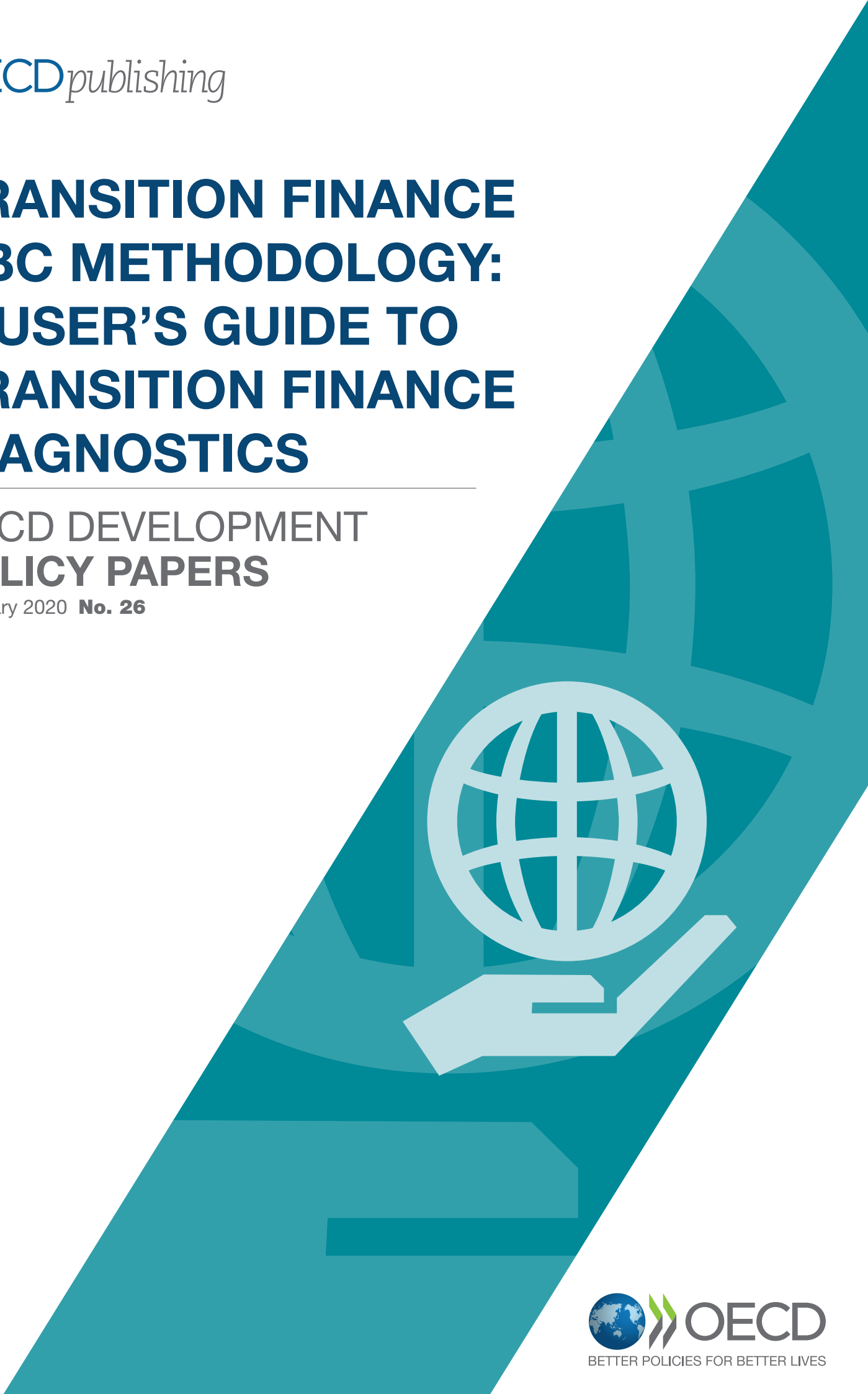
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TRANSITION FINANCE ABC METHODOLOGY: A USER'S GUIDE TO TRANSITION FINANCE DIAGNOSTICS

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Abstract

Transition finance offers a flexible approach for development partners to respond to the changing financial needs of developing countries undergoing transition. The transition finance ABC methodology, part of the transition finance toolkit, provides methodological guidance, metrics, data references and analytical interpretation for users to conduct transition finance diagnostics and country studies.

