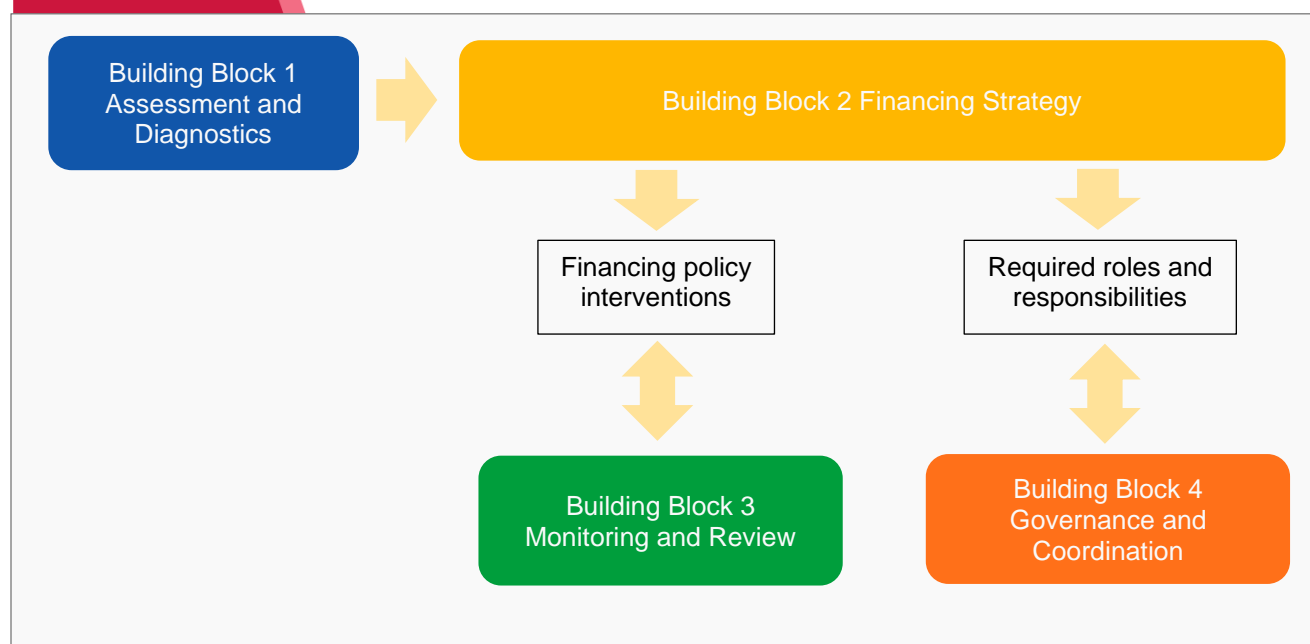
### 3.1 The role of the financing strategy within an INFF

The financing strategy is at the core of the INFF. It is informed by findings from the initial scoping undertaken as part of the inception phase, and by additional insight from in-depth assessments and diagnostics undertaken under [Building Block 1](#). In turn, it articulates the policy interventions and reforms that will require monitoring and review ([Building Block 3](#)), and whose implementation and success will rely, to a large extent, on the institutions and processes underpinning them ([Building Block 4](#)).

As further discussed in Section 4.4, specific roles and responsibilities are identified as part of a financing strategy action plan. These are informed by existing institutional arrangements, but can also highlight areas where governance may need to be strengthened or additional governance structures or mechanisms may be needed. As the financing strategy is implemented, ongoing monitoring and review should feed lessons back into policy design, and support course adjustments as needed.

FIGURE 1.

#### HOW BUILDING BLOCK 2 LINKS TO OTHER INFF BUILDING BLOCKS



## 3.2 Scope

INFFs help countries operationalize the Addis Ababa Action Agenda (AAAA) at the national level, supported by global actions. The scope of the financing strategy spans the Addis Ababa Action Areas. They bring together public finance, private finance, and macroeconomic/systemic conditions (Figure 2), and cover policies, relevant legal and regulatory measures, instruments, and processes (including capacity development).

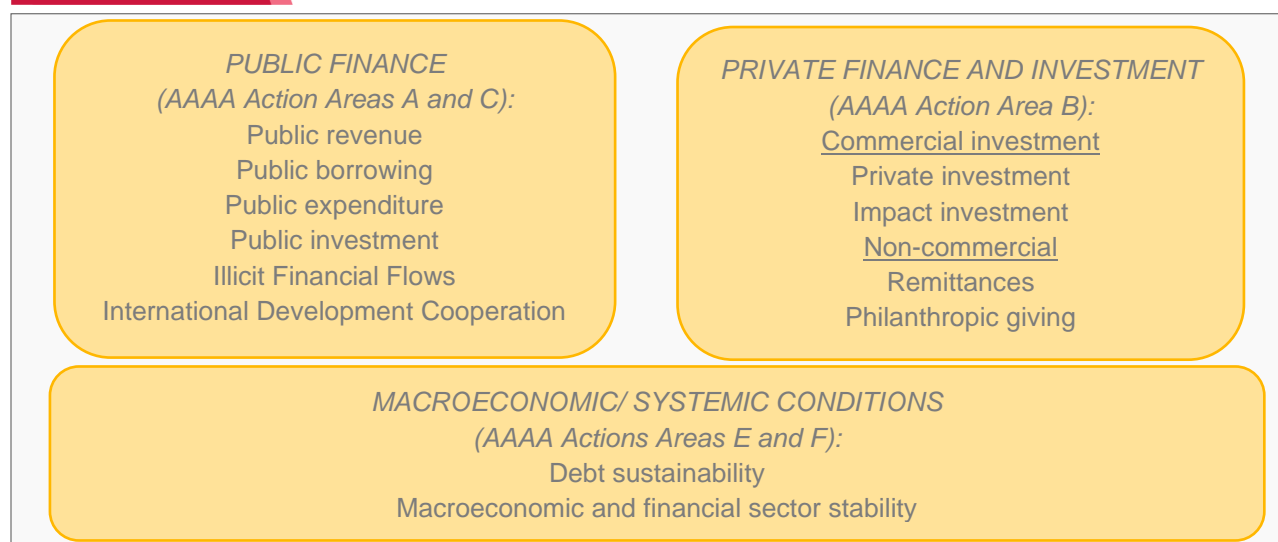
Different countries will use the financing strategy in different ways. Depending on country circumstances and needs, and the outcome of the assessments and diagnostics undertaken as part of Building Block 1, the financing strategy may focus on specific sectors (e.g., infrastructure, health, energy, etc.) or emphasize specific financing policy areas, such as national planning and budgeting processes, policy and regulatory frameworks for private finance, or macro-prudential management.

Alternatively, the financing strategy may address the full range of financing sources and their potential contributions to the implementation of the country's national development plan. Strategies could also include non-financial means of implementation, such as capacity development. Whatever the scope, the approach should be guided by the overarching aim to enhance integration and coherence, considering potential synergies and trade-offs or unintended repercussions across sectors and policy areas (public, private, macroeconomic). (Box 1 illustrates an example of integrated policymaking in the area of macroeconomic policy).

Possible entry points for a financing strategy include overarching policy cycles, such as national planning, as well as sector specific processes, such as the development of sectoral plans. Efforts related to specific financing areas can also provide opportunities for considering a more integrated and strategic approach – including by bringing in and consulting a broad range of stakeholders from the outset (see [Building Block 4 Governance and Coordination](#)).

FIGURE 2.

### EXAMPLES OF FINANCING POLICY AREAS IN THE CONTEXT OF INFFs<sup>1</sup>



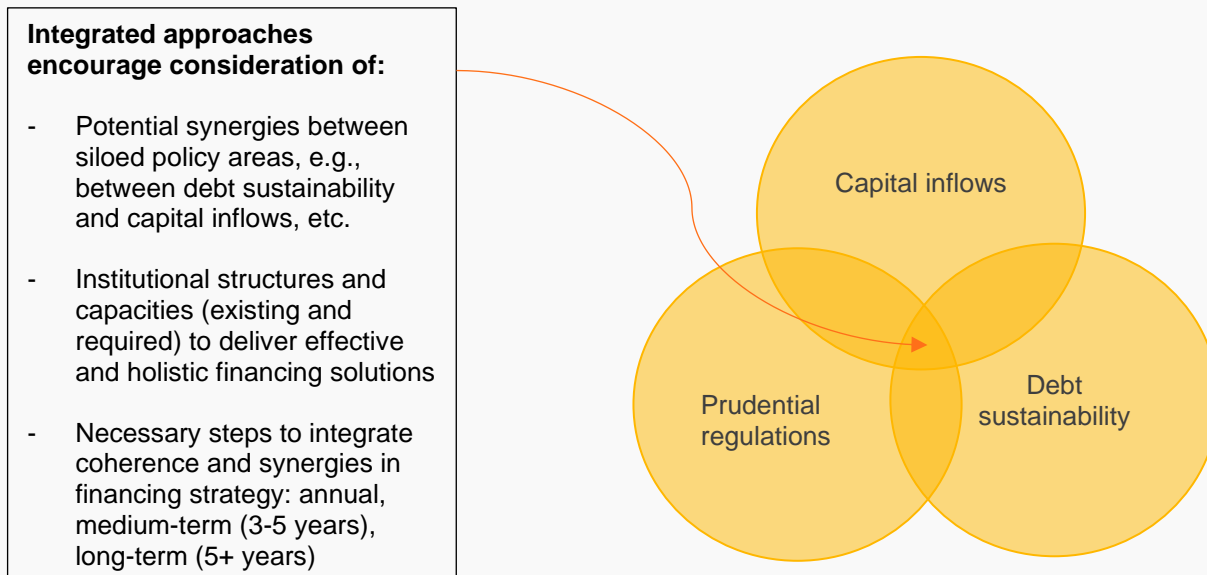
<sup>1</sup> Impact investing definition in AAAA: impact investing “combines a return on investment with non-financial impacts” (paragraph 37).

