STATEMENT BY DR. CARLOS CORREA, EXECUTIVE DIRECTOR OF THE SOUTH CENTRE, TO THE MINISTERS AND GOVERNORS MEETING OF THE INTERGOVERNMENTAL GROUP OF TWENTY-FOUR (G24)

April 2022, Virtual Meeting

1. The lingering COVID-19 pandemic, monetary tightening and increasing geopolitical tension have slowed down the global economic recovery. Projections for the 2022 global GDP growth have been slashed by about one percentage point by major international institutions. Together with inflation, especially spikes in food and fuel prices, and ongoing supply chain disruptions, uncertainty and fragility are looming over the two-speed world economic recovery. This has dimmed the hope to halt or reverse the trend of the rapidly increasing number of people falling into extreme poverty and suffering from hunger. While the COVID-19 virus continues to mutate, the access to vaccination continues to be a major world concern. Developing countries' supply and financing constraints for vaccines and critical medical products must be addressed.

2. Developing countries are facing multiple challenges. The tremendous cost of the pandemic response and the pandemic induced collapse of government revenue have diminished massively the fiscal spaces in developing countries. Therefore, they had no capacity to mount meaningful stimulus packages to spur economic growth which is the main driver of tax revenues, the primary and most reliable source of domestic public resource mobilization. Spillovers of monetary tightening in advanced countries have been less benign to emerging markets and vulnerable countries. Some have already suffered from large depreciation pressure on their currencies relative to international reserve currencies. This is especially so for countries with a high debt level, big foreign exchange exposures and weak current account positions. Increasing interest rates in major developed countries carries risks of potential capital reversal from developing countries. History suggests that capital would swiftly leave poorer countries for higher returns with less risk in richer countries. Capital outflow would further decrease the already limited financing for developing countries. The fiscal and financing divides between developed and developing countries have been the main

causes for the two-speed global economic recovery, a situation which deserves international attention and requires international cooperation to support the vulnerable countries.

3. Currently, unsustainable debt is still a largely overlooked but emerging crisis for the world economy. The debt service burden of developing countries has increased by a wide margin owing to the escalating debt burden and the increasing cost of debt servicing as a result of monetary tightening in major developed countries and the stronger dollar. For countries with high levels of foreign-currency-denominated debt, some are experiencing currency depreciation. This is a dangerous trend as it can lead to currency mismatch in their debt, depleting international reserves and this could trigger a debt crisis. Several developing countries defaulted on their debts in 2021 and a few more countries are on the verge of defaulting right now and have requested for IMF support. It is expected that in the coming months, around a dozen developing economies could prove unable to service their debt. Debt-service burdens in middle-income countries were at 30-year highs. About 60% of LDCs and other low-income countries are now assessed to be in debt distress or at high risk of debt distress. This more than doubled the numbers in 2015. Recently, in assessing the debt vulnerability of developing countries, the World Bank stated that the debt problem facing many developing countries is not a liquidity issue but a solvency crisis.

4. The existing international debt mechanism is not up to the task for debt crisis resolution. The G20 Common Framework is welcome but it primarily envisions debt relief in the form of maturity extensions and interest rate reductions rather than face value reductions. Besides, the Framework lacks inclusiveness as it covers only DSSI low-income countries, thus middle-income income and other countries suffering from unsustainable debt problems cannot seek support under the Common Framework. At present, the framework does not have a clear methodology for comparability treatment of private debt. The framework has neither carrot to provide incentive nor stick to oblige the private sector to participate in debt restructuring. So far, only three countries have applied to the Common Framework and the debt workout progress seems to be slow. The G20 Common Framework needs to be revamped to deliver more quickly on debt restructuring. Work on an international debt workout mechanism has been shelved for decades on the pretext that the current available instruments are sufficient, even if they have been proved otherwise. Therefore, efforts should be made on building international consensus on such a mechanism to allow debt relief and restructuring in a more timely, orderly and fair manner and allow countries to return to the path of debt sustainability and economic growth.

5. For the widening financing gap for developing countries, in the short term, it is necessary to reduce borrowing cost through better policy coordination and avoid aggressive and fast interest rate hikes to smooth financial volatility and avoid triggering strong spillover. Increasing liquidity provision is required, in particular more concessional lending and grants should be made available for the foreseeable future for many low-income economies that have been hit hard by the pandemic and have little fiscal policy space.

6. The simplistic way of determining debt relief by multilateral financial institutions based on per capita income of countries during the pandemic demonstrates the need of a multidimensional vulnerability index to more objectively assess the need of concessional and emergency financing and other international support. It is hoped that such an index will be developed soon.