The paper is organised along the sections: assessing, benchmarking and counselling. The first section, assessment, outlines an economic and socio-political mapping of the country and helps to identify the specific transition a country is undergoing. Benchmarking, section two, helps to form country peer groups and contrast development finance to these countries. Building on the analytical results from the first two sections, the last section on counselling gives exemplary policy guidance to respond to the observed transition challenges.

Acknowledgements

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Background

In its 2017 High-Level Meeting (HLM) Communiqué, the Development Assistance Committee (DAC) set an objective "to better understand the broad catalytic effect of official support and other resources" and to recognise "the interlinkages among ODA, partner countries' domestic resources, private investment, remittances, philanthropy, trade finance and export credits, and other sources of finance (para 15)."

Responding to this call, the OECD has developed a new work stream on transition finance, which explores how countries' access to diverse sources of financing evolves as they *transition* through different development stages. This work stream first focused on developing and introducing the concept of transition finance, describing analytical methods and producing pilot studies in a number of countries deemed representative of a diverse set of transition finance challenges.

The current paper extends the existing work on transition finance by providing operational guidance and compelling evidence on how to implement a transition finance approach. The paper follows a three-pronged methodology (the ABC methodology for transition finance) that allows to Assess, Benchmark and Counsel transitioning countries and development partners, with a focus on deriving specific recommendations for DAC members and partner countries and informing the work of other development stakeholders.

Introduction

What is transition finance?

The OECD Development Co-operation Directorate defines transition as the journey towards sustainable development, and transition finance as the financing of that journey (Piemonte et al., 2019[1]). Although development is often associated with a move towards higher levels of income, the transition finance approach recognises that development is rarely a linear process, and that countries' financing needs and ability to access different financing sources are continually evolving as they transition through different development stages.

Transition finance posits the need to be adaptive and forward looking in order to leverage all available financing opportunities. This entails moving beyond financing strategies based exclusively on historic or current trends: achieving the targets established in the 2030 Agenda will require responsive and realistic financing strategies that allow countries to optimise their access to different financing sources. In the complex and changing landscape of financing for sustainable development, there is also an urgent need to ensure coherence and co-ordination of all the contributions to country financing strategies (OECD, 2018[2]). Transition finance thus takes a holistic approach to development finance, looking at all available sources of financing for sustainable development, and exploring their interactions.

Why is it important?

With ten years remaining to achieve the Sustainable Development Goals (SDGs), implementation is lagging and the financing gap is still estimated to be in the order of trillions. While an increasing number of financing instruments are available to developing countries, financing for sustainable development is also becoming more complex and difficult for countries to navigate.

Studying transition finance helps to better understand, anticipate, and respond to the financing challenges countries face as they move along the development continuum. Financing sustainable development is context-specific and depends on the levels and dynamics of countries' development. While low-income countries tend to rely more on official development assistance (ODA), countries attract more

private financing and are better able to mobilise domestic resources as they progress through the development continuum. The shifts and adjustments between the various flows, however, do not always happen smoothly, and can cause financing gaps in particular sectors or country settings. Failing to adapt countries' financing strategies to such changes, on the other hand, can lead to stagnation or regress of earlier development successes.

What is in the transition finance ABC methodology?

The ABC methodology provides a guiding framework to conduct transition finance diagnostics and implement a transition finance approach. It includes operational guidance to assess and benchmark country contexts, and design specific strategies to maximise the development footprint of the different financing sources. The methodology does not intend to provide a comprehensive assessment of a country's development context. Instead, it focuses on key elements relevant for transition finance, and pinpoints areas that warrant more in-depth research.

The paper is organised into three chapters. Chapter 1 focuses on the assessment of the transition context. It introduces key relevant economic and socio-political indicators and examines the nature and implications of the key transition stages. It also highlights differences in financing for sustainable development market structure and financing mix across countries. Chapter 2 focuses on benchmarking, helping to identify countries with similar structural characteristics and highlighting the opportunities to learn from other countries' experiences. Finally, Chapter 3 concentrates on transition finance strategies, and available policy options and instruments.