**BOX 1.****INTEGRATED MACROECONOMIC POLICYMAKING**

Integrated financing strategies can provide a framework for analysing potential synergies and trade-offs between policy objectives of debt sustainability, capital inflows, and macro-prudential regulations (see Figure 3 below).

Cross-border capital flows can provide significant benefits, such as improving access to funding; however, capital flows—particularly when large and volatile—may also threaten financial stability, especially in small, open economies. Risks are greater in the presence of underlying macroeconomic or financial vulnerabilities, but the risks exist in all countries. For example, non-economic factors, such as disasters or the spread of COVID-19, can lead to capital flight from affected countries or a broader flight to safety.

**Figure 3. Example of trade-offs and integrated approach**



Many countries have adopted flexible exchange rate regimes that broadly follow the “textbook” prescription to allow exchange rates to adjust freely in response to capital flow swings. This frees monetary policy to focus on domestic cyclical conditions in the spirit of a “one target – one instrument” approach. However, large swings in the exchange rate can be disruptive to the real economy as they change domestic prices of exports and imports relative to non-traded goods and services. They can also raise the cost of external debt servicing relative to domestic revenues, sometimes precipitating a debt crisis.

Countries thus often deviate from the textbook framework in a variety of ways. Central bank intervention in foreign exchange markets to influence exchange rates is fairly prevalent, particularly among emerging market economies, and in response to persistent capital inflows. Some Governments have adopted macroprudential measures, which aim to contain systemic risks by smoothing cyclical swings in domestic credit availability. Governments also use measures from another class of policy tools known as “capital flow management measures”. These measures come in a variety of types, including quantitative outflow restrictions, non-interest-bearing reserve requirements for financial inflows, taxes on inflows and/or outflows, or outright bans. The various measures have differing impacts and consequences, both intended and unintended.

This rich variety of policy options points to the importance of national planning in this area, which would aim to provide a more systematic approach to designing an effective macroeconomic policy mix to pursue growth, sustainable development and stability objectives, attuned to country-specific circumstances. The IMF has put forward the concept of an integrated policy framework (IPF) that draws on the host of alternatives to formulate the best policy mix to meet different countries' needs. An INFF may include an IPF as part of its approach. It would consider the role of monetary, exchange rate, macroprudential and capital flow management policies, and their interactions with each other and other policies.

The IMF is working to develop tools to provide more nuanced guidance and advice to Member States on how to design integrated policies in these areas, using modelling, empirical work, and case studies. The case studies seek to identify patterns in country behaviour. Cross-country empirical analysis explores whether these insights generalize, helping to select key features and parameters for models that closely match country conditions on the ground. Ultimately, the work should also inform IMF assessments in its annual Article IV consultations with member countries.

Table 1 provides an overview of potential elements of a financing strategy, organised by financing policy area. These include:

- i. **Policies/strategies/frameworks** that guide and prioritize the mobilisation and alignment of different types of financing and macroeconomic/systemic conditions;
- ii. **Financing instruments and regulations** that governments can deploy to put their policies into practice;
- iii. **Processes and systems** for improved coordination and information management, for example improved budgetary processes and PFM procedures;
- iv. **Actors/stakeholders** that should be involved in the process of designing, selecting, and implementing policy interventions and/or in the adoption of specific instruments;
- v. **References/resources** to existing methodologies and tools developed by various agencies, both domestic and international.



TABLE 1.