7. Rechanneling of the unused newly issued $650 billion SDRs should happen faster, at least it could provide buffer to countries with depleting foreign exchange reserves. IMF quota system should continue to be reformed to reflect the increasing weight of the emerging and developing countries in the global economy while protecting the interest of the poor countries.

8. The pandemic has shown once again the need to reform the credit rating agencies whose operation model and bias have led to judgements which have negative impact on the cost, access, and flow of debt financing.

9. Financial digitalization has grown rapidly. Though it opens opportunities, there are also many potential risks including tax avoidance, tax evasion, illicit financial flows, digital fraud and cyber incidents. Yet, appropriate regulatory approaches to address various risks and possible financial stability threats have not been agreed upon by countries. In the process to develop regulatory framework, the interests and capacities of developing countries should be fully taken into consideration.

10. With declining flows of ODA and FDI, developing countries have to rely even more on domestic resource mobilization through taxation. The taxation of the digital economy remains a primary issue in international tax negotiations. The OECD Inclusive Framework's "Two Pillar Solution" offers minimal revenue benefits to developing countries. The 8 October 2021 agreement reflected an outcome that largely benefits the developed countries, as only a small portion (25%) of MNE non-routine profits will be re-allocated to market jurisdictions, which are expected to be largely developing countries. The administration of this system is also expected to be exceedingly difficult, given the complexity of the rules. Of particular importance are revenue impacts, of especially Pillar One, which should be

contrasted with revenues obtainable from alternatives such as Article 12B of the UN Model Tax Convention.

11. Four Global South countries – Nigeria, Kenya, Pakistan and Sri Lanka – have outrightly refused the “Two Pillar Solution”. Many countries, including half of Africa, are not even members of the Inclusive Framework. Thus, the deal is far from global and developing countries have a wide range of tax policy options available to them for taxing the digitalized economy apart from Pillar One. The South Centre joins ranks with fellow Global South organizations like ATAF in supporting developing countries who reject the deal and opt for alternative solutions. The sovereign rights of these countries to tax MNEs as they see fit must be respected. The use of unilateral coercive measures to limit those rights - such as the US Special 301 - must be unambiguously condemned.

12. The UN Tax Committee continues to provide international tax standards, some of which are more beneficial to developing countries than those being now proposed. As sought by its developing country members, the Committee should take up various issues of relevance to the Global South, such as international shipping, computer software, taxing income from property purchased using illicit financial flows, an improved version of the Subject to Tax Rule to end double non-taxation in tax treaties and improved mechanisms for resolving disputes relating to the taxation of the digital economy.

13. Finally, it is widely recognized that the climate crisis is one of the most relevant challenges of our time. According to the latest IPCC reports we are running faster to overshoot the global warming of 1.5°C in the next 20 years or before. This is more than figures. This means more melting of ice, higher sea levels, more heatwaves, droughts and other types of extreme weather conditions, and greater impacts on food security, health, the environment, and sustainable development. Those places that occasionally suffered extreme weather conditions in the past would likely witness more frequent droughts, disastrous flooding, wildfires, heatwaves, and other climate change-related disasters in the years to come. All these extreme weather events have triggered significant displacement of people around the world and have severely affected vulnerable people on the move. In this context, climate finance is crucial to help developing countries implement their Nationally Determined Contributions. That makes it extremely important that developed countries fulfil their commitments to provide U$ 100 billion per year by 2024, which so far has not been fulfilled. It is also important for technical works in the Standing Committee on Finance of the UNFCCC to work on a clear operational definition of climate finance which can be useful to

better inform developing countries about the financial tools available to them in terms of climate finance.

14. A more balanced approach to the allocation of resources for both mitigation and adaptation is required. To date international climate finance has allocated more resources to mitigation. However, adaptation is more relevant for developing countries who suffered already the impacts of extreme weather events without being responsible for the climate crisis. One important issue is that climate finance should not lead developing countries to get more indebted. Several studies have demonstrated that a significant percentage of climate finance is being channelized through loans, in no concessional terms instead of grants, which runs against UNFCCC principles. Finally, it is also highly important that the works related to the development of the New Quantified Collective Goal reflect the actual needs of developing countries for the next 10 years, with full respect to the principles of the UNFCCC and the Paris Agreement.

15. In view of the multiple challenges faced by developing countries as described above, the efforts of G24 in helping to coordinate the positions of developing countries on international monetary and development finance issues remain critical. The South Centre will continue to support those efforts.