All three chapters follow the same structure. Each chapter starts with a presentation of the core questions and discussion points, followed by a description of relevant indicators and analytical insights (citing, where possible, from the existing literature). All chapters end with a link to the corresponding section of the companion interactive dashboard and a list of operational references to further explore particular aspects of transition finance.

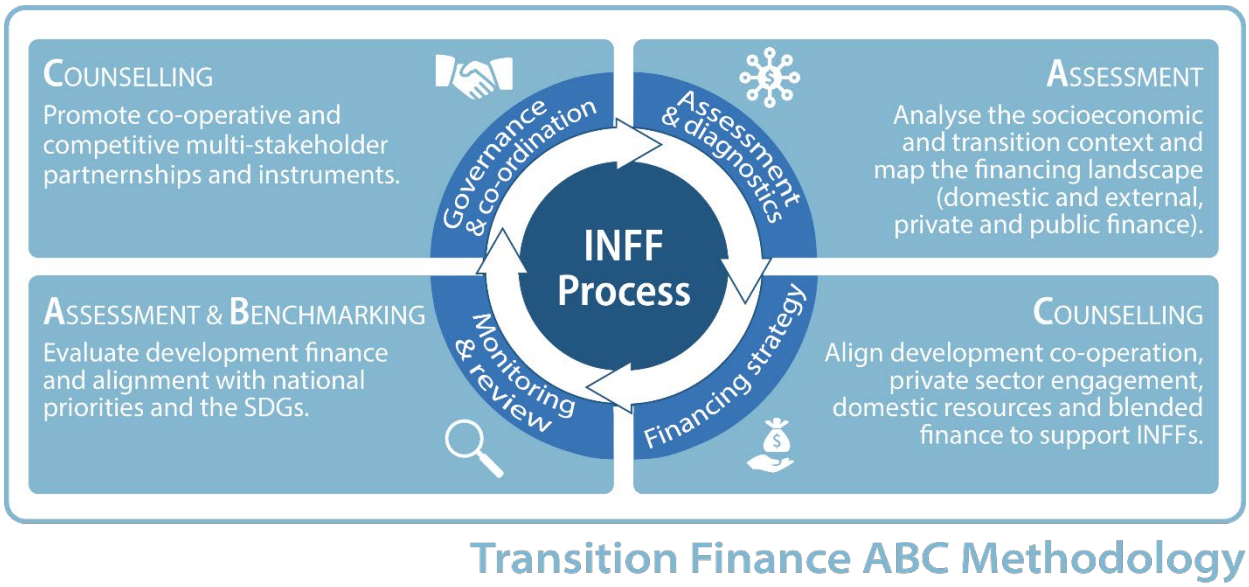
How does the transition finance approach contribute to the 2030 Agenda?

The Addis Ababa Action Agenda (AAAA) called for the mobilisation of a wide range of financing sources and the development of holistic and country-level financing strategies – the Integrated National Financing Frameworks (INFFs) – that define the contributions that each source can make to countries' national development plans. The transition finance approach proposed in the ABC methodology can inform how the DAC and other development partners can best contribute to each INFF process, by promoting an approach that is:

- **Holistic:** considering the contributions from, and the potential of, all financing sources and actors (domestic, external, public, private).
- **Integrated:** taking into account the multitude of stakeholders in the financing for sustainable development landscape and promoting enhanced co-ordination among them.
- **Long-term:** looking at past trends and status, but also obtaining insights from overall trends and trajectories to provide a forward-looking perspective.

The ABC methodology for transition finance contributes to the INFF process by allowing DAC donors, country governments and other development stakeholders to leverage the full potential of the financing available for sustainable development. The ABC methodology can help assess the financing for sustainable development landscape at the national level and support the design and implementation of financing strategies tailored to specific country needs and transition contexts. Figure 1 below shows how the ABC methodology for transition finance superimposes on UNDESA's depiction of the INFF process.

Figure 1. Transition finance and Integrated National Financing Frameworks (INFF)



Source: Authors' illustration.