## EXAMPLES OF FINANCING STRATEGY ELEMENTS

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
<b>PUBLIC FINANCE (Action Areas A and C)</b>					
<b>Public revenue</b>	<ul style="list-style-type: none"> <li>- Revenue strategies</li> <li>- Tax policies (e.g., to enhance the progressivity of tax systems, reduce key tax distortions to growth, or support green recovery, etc.)</li> <li>- PFM reform strategies</li> </ul>	<ul style="list-style-type: none"> <li>- Different types of taxes (e.g., income tax, VAT, customs duties, etc.)</li> <li>- Public assets</li> <li>- Grants (i.e., budget support) <i>(see also international development cooperation below)</i></li> </ul>	<ul style="list-style-type: none"> <li>- Integrated Financial Management Systems (IFMS)</li> <li>- PFM reform processes</li> <li>- Professionalising public sector auditing and accounting</li> </ul>	<p>State: Ministry of Finance, Revenue authority</p> <p>Non state: Think tanks, CSOs</p> <p>International partners: World Bank, IMF, UN, bilateral development partners active on fiscal issues</p>	<ul style="list-style-type: none"> <li>- <a href="#">Platform for Collaboration on Tax Medium Term Revenue Strategies (MTRS)</a></li> <li>- <a href="#">IMF Fiscal Affairs Department technical assistance reports</a></li> <li>- <a href="#">IMF Fiscal Transparency Evaluations (FTEs)</a></li> <li>- <a href="#">Tax Administration Diagnostic Assessment Tool (TADAT)</a></li> <li>- <a href="#">IMF and WB Tax Policy Assessment Framework (TPAF)</a></li> <li>- <a href="#">Public Expenditure and Financial Accountability (PEFA) Programme</a></li> <li>- <a href="#">The Addis Tax Initiative</a></li> <li>- <a href="#">Tax Inspectors Without Borders</a></li> <li>- <a href="#">OECD Inclusive Framework on BEPS</a></li> <li>- <a href="#">UNDP Development finance assessment (cross-cutting)</a></li> </ul>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
<b>Public borrowing</b>	<ul style="list-style-type: none"> <li>- Debt management strategies</li> <li>- Medium-term budgets/ frameworks, national budget and supporting documents</li> <li>- Debt transparency policies</li> </ul> <p><i>(all relevant to debt sustainability below)</i></p>	<ul style="list-style-type: none"> <li>- Loans (concessional and non-concessional)</li> <li>- Domestic borrowing (government T-Bills, Notes and Bonds)</li> <li>- International borrowing (including sovereign and sub-sovereign)</li> <li>- 'Thematic' bonds, i.e., Green Bonds</li> <li>- Islamic finance</li> </ul>	<ul style="list-style-type: none"> <li>- Debt management principles</li> <li>- Debt sustainability analyses</li> <li>- Debt management processes</li> <li>- Cash management processes</li> </ul> <p><i>(all relevant to debt sustainability below)</i></p>	<p>State: Ministry of Finance, Central Banks, local governments</p> <p>Non state: banking association, stock exchange</p> <p>International partners: UN, IMF, World Bank and other MDBs <i>(all relevant to debt sustainability below)</i></p>	<ul style="list-style-type: none"> <li>- <a href="#">World Bank Debt Management Performance Assessment (DeMPA)</a></li> <li>- <a href="#">IMF Debt Sustainability Analysis (DSA)</a></li> <li>- <a href="#">Public Expenditure and Financial Accountability (PEFA) Programme</a></li> <li>- <a href="#">OECD Transition Finance Toolkits</a></li> <li>- <a href="#">UNCTAD DMFAS</a></li> <li>- <a href="#">Commonwealth DMP</a></li> <li>- <a href="#">UNCTAD Principles on Sovereign Lending</a></li> </ul>
<b>Public expenditure</b>	<ul style="list-style-type: none"> <li>- Expenditure strategies/frameworks</li> <li>- Annual government budgets</li> <li>- Programme based budgeting</li> <li>- SDG budgeting</li> <li>- Sector budgeting</li> <li>- Gender responsive budgeting</li> <li>- Medium Term Expenditure Frameworks (MTEFs)</li> </ul>	<ul style="list-style-type: none"> <li>- Public spending</li> <li>- Subsidies</li> <li>- Transfer payments</li> </ul>	<ul style="list-style-type: none"> <li>- Public Expenditure Tracking System (PETS)</li> <li>- IFMS</li> <li>- Improved budgetary processes and PFM procedures</li> <li>- Professionalised public sector auditing and accounting</li> <li>- Internal control systems</li> <li>- Equitable Resources Allocation systems</li> </ul>	<p>State: Ministry of Finance or other Ministries responsible for public expenditure and oversight</p> <p>Non state: CSOs, think tanks</p> <p>International partners: UN, World Bank, IMF, bilateral partners active on PFM</p>	<ul style="list-style-type: none"> <li>- <a href="#">IMF Expenditure Assessment Tool</a></li> <li>- <a href="#">Public Expenditure and Financial Accountability (PEFA) programme</a></li> <li>- <a href="#">PFM tools based on PEFA scoring mechanism</a></li> <li>- <a href="#">WB Public Expenditure Review (PER)</a></li> <li>- <a href="#">WB Public Expenditure Tracking Survey (PETS)</a></li> <li>- <a href="#">UN Women GRB Guidance and Training</a></li> <li>- <a href="#">UNDP Budgeting for the SDGs</a></li> </ul>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
			<ul style="list-style-type: none"> <li>- Systems to track gender equality budget allocations and expenditure</li> </ul>		<ul style="list-style-type: none"> <li>- <a href="#">Paris Collaborative on Green Budgeting</a></li> <li>- <a href="#">The Coalition of Finance Ministers for Climate Action (Santiago Action Plan)</a></li> </ul>
<b>Public investment</b>	<ul style="list-style-type: none"> <li>- Public investment strategies</li> <li>- Annual government budgets</li> <li>- Programme based budgeting</li> <li>- SDG/Green budgeting</li> <li>- Sector budgeting</li> <li>- Gender responsive procurement</li> <li>- Public-private partnership policy, infrastructure development strategy, budget documents</li> </ul>	<ul style="list-style-type: none"> <li>- Public investment instruments (e.g., equity, guarantees, loans)</li> <li>- Sovereign Wealth Funds</li> <li>- Blended finance instruments</li> </ul>	<ul style="list-style-type: none"> <li>- Public procurement processes</li> <li>- Financial internal control systems</li> <li>- Professionalised public sector auditing and accounting</li> </ul>	<p>State: Ministries of Finance/Economy/ Planning, or other Ministries responsible for public investment; NDBs, SOEs</p> <p>Non state: CSOs, Think tanks</p> <p>International partners: World Bank, IMF, IFC, UN, other bilateral and multilateral partners working on public investment management (including DFIs)</p>	<ul style="list-style-type: none"> <li>- <a href="#">World Bank Country readiness diagnostics for PPPs</a></li> <li>- <a href="#">WB Public-Private Infrastructure Advisory Facility</a></li> <li>- <a href="#">Public Expenditure and Financial Accountability (PEFA) programme</a></li> <li>- <a href="#">IMF Public Investment Management Assessment (PIMA)</a></li> <li>- <a href="#">UNDESA Regulatory Impact Assessment Tool</a></li> <li>- <a href="#">UNECE People-first Infrastructure Evaluation and Rating System (PIERS), including the PIERS Self-Assessment Tool</a></li> </ul>
<b>International development cooperation</b>	<ul style="list-style-type: none"> <li>- Development cooperation policies/ frameworks</li> <li>- National Development Cooperation policy/strategy</li> </ul>	<ul style="list-style-type: none"> <li>- Grants</li> <li>- Technical assistance</li> <li>- Loans (concessional and non)</li> <li>- Blended finance instruments</li> </ul>	<ul style="list-style-type: none"> <li>- Systems for donor coordination and cooperation</li> <li>- Gender policy marker</li> </ul>	<p>State: Ministry of Finance, Ministry of Planning, relevant line Ministries, NDBs</p> <p>International partners: UN, bilateral and multilateral</p>	<ul style="list-style-type: none"> <li>- <a href="#">UN Development Cooperation Forum (DCF) Surveys</a></li> <li>- <a href="#">Global Partnership for Effective Development Cooperation (GPEDC) Monitoring country profiles</a></li> <li>- <a href="#">OECD Transition Finance Toolkits</a></li> </ul>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
				donors, DFIs and MDBs  Non-state: Civil society	- <a href="#">OECD Impact Standards for Financing Sustainable Development</a>
<b>Illicit Financial Flows (also part of public revenue)</b>	<ul style="list-style-type: none"> <li>- AML/CFT policies/strategies</li> <li>- Tax policies/strategies</li> <li>- Disclosure policies (financial transactions)</li> </ul>	<ul style="list-style-type: none"> <li>- Regulation, i.e., AML/CFT</li> <li>- Tax instruments</li> <li>- Tax treaties and standards (e.g., automatic exchange of information, BEPS, etc.)</li> <li>- Asset recovery instruments</li> </ul>	<ul style="list-style-type: none"> <li>- Regulatory oversight systems</li> <li>- Information management systems and oversight</li> <li>- Asset recovery processes</li> </ul>	<p>State: Ministry of Finance, Financial Intelligence Units, Tax Administrations/ Revenue Authority, Central Bank, Auditor General, Public Account Committees</p> <p>Non state: Anti-corruption agencies, CSOs, Think tanks, Banking associations</p> <p>International partners: OECD, World Bank, IMF, UN, other partners working on IFFs</p>	<ul style="list-style-type: none"> <li>- <a href="#">Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) reviews</a></li> <li>- <a href="#">IMF Fiscal Transparency Evaluations (FTEs)</a></li> <li>- <a href="#">IMF Tax Administration Diagnostic Assessment Tool (TADAT)</a></li> <li>- <a href="#">IMF and WB Tax Policy Assessment Framework (TPAF)</a></li> <li>- <a href="#">Public Expenditure and Financial Accountability (PEFA) Programme</a></li> </ul>
<b>PRIVATE FINANCE (Action Area B)</b>					
<b>Commercial private investment</b>	<ul style="list-style-type: none"> <li>- Private sector development strategies</li> </ul>	<ul style="list-style-type: none"> <li>- Regulations, principles and standards (to increase transparency and</li> </ul>	<ul style="list-style-type: none"> <li>- Processes for private sector engagement</li> </ul>	<p>State: Central Bank, Ministries of Finance/ Economy/ Industry and</p>	<ul style="list-style-type: none"> <li>- <a href="#">IFC Private Sector Diagnostics</a></li> <li>- <a href="#">UNCTAD Productive Capacities Index (PCI)</a></li> </ul>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
<b>(domestic and foreign)</b>	<ul style="list-style-type: none"> <li>- Industrial development strategies</li> <li>- SME development policies</li> <li>- Sustainable investment promotion policies (including for foreign investment)</li> <li>- Financial sector development strategies (<i>see also under financial sector stability below</i>)</li> <li>- Financial inclusion strategies</li> <li>- Banking supervision frameworks</li> <li>- Sustainable financial market roadmaps</li> <li>- PPP policy frameworks/ strategies<sup>2</sup></li> </ul>	<ul style="list-style-type: none"> <li>- sustainable development alignment)</li> <li>- PPPs (involving the private sector in public service delivery)</li> <li>- Blended finance, including guarantees, mezzanine finance, equity/quasi equity investments, loans to private entities, etc.</li> <li>- Digital finance</li> <li>- Tax rebates and other incentives (e.g., temporary exemptions)</li> <li>- Private sector sustainable investment disclosure regulations</li> </ul>	<ul style="list-style-type: none"> <li>- Regulatory oversight systems</li> <li>- Information management systems and oversight</li> <li>- Policy dialogue processes</li> </ul>	<p>Commerce, Financial regulatory authorities, NDBs, investment promotion agencies</p> <p>Non-state: Private sector associations, chambers of commerce, business councils, stock exchange, banking Associations, institutional investors</p> <p>International partners: UN, IMF, World Bank and other MDBs, bilateral development partners working on private sector development, including DFIs</p>	<ul style="list-style-type: none"> <li>- <a href="#">IMF Financial Development Index</a></li> <li>- <a href="#">IMF Financial Sector Assessment Programme (FSAP)</a></li> <li>- <a href="#">UNCTAD Investment Policy Reviews</a></li> <li>- <a href="#">Joint database of published diagnostics by MDBs and other development partners</a></li> <li>- <a href="#">WB National Financial Inclusion (NFIS) Toolkit</a></li> <li>- <a href="#">World Bank Doing Business reports</a></li> <li>- <a href="#">World Bank Enterprise Surveys</a></li> <li>- <a href="#">UNDP Inclusive business ecosystem development</a></li> <li>- <a href="#">SDG Impact Standards</a></li> <li>- <a href="#">UNEP-UNDP Sustainable finance diagnostic</a></li> <li>- <a href="#">Joint database of published diagnostics by MDBs and other development partners</a></li> <li>- <a href="#">OECD-UNDP Framework for SDG-Aligned Finance</a></li> <li>- <a href="#">OECD MNE Guidelines</a></li> </ul>

<sup>2</sup> E.g., [Philippines' Local PPP Strategy](#); [Guyana's PPP Policy Framework](#)

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
					- <a href="#">Women's Empowerment Principles (WEPS)</a> <a href="#">UNDP SDG Investor Maps</a>
<b>Impact investment</b>	- Impact investing policies /responsible investment frameworks	- Tax and other incentives - Blended finance/ 'Private sector instruments', incl guarantees, mezzanine finance, equity investments, loans to private entities (to increase scale of private sector investment that is aligned with sustainable development)	- Regulatory oversight systems - Information management systems - Private sector engagement processes	State: Ministries of Finance/ Economy/ Planning, Central Bank, Financial regulatory agencies  Non-state: Impact investors networks, business councils, banking Associations, stock exchanges  International partners: UN, DFIs and MDBs	- <a href="#">Global Investors for Sustainable Development Alliance</a> - <a href="#">UN Global Compact Principles</a> - <a href="#">IFC Impact Principles</a> - <a href="#">OECD Impact Standards for Financing Sustainable Development</a> - <a href="#">Principles for Responsible Investment</a> - <a href="#">KfW Innovative Financing Toolbox</a>
<b>Remittances (diaspora financing)</b>	- Diaspora engagement policies and strategies (e.g., <a href="#">Jamaica</a> ) - Remittances policies and strategies	- Regulation (to increase/facilitate remittance flows) - Diaspora mutual funds (e.g., <a href="#">Rwanda</a> ) - Investment incentives for the diaspora - Grant programmes (e.g., matching grants with	- Regulatory oversight systems - Information management systems and oversight	State: Central Bank, Ministry of Planning/ Finance, Financial regulatory agencies, Office or division responsible for diaspora affairs  Non-state: diaspora networks, (private	- <a href="#">UNDP Guidelines and Case Studies on Remittances (Diaspora Financing)</a>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
		diaspora investments) <sup>3</sup> - Trusts that can serve as single window for philanthropy from diaspora (e.g., <a href="#">India</a> )		sector) banks, money transfer operators and mobile money operators	
<b>Philanthropic giving</b>	- National plan, relevant sector and thematic strategic plans	- Regulation (to facilitate philanthropic flows and/or the establishment of NGOs and foundations, and to align use of philanthropy with national priorities) <sup>4</sup> - Blended finance mechanism	- Systems for philanthropic coordination and cooperation	State: Ministry of Planning, relevant line ministries  Non-state: Foundations (individual and corporate), NGOs/NGO networks, large Foundations, faith networks	- <a href="#">Civicus: Enabling environment national assessments</a>
<b>MACROECONOMI/ SYSTEMIC CONDITIONS (Action Areas E and F)</b>					
<b>Debt sustainability</b>	<i>(see public borrowing above)</i>	- Debt management practices - Inflation indexed bonds - Debt buy backs - Debt swaps	<i>(see public borrowing above)</i>	<i>(see public borrowing above)</i>	<i>(see public borrowing above)</i>

<sup>3</sup> E.g. in Kosovo: [https://www.ks.undp.org/content/kosovo/en/home/operations/projects/poverty\\_reduction/DEED.html](https://www.ks.undp.org/content/kosovo/en/home/operations/projects/poverty_reduction/DEED.html)

<sup>4</sup> For examples of philanthropy-related regulations see: <https://www.icnl.org/resources/research/ijnl/legal-framework-for-global-philanthropy-barriers-and-opportunities>

AAAA Action Areas	POLICIES/ STRATEGIES/ FRAMEWORKS	FINANCING INSTRUMENTS/ REGULATIONS	PROCESSES/ SYSTEMS	ACTORS (to engage)	USEFUL REFERENCES/ RESOURCES
<b>Macroeconomic and financial sector stability</b>	<ul style="list-style-type: none"> <li>- Macroprudential policies</li> <li>- Monetary policies</li> <li>- Exchange rate policies</li> <li>- Financial sector development strategies (<i>see also under private investment above</i>)</li> <li>- Financial inclusion policies</li> <li>- Capital flows management policies</li> </ul>	<ul style="list-style-type: none"> <li>- Regulation</li> <li>- Capital controls</li> <li>- Risk management</li> </ul>	<ul style="list-style-type: none"> <li>- Early warning systems</li> <li>- Inter-agency coordination processes</li> <li>- Reserve and Asset Management practices</li> <li>- Diagnostic assessment processes</li> <li>- Financial oversight processes</li> </ul>	<p>State: Central Bank, Ministry of Finance, financial regulatory authorities</p> <p>Non-state: domestic financial institutions, banking associations, institutional investors</p> <p>International partners: UN, IMF, FSB, BIS</p>	<ul style="list-style-type: none"> <li>- <a href="#">IMF Financial Development Index</a></li> <li>- <a href="#">WB Reserve Advisory and Management Partnership (RAMP)</a></li> <li>- <a href="#">IMF Integrated Policy Framework</a></li> </ul>



### 3.3 Limitations

In practice, implementing INFFs and formulating effective financing strategies requires overcoming numerous deep-rooted challenges, as well as recognizing some fundamental limitations. Potential challenges include:

- Strategies are time-bound, emphasizing the need to regularly update assessments and diagnostics (and embed these in the policymaking process), rather than considering them as one-offs;
- Data limitations and blind spots (i.e., where data is weak or unavailable, where there is a high degree of uncertainty about forward projections, or a lack of capacities) need to be acknowledged by policymakers;
- Governance challenges to overcoming policy siloes may include persistence of sectoral priorities and fragmentation of government, potential lack of political will and prioritization, and poor design and articulation of priorities.

Successfully implementing an integrated financing strategy is a multifaceted process cutting across many areas, which often cannot be changed in the short-term. To respond to these limitations and challenges, policymakers need to be cognizant of existing national efforts, capacities, and constraints. Where data, capacity, or governance constraints prohibit a more structured approach, a more ad hoc use of the guiding process presented below can still provide valuable insights and help bring more analytical rigor to the inherently political process of strategy development.

## 4. ‘How To’ – Financing strategies in practice

This section puts forward a step-by-step approach to formulate financing strategies that are coherent, sustainable and risk-informed. While INFF financing strategies will differ from country to country, in all cases, the strategy must emerge through active iteration and learning, guided by national governments in collaboration with other relevant stakeholders (see [Building Block 4 Governance and Coordination](#)). It focuses on leveraging existing

assessments and frameworks to identify policy options, building on local and international good practices where possible.

While this process is not linear, this section outlines a sequenced approach to understanding the steps policymakers could take (Figure 4), including several toolkits and templates that may be used to help guide the process.

FIGURE 4. STEP BY STEP GUIDANCE

### STEP 1: ESTABLISH SCOPE AND FINANCING POLICY OBJECTIVES

- *What needs are you trying to address with your financing strategy? What is the required scope and approach (e.g., national/ subnational)?*
- *What financing gaps did the BB1 assessments identify? Which sectors are particularly underfunded?*
- *What are the opportunities, risks, and binding constraints identified (current situation analysis)?*
- *What are your financing policy objectives? Who should be involved?*

### STEP 2: IDENTIFY POLICY OPTIONS

- *What existing policies, legal or regulatory measures, financing instruments, or processes support the achievement of the objectives defined in Step 1?*
- *What do existing strategies/frameworks/assessments show in terms of potential policy solutions? Which financing instruments are particularly promising?*
- *What further opportunities exist (can stakeholders or partners identify additional solutions based on their experiences)?*

### STEP 3: POLICY PRIORITISATION

- *To what extent do policies align with the coherence, sustainability, risk checks?*
- *What trade-offs/externalities have to be considered?*
- *What integrated approaches, solutions and scenarios can policymakers pursue?*
- *To what extent are preconditions (institutional, procedural, etc) and resource requirements met? What solutions can policymakers pursue?*
- *What policies can be implemented in the near term, and which in the medium-long term?*

### STEP 4: OPERATIONALISATION

- *Which actions need to be taken for the policy outcomes? What time-frame applies to your measures? How should interventions be sequenced?*
- *Who should be responsible for their implementation, and who needs to be consulted?*

## 4.1 Step 1: Establish scope and financing policy objectives

The scope and form of the financing strategy will differ depending on country circumstances and needs. In some cases, national authorities may want to develop a comprehensive strategy document (time-bound, action items). In other cases, it may serve to better tie together existing strategies and documents and link them to national sustainable development strategies or plans. Similarly, the financing strategy may focus on specific sectors or financing policy areas, considering synergies and trade-offs, or address the full range of financing sources and their contributions to a national development plan (a good practice is for a financing strategy to support a national development plan). In all cases, developing an integrated financing strategy is a country-led process that requires an inclusive approach. It is important to involve many agents (state and non-state) from the outset, as they will bring different perspectives and foster integrated thinking.

Polymakers also need to determine the financing objectives of the strategy. These can be formulated on two related levels. The first level includes matching needs assessments to resources, such as public revenues, aid, and sometimes private financing. The second level comprises financing policies, regulatory frameworks, and other aspects of the enabling environment—which aim to align financing and behaviour with sustainable development. These policies will also impact and can reduce funding needs. In all cases the financing strategy aims to foster integrative thinking from the start (e.g., ensuring that tax and investment policies are not conflicting, or that macroeconomic, trade and technology policies jointly reinforce overarching development priorities).

In most countries, the objectives of financing strategies will respond to needs arising from national development strategies, as identified in the

Assessments and Diagnostics phase (Building Block 1) (see Table 2), namely:

- i. Financing opportunities, e.g., increase the availability of private finance for renewable energy, or increase FDI in line with peer countries (from building block 1.2);
- ii. Estimated financing gaps at macro/ sectoral/ programmatic level (depending on the level of analysis used in building blocks 1.1-1.2), e.g., mobilise institutional investors to close the private finance gap in affordable housing, energy, or digital investments, or reduce the gender gap in financial inclusion;
- iii. Specific binding constraints, e.g., overcome inefficiencies in tax collection (from building block 1.4);
- iv. Financing policy objectives based on the risk assessment, e.g., strengthen capital account management, including prudential regulation (from building block 1.3).

The financing policy objectives should be clearly defined and it may be helpful to standardize their level of detail. The key is to provide enough specificity to guide the policy identification process and to be consistent in the level of detail used.

TABLE 2.

## DEFINING FINANCING POLICY OBJECTIVES

<b>Financing objectives</b> List objectives to be pursued through the financing strategy with the aim of closing financing gaps, maximising opportunities, and addressing binding constraints E.g., Increase FDI in the energy sector (private finance)			
<b><u>Financing gaps</u></b>	<b><u>Opportunities</u></b>	<b><u>Risks</u></b>	<b><u>Binding constraints</u></b>
List estimated financing gaps – at macro/ sectoral/ programmatic level (depending on level of analysis used in financing needs and financing landscape assessments)  E.g., Rs1.3 trillion gap in private finance in the energy sector (Nepal example in Building Block 1.2 guidance)	List financing opportunities emerging from the financing landscape assessment  E.g., Higher levels of FDI in peer countries compared to domestic economy (Philippines example in Building Block 1.2 guidance)	List risks emerging from the risk assessment  E.g., Collapse in global commodity prices (example in Building Block 1.3 guidance)	List specific obstacles identified in the binding constraints diagnostic  E.g., Inefficient financial intermediation due to bureaucratic loan application process and high collateral requirements (Egypt/ Sri Lanka examples in Building Block 1.4 guidance)

## 4.2 Step 2: Identify policy options

National authorities will need to identify policies, legal or regulatory measures, financing instruments, and processes that can support the achievement of the objectives defined in Step 1. Policymakers can consider a broad range of options at this point. Identifying policy options is a consultative process, using existing tools and resources to determine policy solutions and recommendations.