Table of contents

Transition Finance ABC Methodology 2

A - Assessing 11
A1 – Understanding the economic and socio-political setting 13
A2 – Examining the transition context and its implications 16
A3 – Analysing the financing mix 19

B - Benchmarking 26
B1 – Identifying peer countries in the transition finance landscape 28
B2 – Conducting a comparative analysis 29
B3 – Learning from good (and bad) practices 34

C - Counselling 37
C1 – The co-operative approach 39
C2 – The competitive approach 41
C3 – The case for a renewed partnership 44

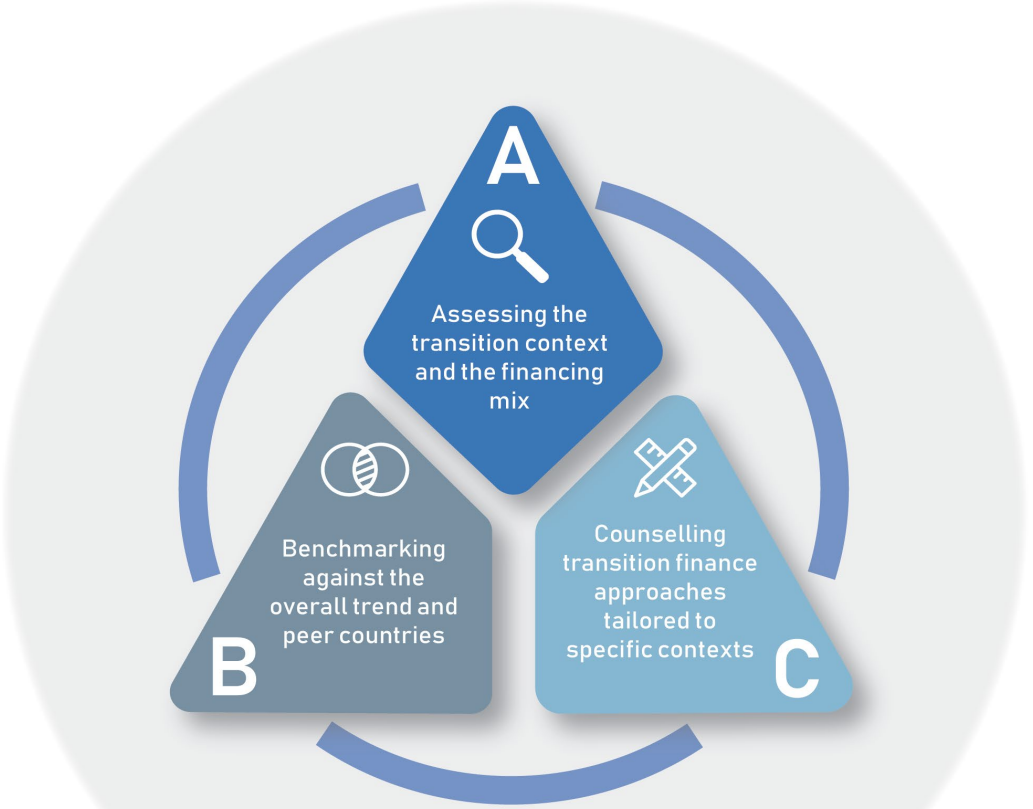
Annexes 47
Glossary 47
References 49

FIGURES

Figure 1. Transition finance and Integrated National Financing Frameworks (INFF) 6
Figure 2. Non-linearity of development: Income level over time for transition finance pilot countries 17
Figure 3. Key transition stages based on income levels 18
Figure 4. Non-income country groups 19
Figure 5. Data criteria for key financing sources 20
Figure 6. Evolution of Zambia's financing mix over time 23
Figure 7. Share of ODA received by Afghanistan for each SDG 25
Figure 8. Key structural factors for the identification of peer countries 28
Figure 9. Framework for the comparative analysis 29
Figure 10. Comparative analysis of Zambia's external financing sources 30
Figure 11. Access to ODA and private financial flows (SIDS vs all countries) 31
Figure 12. Chile's and Uruguay's external financing and tax revenue 32
Figure 13. Financing gaps and surpluses across sectors in Zambia 33
Figure 14. Korea: an impressive success story 35

ABC Methodology for Transition Finance

A three-pillared guiding framework for the implementation of transition finance approaches.