Policymakers can use the following two questions to guide their efforts: (i) what is already in place (strengths/weaknesses/gaps)?; and (ii) what further opportunities exist?

### *i. What current practices and initiatives are in place?*

Start by mapping all relevant recent or current practices and initiatives as the basis for a holistic, integrated approach to financing and the identification of solutions for the financing objectives articulated in Step 1. It is essential first to answer what initiatives are currently used, and how they could be brought together within a holistic financing strategy, before addressing the question of further opportunities. Starting with current practices is also a potentially empowering way of ensuring that local authorities develop a clear view of the problem and provides national ownership of the process.

TABLE 3.

## EXAMPLE OF MAPPING OF CURRENT PRACTICES

FINANCING OBJECTIVES	GOVERNMENT ACTIONS	RESPONSIBLE GOVERNMENT INSTITUTION	ASSESSMENT INDICATOR		PARTNER SUPPORT	STATUS AND SUITABILITY OF ACTIONS (strengths, weaknesses, gaps)
			INDICATOR OF PROGRESS	BASELINE		
Development of domestic debt markets	Normalise and extend the yield curve	Ministry of Finance	DeMPA	2019	Support domestic capital market development (AfDB), WBG	Ongoing. No progress until cash management issue resolved.
	Enhance secondary market activities		DSA	2018		
	Introduce a wider spectrum of instruments		PEFA	2017		
	Introduce a wider spectrum of instruments		INFF Building Block 1	2021		
Overcome inefficiencies in tax collection	Improve tax policy design, legislation framework and tax and customs administration	Ministry of Finance and Revenue Administration	TADAT	2017	TA support to Ministry of Finance and revenue administrations (IMF, Germany-GIZ)	Ongoing. Updating tax laws potential low hanging fruit not realised.
			MTRS	2018		
Increase private finance in the renewable energy sector	Develop risk sharing instrument to leverage private investment for renewable energy	Ministry of Finance, Ministry of Commerce, Ministry of Environment	FSAP	2018	TA support (Germany-KFW)	Ongoing. Local good practice, with potential to be replicated.
			WB LTF Diagnostic	2019		
Better align the national budget with the SDGs	Institutionalise consideration of SDGs in budget formulation and establish systems to track SDG-aligned expenditures	Ministry of Finance	UN Women Gender Responsive Budgeting Diagnostics	2018	TA support to Ministry of Finance and line ministries (UNDP, UN Women, UNDRR)	Ongoing. Weak budget execution procedures and controls remain a challenge. Developing clear procurement guidelines potential low hanging fruit.
			UNDRR Risk Informed Budget Reviews	2019		
			INFF Building Block 1.2	2021		

The foundation for this mapping should be the policy mapping undertaken as part of the [inception phase](#), as well as the scoping done on existing policy frameworks as part of the in-depth assessments and diagnostics undertaken under Building Block 1. The financing needs, landscape and risk assessments identify financing policy challenges, opportunities

and risks related to current practices. They flag areas where underlying market, policy or capacity constraints may be inhibiting effective mobilization and use of financing. The binding constraints diagnostic deepens the analysis of impediments and their root causes, and can help inform the mapping of current practices further.

The mapping exercise should cover all relevant government actions and actors, as well as support efforts by financial institutions, international organizations, and non-state actors to tackle any aspect identified in Step 1. Make use of existing national assessments, program evaluations, or strategies to determine what current practices and initiatives are already in place. For instance, it may be useful to revisit an annual report from an ongoing financial sector development program or consult sector financing strategies that are being implemented.

To leverage international expertise, revisit recent (last three years) assessments, tools, or frameworks carried out in your country. International organizations carry out targeted analysis and assessments that can inform analysis of current practices (see Table 1 for a comprehensive overview of tools to consult). For example, the IMF Fiscal Affairs Department Technical Assistance reports provide evidence on key impediments of fiscal policy and processes at the country level. Reports on public sector balance sheets, medium-term budget frameworks and fiscal risk management can shed light on important institutional gaps that may in turn inform more detailed and in-depth analysis of current practices. Fiscal transparency diagnostics can be used to pinpoint key weaknesses in relation to fiscal reporting, forecasting and budgeting, risk analysis and management, and resource revenue management, which in turn can flag possible related institutional or capacity constraints. Public Expenditure Tracking Surveys (PETS) can inform sector-specific assessments of how public resources flow through different levels of administration and to identify specific challenges such as leakages or issues related to the deployment of human resources at the service provision level.

Table 3 above can be used as a template to document and map current practices. Based on the resources outlined above, select the most relevant information on current policy measures including any

strengths, weaknesses, or gaps to consider going forward. This process will provide the basis for identifying further opportunities.

## ***ii. What opportunities exist to fill gaps, and strengthen policies, frameworks, and institutions further?***

Reform efforts often focus on replacing the current internal practices with external good practices. There are, however, more options for policymakers to work with than just these two. Notably, when introducing new policy and reform ideas, policymakers can consider the following solutions: local good practices, low hanging fruit, external good practices, or hybrid solutions.

While “right” or “best” solutions are context-specific and hard to identify, policymakers should always consider two dimensions when determining policy options: whether solutions are technically correct (i.e., they address the objective identified and they are proven to solve the problem being considered), and whether they are administratively and politically feasible (have the solutions proved to work in this context, such that the people in the context know how to implement them?).<sup>5</sup>

**Local good practices** are the first opportunity and refer to ideas that are already being acted upon (they are thus possible), yielding positive results (solving the problem, and thus being technically correct). Policymakers identified these in the previous step during the mapping exercise. In some cases, these solutions can be scaled up or replicated in different sectors/ areas. For example, policymakers may replicate a successful early-stage project risk sharing facility in the renewable energy sector in other sectors, such as agribusiness.

**Low-hanging fruit** is the second area of opportunity. Based on the mapping of current practices, these refer to ideas not yet acted upon, but which would require relatively little effort to

<sup>5</sup> Based on the work of [Andrews, Pritchett, and Woolcock \(2017\)](#).



emerge and be institutionalized. For instance, in many cases, existing practices may offer opportunities for small improvements. Policymakers can identify these opportunities by engaging with practitioners in the field who often think about ways to improve practices but lack incentives to share their ideas.

should start by grouping a few of these (rather than settling on one prematurely). Policymakers must translate these ideas to local contexts. Specifically: (i) does the idea come from a similar administrative context?; (ii) why was the practice done, and how was it done?

## BOX 2.

## ROLE OF INTERNATIONAL INSTITUTIONS IN HELPING IDENTIFY POLICY OPTIONS

International institutions can play an important role in supporting governments as they shape the financing strategy. Governments can use these partnerships to identify, design, and implement policy solutions that will advance the objectives of the financing strategy.

Many international partners have significant expertise to support governments in the process of developing practical policy solutions. With their substantive expertise and engagement across country contexts, international partners often have knowledge of potential financing solutions that may be relevant to national institutions and priorities. They can act as a source of ideas for potential innovations and facilitate exchange between countries with experience in particular areas of financing. International partners can often offer technical assistance in designing and adapting solutions, whether concerning policy change, regulatory reform, adapting or introducing financing instruments, or building processes to manage financing policies. International partners can also provide capacity building support that helps governments build up the capability to deliver and manage effective financing policies.

Governments can access support from international partners across a wide range of public and private financing policy solutions. In terms of practical guidance on which partners hold expertise in each area of financing, the assessments and diagnostics guidance highlights tools offered by different partners (see also Table 1 in Section 3 above), and many of these diagnostic services can feed into and shape the development of specific financing solutions. Governments can build on existing collaboration with international partners. The process of developing policy options within a financing strategy may prompt dialogue about adapting or expanding existing programming in line with the INFF process. Governments can also reach out to international partners that offer services across a range of financing areas; for example, [UNDP's Finance Sector Hub](#) provides peer examples and services across seven public and private financing areas in relation to INFFs.

**External good practices** refer to ideas that have proven themselves in other country contexts and are technically correct. These are often the first set of ideas suggested by partners and international organizations. As mentioned above, policymakers can access the diagnostic services and existing collaborations with international partners to identify and develop financing policy options. Countries

Ultimately, combining different practices could lead to **hybrid policy solutions**. In most cases, the process described above yields positive and negative lessons from each solution—with no single idea proving to be “the solution.” These lessons lead to the emergence of new hybrids or locally constructed solutions that blend elements and lessons from different areas of opportunity.

All policy ideas and solutions identified as part of Step 2 (i.e., those deemed technically correct and administratively and politically feasible) can be summarised in a table, before being considered in an assessment process as part of Step 3. All policy solutions will have associated costs and benefits, including trade-offs as well as possible externalities. These will be considered in the next step.

### 4.3 Step 3: Policy prioritisation

An assessment exercise can help prioritise policy solutions identified in Step 2. The approach can be used as part of a policy assessment at any level – national, sectoral, project-specific. It aims to foster integrated thinking and creative approaches to mobilize finance, avoid fragmented decision-making, and consider financing policies in different areas alongside each other to increase their impact.

Policy prioritization can take place in two phases: (i) **coherence checks** to make trade-offs and integration explicit, and (ii) assessment of

**preconditions and resource-requirements** to support sequencing of interventions. It is guided by explicit evaluation checks, toolkits, and templates, to ultimately support a decision on whether policy interventions can be implemented in the near-term, and what longer-term efforts would need to be put in place. This approach considers inherent trade-offs and externalities in policymaking, ultimately weighing up costs and benefits of policy choices, and exploring creative solutions to overcome impediments by combining policy options with other policies, instruments, and regulations.

**Coherence checks** should be applied to all policy options identified in Step 2 (e.g., using Table 4a or a similar format), asking three overarching questions:

- i. Have **macro checks** been considered (are policies consistent with macro-objectives, i.e., growth targets, debt sustainability targets, etc.)? <sup>6</sup>
- ii. Have **coherence checks** been considered (i.e., are they aligned with all dimensions of sustainable development, or do they

TABLE 4a.

#### TEMPLATE FOR ASSESSING POLICY OPTIONS

POLICY OPTIONS	MACRO CHECK	COHERENCE CHECK	RISK CHECK
List policy options identified in Step 2	Note the extent to which the option: <ul style="list-style-type: none"> <li>- Is consistent with macro-economic targets</li> </ul>	Note the extent to which the option: <ul style="list-style-type: none"> <li>- Contributes to dimensions of sustainability (economic, social, environmental)</li> <li>- Creates trade-offs/externalities</li> <li>- Creates win-wins and synergies across sectors/actors</li> </ul>	Note the extent to which the option: <ul style="list-style-type: none"> <li>- Reduces risk/ increases resilience of the country's ability to finance SD outcomes over time</li> <li>- Could create new risk</li> </ul>
Template to be filled in...			

<sup>6</sup> See also Benedek, D., E. Gemayel, A. Senhadji, and A. Tieman, 2021, "A Post-Pandemic Assessment of the Sustainable Development Goals," *IMF Staff Discussion Note, forthcoming, International Monetary Fund, Washington, DC* for a methodology useful for the macroeconomic coherence checks.



jeopardise any dimension of sustainability; what trade-offs/externalities need to be considered, do they have strong linkages across sectors and enable win-wins)?

- iii. Have **risk checks** been considered (i.e., are they sufficiently risk informed, or could they create new risk)?

Answering these questions can help reveal whether policy options are not well-aligned with some sustainable development priorities, or whether they have unintended consequences that need to be considered. Retain those policy options that are deemed to be well-aligned with sustainable development as is. For other policy options, start by highlighting trade-offs and externalities. Trade-offs

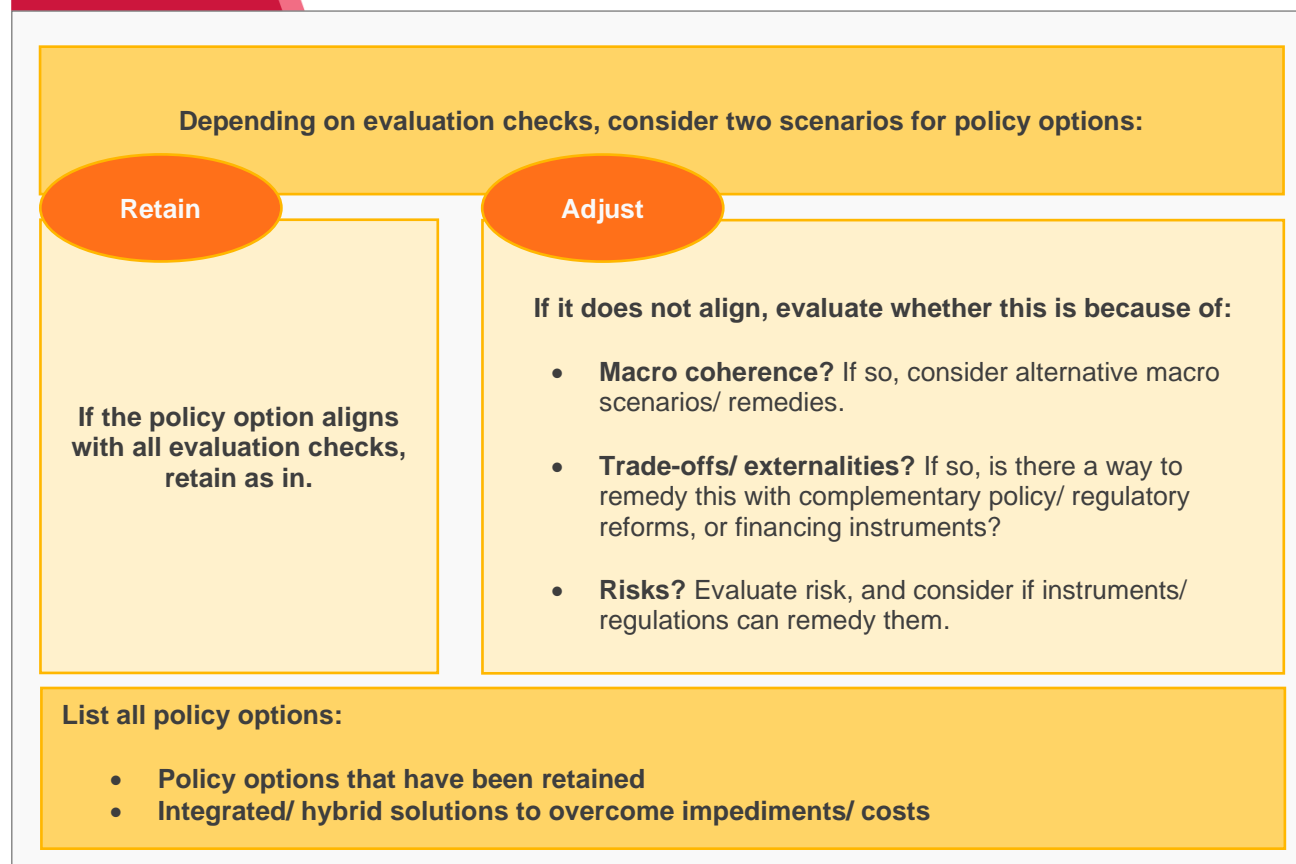
can then either be accepted, or remedies considered. In some cases, potential trade-offs or externalities can be reduced or avoided altogether by discrete policy interventions.

Governments have a vast array of tools, instruments, and regulations available to foster integrated solutions (revisit Table 1 for an overview).

They can strengthen investors' enabling environment via regulatory, legal, and institutional reforms. They can enhance the effective progressivity of their tax systems, reduce key tax distortions to growth, exploit corrective taxes, and set tax incentives to increase the financial return for investors or minimize potential negative externalities.<sup>7</sup> They can also share risk at the

FIGURE 5.

## THE POLICY PRIORITISATION APPROACH: OVERCOMING IMPEDIMENTS



<sup>7</sup> Tax incentives are often inefficient and have the potential to erode the tax base, therefore their role in the policy mix should be carefully assessed.

project/investment level by using blended financing instruments to mobilise private sector investment (Box 5 below summarises the opportunities and risks associated with the use of public-private instruments).

In some cases, however, there may be trade-offs that cannot be remedied in the short term, e.g., due to fiscal constraints, or critical **preconditions** missing that prevent certain interventions. Some of these may have been highlighted in the binding constraint analysis. For example, provision of guarantees for financing of large infrastructure projects, electricity production, or transportation creates fiscal risks that can ultimately undermine debt sustainability. The success of policies to increase access to long term finance via domestic financial markets depends on mature capital markets, functioning oversight bodies, and a stable domestic banking sector being in place. To address such underlying constraints or preconditions, medium-to long-term approaches will be needed.

Programs and policies require resources, institutions and processes to function. What is more, policies typically cross over multiple authority domains in which many different agents and processes act to constrain or support behaviour.

To check resource constraints and preconditions, the following questions should be asked:

- i. Have **preconditions** been considered (i.e., are the institutional preconditions in place, does it enjoy the required political backing, are there available instruments that could support its implementation)?
- ii. Have **resource requirements** been considered (i.e., can it rely on existing capacity for effective implementation/ are financial resources available for its implementation)?

If policy options align with preconditions and resource checks, they present opportunities for 'quick wins'. In case they do not, remedies can be considered to alleviate constraints in the medium and long-term (Figure 6). Policy interventions can be prioritized and sequenced, e.g., by embarking on a medium-term effort to raise revenue, through medium-term revenue strategies (see Box 4), or additional stand-alone strategies, e.g., a long-term finance strategy for the domestic financial sector. Policymakers can also make specific donor support requests on the basis of this assessment.