Assessing

1. What is the country's socioeconomic setting? What challenges and opportunities does that present?

2. What is the transition context?

3. What is the current financing mix? How do public, private, domestic and international flows interact?

Benchmarking

1. Which countries share common characteristics with the target country?

2. How does the financing mix compare to other countries? How could the substitution effects impact transition?

3. What lessons can be learned from structural and aspirational peers?

Counselling

1. How can development partners minimise the risk of transition setbacks?

2. How can development partners best encourage private investment and private sector development?

3. How can development partners strengthen partnerships and utilise new methods and tools to support the transition?

Acronyms and abbreviations

AAAA	Addis Ababa Action Agenda
ABC	Assessing, Benchmarking, Counselling
ADB	Asian Development Bank
AfDB	African Development Bank
BEPS	Base erosion profit shifting
BOP	Balance of payments
CARI	China Africa Research Initiative
CDP	Committee for Development Policy
CPI	Corruption Perceptions Index
CPIA	Country Policy and Institutional Assessment
CRS	Creditor Reporting System
CSR	Corporate Social Responsibility
DAC	Development Assistance Committee (OECD)
DCD	Development Co-operation Directorate (OECD)
DFA	Development Finance Assessment
DRM	Domestic resource mobilisation
DSA	Debt Sustainability Assessment
EU	European Union
EVI	Economic Vulnerability Index
FDI	Foreign direct investment
FSD	Financing for sustainable development
GDP	Gross domestic product
GNI	Gross national income
GPEDC	Global Partnership for Effective Development Co-operation
GRD	Government Revenue Dataset
HAI	Human Asset Index
HDI	Human Development Index
HIC	High-income country
HIPC	Heavily indebted poor country
IADB	Inter-American Development Bank
IBRD	International Bank for Reconstruction and Development
ICTD	International Centre for Tax and Development
IDA	International Development Association

IDS	International Debt Statistics
IMF	International Monetary Fund
INFF	Integrated National Financing Framework
LDC	Least developed country
LIC	Low-income country
LLDC	Landlocked developing country
LMIC	Lower middle-income country
MDB	Multilateral development bank
ODA	Official development assistance
ODF	Official development finance
OECD	Organisation for Economic Co-operation and Development
OOF	Other official flows
PEFA	Public expenditure and financial accountability
PFM	Public Financial Management
PPP	Public-private partnership
R&D	Research and development
SDG	Sustainable Development Goal
SDSN	Sustainable Development Solutions Network
SIDS	Small island developing state
SME	Small and medium enterprise
VAT	Value-added tax
UMIC	Upper middle-income country
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDESA	United Nations Department of Economic and Social Affairs
UNDP	United Nations Development Programme
UN-OHRLLS	United Nations Office of the High Representative for Least Developed Countries, Landlocked Developing Countries and Small Island Developing States
UNU-WIDER	United Nations University – World Institute for Economic Development Research
USD	United States Dollar
WBG	World Bank Group
WDI	World Development Indicators
WEF	World Economic Forum
WIID	World Income Inequality Database
WTO	World Trade Organisation

A - Assessing

This chapter describes the process and inputs required to conduct country-level assessments on transition finance. It introduces the key indicators and data sources used to analyse the economic and socio-political setting of a given country, and provides guidance to study how these characteristics shape its ability to access various sources of development finance. The methodology also supports the analysis of each country's transition context: it provides a mapping of the key transition stages, their respective implications (administrative, technical, financial and economic) and the role and responsibilities of the main development stakeholders. Finally, the chapter provides pointers to analyse the composition and evolution of the financing mix.

Assessing - Core questions and discussion points:

A1 – Economic and socio-political setting

- What is the country's economic and socio-political setting? How does it affect access to financing for sustainable development?
- What are the country's strengths? Where are the opportunities?
- How does the setting influence the transition strategy?

A2 – Transition context

- What is the transition context in the country? What are the implications?
- How does the national financing strategy align with the SDGs?
- What role are DAC members and other development partners playing in the transition?