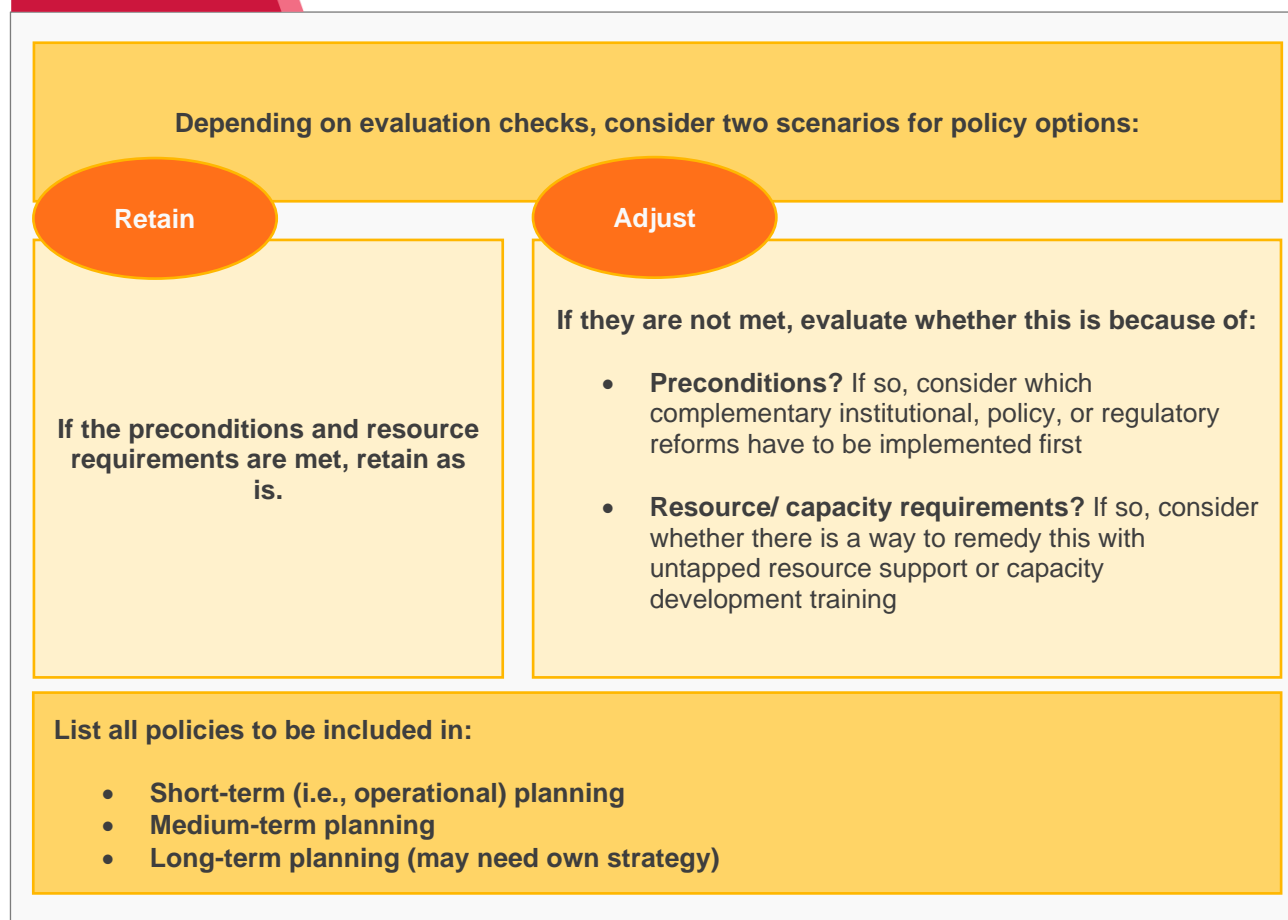
TABLE 4b.

### TEMPLATE FOR PRIORITISING POLICIES FOR IMPLEMENTATION

POLICY OPTIONS	PRECONDITIONS	RESOURCE REQUIREMENTS
List policy options from previous step (see Figure 6)	Note the extent to which: <ul style="list-style-type: none"> <li>- There is political backing for the option</li> <li>- Relevant institutions/ processes/instruments are available/ can be deployed to support implement action of the policy option</li> </ul>	Note the extent to which: <ul style="list-style-type: none"> <li>- Capacity exists for effective implementation (or there are plans in place to secure required support to build the necessary capacity)</li> <li>- Financial resources exist and can be allocated to its implementation (or can be secured from development partners)</li> </ul>
<i>Template to be filled in...</i>		

FIGURE 6.

## THE POLICY PRIORITISATION APPROACH: IDENTIFYING TIMEFRAMES



BOX 3.

## EXAMPLE – REDUCING CARBON EMISSIONS IN CHILE <sup>a</sup>

In 2014, Chile initiated a comprehensive tax reform, including three green taxes: a carbon tax, a tax for local pollutants and a tax for vehicles. This box will focus on the decision-making process and considerations by Chilean policy makers around adopting a carbon tax, which included many of the elements put forward in the step by step guidance for developing a financing strategy.

Chile's comprehensive tax reform was linked, from the outset, to broader sustainable development objectives, including to reduce local atmospheric pollution, as well as carbon emissions to comply with Chile's national commitments under the Paris Agreement. The overall **financing policy objectives (Step 1)** of the tax reform were to (i) raise additional resources of 3 per cent of GDP to finance education and other social spending and close the structural deficit, and (ii) to enhance progressivity of the tax code. While changes to income tax system were the key pillar of the reform, it also included green taxes. Such green taxes contribute to the overall resource mobilization objectives. But they also help align the tax system and investment incentives with environmental policy goals, by internalizing the environmental costs generated by economic activity – in other words, by creating a cost for polluting.

There are many different ways to reduce atmospheric pollution and harmful emissions – emissions trading systems, carbon taxes, fuel taxes, removal of fossil fuel subsidies, regulations, payments for emission reductions, and others can all be used. In Chile, the main **policy option identified (Step 2)** was a carbon tax, chosen due to its administrative feasibility (in contrast to a cap and trade policy), and resource mobilization potential. Both the carbon tax and the tax on local atmospheric pollution tax direct emissions – they target emissions from specific liable stationary facilities (those with combined power capacity of 50 Megawatt or more).<sup>b</sup> This specific tax design choice was informed by a range of efficiency and equity considerations that mirror **coherence and preconditions checks in Step 3**.

The overall tax reform was directly linked to macroeconomic objectives, seeking to close a long-standing structural deficit (**macro check**). With a focus on income taxation, responding to a highly skewed income distribution, and targeted efforts to close tax evasion and avoidance opportunities, the reform was also well aligned with Chile's equity targets (**coherence check**). Considerations around policy coherence also informed the specific design of the carbon tax: its primary objective was to reduce pollution, but policy makers also considered unintended consequences and impacts on economic and social objectives. Rising prices of the goods and services produced by liable stationary facilities could disproportionately affect poor households, and ultimately impact growth prospects, depending on the tax rate and the affected group. To analyze the trade-offs, Chile carried out an analysis on the possible impact of the planned CO<sub>2</sub> tax on consumers (both firms and households). It showed that the intended rate – which was relatively low and only placed on turbine and boilers within a power generation above a certain threshold - would result in very little impact on consumers. In terms of **risk checks**, the tax proposals were directly informed by the desire to address risks arising from climate change and local pollution.<sup>c</sup>

Policy makers also considered **preconditions and resource requirements**. Building relevant institutional infrastructure is a key precondition. In the case of Chile, to correctly track and price emissions, a robust system for measurement, reporting and verification (MRV system) was implemented, and the coordination between various actors strengthened. Constitutional constraints also influenced policy design, in particular the prohibition to expressly discriminate among economic sectors. **Required political backing** was secured by introducing the carbon tax within a larger tax reform. To address **resource and capacity requirements**, Chile took proactive steps to build capacity in the public and private sector, including through capacity building workshops and dialogue with private and public stakeholders.

Tax reform **operationalization (Step 4)** was carried out over a period of 3 years, with the carbon tax coming into force in 2017, following three years of extensive preparations and coordination with relevant stakeholders. Pursuant to a reform passed in 2019, Chile broadened the tax base and is now also working on developing an offset regulation which is expected to be operational in 2023. While the initial carbon tax was low, for the above noted reasons, it thus nonetheless acted as a signaling device, and supported the development of an institutional infrastructure. It provided the basis for more ambitious steps down the road – a key lesson identified by policy makers involved in the process.<sup>d</sup> With these measures, Chile started paving the way towards implementing an Emissions Trading System (ETS) in the medium to long term, illustrating the iterative nature that also underlies the Financing Strategy Guidance process.

<sup>a</sup> This illustration is inspired by the green tax reforms introduced in Chile starting in 2014. However, it does not claim to paint a full picture of the respective decision-making processes in Chile but rather tries to illustrate, with a very practical example, how the INFF Financing Strategy Guidance can help structure decision-making processes to identify and implement integrated financing solutions.

<sup>b</sup> See for example: Committee of Experts on International Cooperation in Tax Matters. 2019. Environmental tax issues. Discussion Note. Nineteenth session, Geneva, 15-18 October 2019. E/C.18/2019/CRP.233. [https://www.un.org/esa/ffd/wp-content/uploads/2019/10/19STM\\_CRP23-Environmental.pdf](https://www.un.org/esa/ffd/wp-content/uploads/2019/10/19STM_CRP23-Environmental.pdf).

<sup>c</sup> According to Kreft *et al.* (2017), cited by Pizarro and Pinto, losses caused by climate change in Chile amount to USD 2.6 billion (*Chile: impuestos verdes, diseño e implementación; included in Precio al Carbono en América Latina. Tendencias y Oportunidades* – SPDA and Konrad Adenauer Stiftung, 2019).

<sup>d</sup> See for example: [Rodrigo Pizarro. 2019. Lessons from the Carbon Tax in Chile. Presentation for the Coalition of Ministers of Finance for Climate Action.](#)

## BOX 4.

## LEVERAGING EXISTING FRAMEWORKS: CASE EXAMPLE MTRS

Integrated National Financing Frameworks (INFFs) provide a framework to raise financing for sustainable development in a holistic manner, bringing together different financing policy areas (public and private financing and macro-systemic issues), and better aligning them with medium- and long-term national sustainable development priorities. Medium-Term Revenue Strategies (MTRS) can be an important component of this approach.