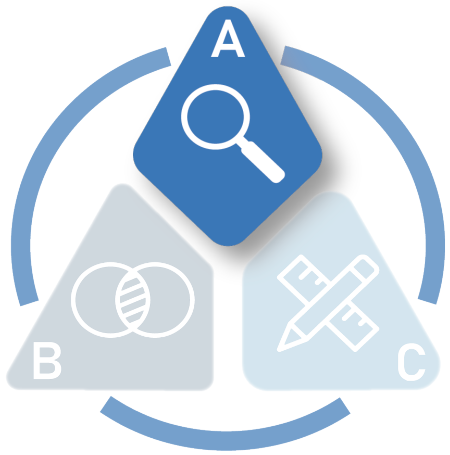
A3 – Financing mix

- What are the characteristics of the financing mix?
- How has access to financing for sustainable development been impacted by the transition?
- What are the substitution effects between public, private, domestic and international resources?

The OECD work on transition finance shows that countries' capacity to access specific financing sources varies according to their level of development and structural characteristics. As a result, the ABC methodology for transition finance starts with an assessment of the country's development context and trajectory, which helps gauge the various challenges and opportunities faced by each country.

The transition finance assessment broadly consists of three steps, which are described and explained in this chapter.

Assessing



A1: Understand the socioeconomic setting of the country.

A2: Position the country within the transition finance continuum to assess its specific challenges and opportunities.

A3: Explore the characteristics of the country's financing mix.

A1 – Understanding the economic and socio-political setting

Economic and socio-political factors play a significant role in shaping the supply and demand for financing in financing for sustainable development markets. These factors influence for example a countries' capacity to mobilise financing sources. The analysis of key economic and socio-political indicators is thus particularly useful to understand a country's structural (exogenous) characteristics and to explain how the country fares in terms of access to sustainable development finance.

This chapter provides examples of key indicators used for transition finance assessments. However, data availability varies significantly from one country to another and the list of indicators presented below is far from exhaustive: users conducting a transition finance assessment in a specific country should base their analysis on all relevant data available, including from country-specific data sources not listed below.

Economic factors

Economic factors of interest for a transition finance assessment may include:

1. Income level;
2. Output and productivity;
3. Debt sustainability;
4. Macroeconomic stability;
5. Balance of payments;
6. Trade;
7. Competitiveness; and
8. Economic vulnerability.

For a rapid assessment of these macroeconomic factors, the following indicators listed in Table 1 are especially useful.

Table 1. List of key economic indicators for transition finance assessments

Indicator	Definition and relevance for transition finance	Data source
Income		
Gross national income (GNI) per capita (Atlas method)	**Definition:** The GNI per capita measures the average income generated by a country's citizens, thus providing an indication on living standards. It is easily available for most countries, and correlated with other non-monetary measures of the quality of life (e.g. life expectancy at birth, school enrolment rates). **Relevance:** Used as a graduation threshold to assess eligibility to ODA, concessional windows from various MDBs, and international support measures. One of three criteria used by UNCDP to determine graduation from the list of LDCs (along with the EVI and the HAI).	WDI (World Bank)
Output and productivity		
Gross domestic product (GDP)	**Definition:** Total monetary value of all the goods and services produced by an economy. **Relevance:** Used as a measurement of a country's overall economic activity, in particular to estimate the size of the economy.	WDI (World Bank)
GDP growth	**Definition:** Reflects change in GDP relative to previous periods. Also available for GDP per capita growth. **Relevance:** Used to assess the health of an economy (contracting or expanding), and thus particularly useful to understand and anticipate countries' development trajectories. GDP growth signals changes in income and can signal changes in overall living conditions.	WDI (World Bank)
Value added by sector	**Definition:** Reflects the total contribution of each economic sector to the overall production of a country. **Relevance:** Provides an indication of the sectoral strengths and weaknesses of each country, including overreliance on certain sectors (e.g. extractive industries). Changes in the sectoral	WDI (World Bank)