MTRS help countries undertake comprehensive tax system reform for boosting tax revenues over the medium term. They can play an important role in supporting governments shaping a financing strategy, particularly when domestic resource mobilization is a priority. INFFs could help countries leverage the ongoing work of an MTRS, linking it prominently to the financing of a national strategy or plan, while also better aligning tax system reforms with other policy areas, by avoiding fragmented decision-making.

The MTRS comprises four interdependent components which governments must undertake for sustained tax reforms in a country, including:

1. **Setting a revenue mobilization target** – considering spending priorities required to support economic and social development. This exercise has to be led by the government and, at the same time, be inclusive, involving a broader stakeholder community (ideally society as a whole).
2. **Designing a MTRS road map**—covering tax policy, revenue administration, and the legal framework. This broad approach allows for policy, administrative and legal framework linkages to influence the overall tax system effectiveness. Policymakers drafting INFF financing strategies can leverage these ideas, and consider them in an integrative manner and other financing policy options.
3. **Sustaining a medium-term commitment to reform** – for the drafting and implementation of the tax system reform, sustained political support is necessary. As with an INFF, a whole-of-government approach is crucial to support tax system reform formulation and implementation across its different fronts. Some reforms demand support from government entities beyond the revenue agencies and the ministry of finance. For example, enforcement of taxpayers' compliance in certain sectors demands cooperation with other enforcement agencies.
4. **Engaging with external development partners** – to solicit support for the government led tax reform strategy and process. While resources for the tax reform process are to be identified and allocated domestically, the fourth component provides for coordination with external bilateral and multilateral development partners for efficient planning and allocation of resources the provision of technical assistance.

## BOX 5.

## PUBLIC-PRIVATE INSTRUMENTS: THE NEED FOR A TAILORED APPROACH

When thinking about public-private finance policies as part of a financing strategy, policymakers can consider blended finance as a potential instrument to mobilize private finance. Blended finance is most relevant for investments with **high sustainable development impact that** are not attracting private investment **but still have a solid business rationale** and potential cash flows. As part of this process, national authorities need to consider the attendant risks, trade-offs, and preconditions that come with these instruments (see Figure 7).

While blended finance can be an option to support post COVID-19 recovery efforts, **a new approach to blended finance is necessary** to improve its impact. This approach should include:

- i. Using blended finance as part of the broader toolbox of instruments to finance national priority investments and develop national productive capacities; **A country-led blended finance analysis** within an Integrated National Financing Framework (INFF) could guide development partners on where and how to use blended finance;
- ii. A shift to focus on **sustainable development impact** rather than bankability and leverage volumes;
- iii. Providing capacity development, and **enhancing transparency in reporting** and monitoring;
- iv. **Using non-concessional resources** (such as from development banks) when possible. This would allow official development assistance (ODA) to be used directly for support of social sectors that may be less suitable for blended finance transactions.

**Figure 7. Opportunities, risks, trade-offs, and preconditions of public-private financing instruments**



Scaling up blended finance may be more challenging in the COVID-era as blended finance deals generally favor low-risk, less-costly projects, which may prove challenging to find due to heightened financial risks from the crisis. Reorienting blended finance to a focus on impact within the context of an INFF can help better position it as an option to support recovery efforts. Blended finance [principles from the Addis Agenda](#), as well as those of the DFI Working Group on Blended Concessional Finance for Private Sector Projects, the [DAC Blended Finance Principles](#) and the shared values that underpin the [Tri Hita Karana Roadmap](#) for Blended Finance, can guide countries in establishing an appropriate environment for blended finance.

In the absence of sufficient domestic capital, international development banks can also play an essential role in providing these instruments, ultimately absorbing risks at the project/investment level. Similarly, policymakers can strengthen capacities by identifying opportunities to access technical assistance, engaging in new and existing peer-to-peer exchange mechanisms, fostering partnerships with relevant international organisations and bilateral programmes.

## 4.4 Step 4: Operationalisation

The final step brings everything together, by formulating a holistic financing strategy that can guide national efforts to mobilize public and private resources for national priorities. The strategy will concisely lay out:

- the financing objectives it seeks to achieve (as developed in Step 1);
- how existing financing policies and instruments can be brought together (based on the assessment of current practices and initiatives in Step 2); and
- the reforms, new policies and instruments needed to complement them (as prioritized in Step 3).

The strategy will provide direction for the systemic changes and reforms that are needed over time. To this end, it should also include a list or table of actions to be undertaken ranging from short term operational actions to long term planning activities. The actions should align with the objectives outlined in Step 1, which address the opportunities, risks and constraints identified in Building Block 1 “Assessment and Diagnostics”. Table 5 below provides a template for policymakers to populate,

including several key considerations for operationalising the chosen policy actions.

A periodic review and updating of this table can be incorporated directly into the integrated financing strategy process (for example every two years), as part of the responsibilities of the governance entities (see also Building Block 3). Another approach is to have a “living” document, where new actions and next steps are identified over time, enabling the financing strategy to refocus and continuously realign efforts to changes in the global financing landscape, as well as shifting policy priorities.

Effective governance and coordination, including political leadership, will be key for this undertaking (link to Building Block 4). Equally important, a robust M&E system should include appropriate steps to monitor outputs and direct outcomes associated with integrated financing strategy action plan (see Building Block 3 “Monitoring and Review”). A tracking system, which should feed into an overarching INFF reporting structure, may be needed to monitor the execution of outputs and outcomes of policy actions to ensure that implementation is on track.



TABLE 5.

## TEMPLATE FOR INFF ACTION PLAN

POLICIES	ACTIONS/ ACTIVITIES	TIMEFRAME	SEQUENCING	ROLES AND RESPONSIBILITIES	
				RESPONSIBLE ACTORS	ACTORS TO BE CONSULTED/ INVOLVED
List all policy options identified in the previous steps	List specific actions/ activities that would be required to either implement the policy, or to guide long-term planning (e.g., draft TORs for long-term finance diagnostic)	Indicate timeframe for implementation of specific activities (ST/MT/ LT)	Note considerations around whether activities under the same policy and/or across different policies would need to be implemented in a particular sequence (e.g., 'A' needs to happen before 'B' can be implemented)	List lead actors/ agencies – those responsible for the implementation of the activity	List actors/ agencies that would need to be consulted/ involved in the implementation of the activity but that would not be accountable for its success
<i>Template to be filled in...</i>					

## BOX 6.

## FINANCING STRATEGIES IN FRAGILE CONTEXTS: SIERRA LEONE

Sierra Leone was one of the first countries to adopt the integrated national financing framework concept and adapt it to the national context and institutions. Sierra Leone started exploring the potential for an INFF in late 2018 as part of developing its 2019-2023 Medium-Term National Development Plan (MTNDP) and the subsequent development of the national Roadmap for Walking out of Fragility. Sierra Leone's context is characterised by the legacy of earlier conflict, and the country had recently been through the Ebola epidemic from 2014-2016.

The Sierra Leone example identified how features such as weak institutions, unstable political regimes, low state legitimacy, and conflict, which may be amplified by natural disasters or epidemics, often constrain the financing options more than economic factors do. Pre-COVID, financing sources were already low, which has been exacerbated by the pandemic. Once the recovery is underway, restoring and further enhancing finance access is even more critical than before.



Evidence from Sierra Leone underlined several lessons in such contexts:

- **Risk tolerance:** evidence suggests that policymakers and donors need to accept a more flexible macroeconomic framework, as financing options are highly constrained;
- **Quick and strategic:** taking immediate/short-term reform steps can address pressing needs and build momentum. This approach needs to be tied into a medium-term strategy of sequenced reform measures;
- **Political commitment and international support:** financing policy reform efforts require strong political commitment supported by international partners. It is imperative to increase development finance expertise on the ground, including through the United Nations;
- **Contingency financing options:** need to be included in all financing plans for inevitable natural or conflict related shocks, and to provide a buffer should new opportunities arise;
- **Phasing:** need to phase in and sequence the development financing mix over time, for example by planning for the gradual decrease of official development assistance, as domestic resource mobilization improves and private sector investment grows.

## 5. Lessons learned

Several countries have drafted financing strategies to go along with their national development plans, albeit few have ventured to do so in the integrated manner proposed above. The following key lessons emerge from country-level experience:

- The need to place the policy formulation process within broader strategic processes (e.g., align financing strategies with national development plan cycles) to ensure that the exercise responds to practical needs of domestic policymakers and to facilitate legitimization and uptake of its results (Step 1);
- Build support at the highest level of government, complemented by leadership at a senior technical level (political backing combined with technical expertise);
- In identifying options, national authorities should always consider whether solutions are technically correct (i.e., they address the objective identified) and administratively and politically feasible in a given context (Step 2);
- Engage inclusively with the legislature, the private sector, civil society, development partners, and other relevant stakeholders, ensuring a broad-based buy-in throughout the process;
- Take a gradual, targeted and adaptive approach to ensure effective prioritization of policy actions and responsiveness to feedback and changing circumstances;
- Going forward, an integrated approach to financing is key to build resilience and

achieve the SDGs. A financing strategy will help identify all options and support the required prioritization of financing policy actions that best respond to needs and constraints while not losing track of the national (sustainability) goals;

- The need to phase in and sequence the development financing mix over time, for example, by planning for the gradual decrease of official development assistance,

as domestic resource mobilization improves and private sector investment grows (Step 3);

- Governance and coordination key for successful undertaking (link to building block 4). Need successful leadership while also creating incentives for horizontal and vertical integration and allowing for multi-stakeholder participation.



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