	distribution of GDP also reveal important development dynamics (e.g. moving from a large share of agricultural production in GDP to manufacturing or services).	
Debt sustainability[1]		
General government debt	**Definition:** Total government debt as a percentage of GDP. **Relevance:** It is an indicator of an economy's health, particularly for the sustainability of government finance. Large debt levels and debt servicing costs can constrain public expenditure and limit future borrowing.	WEO (IMF)
External debt	**Definition:** Corresponds to the outstanding amount of an economy's debt that is owed to non-residents. **Relevance:** External indebtedness influences a country's creditworthiness as well as investor perceptions. This in turn can alter countries' ability to attract private investments or to raise debt. External debt can be mitigated by a country's capacity to obtain foreign exchange through exports, primary income, and workers' remittances. The currency denomination of external debt is important in case of changes in the exchange rate.	IDS (World Bank)
Macroeconomic stability		
Inflation rate	**Definition:** Percentage change in the nominal cost of acquiring a basket of defined goods and services. **Relevance:** Low and stable inflation reduces uncertainty for consumers, businesses and the government, which in turn encourages investment.	WDI (World Bank)
Real interest rate	**Definition:** Lending interest rate adjusted for inflation. **Relevance:** Real interest rate levels alter the behaviour of economic agents, including investors: e.g. when the real rate of interest is low, income usage moves from saving to consumption, deriving on increased physical investment.	WDI (World Bank)
Exchange rate	**Definition:** Reflects the value of one country's currency in relation to another. **Relevance:** For private investors, currency stability reduces investors' needs to manage exchange-rate risk. For national accounting, currency stability reduces the threat posed by debt issued in foreign currency.	WDI (World Bank)
Balance of payments		
Current account balance	**Definition:** Sum of net exports, primary income (net earnings of foreign investments) and net transfers (including ODA inflows and remittances). **Relevance:** Corresponds to the difference between national savings and investment. A positive current account balance indicates the country is a net lender to the rest of the world, while a negative current account balance indicates that it is a net borrower.	IMF
Financial account balance	**Definition:** Sum of net FDI, portfolio investment, other investment and reserve account. **Relevance:** Indicative of a country's attractiveness to foreign investors. A financial account surplus reflects that more money is flowing into than leaving the country, but also suggests an increase in non-resident ownership of the country's assets.	IMF
Trade		
Trade-to-GDP ratio	**Definition:** Represents the sum of exports and imports measured as a share of gross domestic product. **Relevance:** Indicates the importance of international trade relative to a country's domestic production and signals a country's integration into the world economy. Also often considered as (simple) indicator to proxy a country's trade "openness".	WDI (World Bank)
Competitiveness		
Global Competitiveness Index	**Definition:** Measures competitiveness along 12 pillars: institutions, infrastructure, macroeconomic environment, health and primary education, higher education and training, goods market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication and innovation. **Relevance:** Measures the set of institutions, policies, and factors that set the sustainable current and medium-term levels of economic prosperity.	WEF
Ease of Doing Business Index	**Definition:** Assesses the level of business regulatory performance at the country level. **Relevance:** Empirical evidence has shown that regulatory efficiency and quality is associated with higher economic growth and attractiveness for the private sector.	WDI (World Bank)
Economic vulnerability		

[1] In addition to the indicators presented in Table 1, the assessment should include a review of the country's Debt Sustainability Assessment (DSA). All DSAs are accessible on the IMF website and include information on countries' fiscal deficit, debt service, creditors, debt maturity and debt currency composition.

Economic Vulnerability Index (EVI)	**Definition:** Assesses economic vulnerability based on 8 indicators: population size, remoteness, merchandise export concentration, share of agriculture, forestry and fisheries in the GDP, homelessness owing to natural disasters, instability of agricultural production, instability of exports of goods and services, share of population living in low elevated coastal zone. **Relevance:** One of three criteria used by UNCDP to determine graduation from the list of LDCs (along with the GNI per capita and the HAI). Economic vulnerabilities are important determinants of a country's development trajectory and capacity to access financing.	UNCDP

Socio-political factors

Socio-political factors of interest for transition finance assessments may include:

1. Governance level and institutional quality
2. Human development; and
3. Inclusiveness.

For a rapid assessment of socio-political factors, the following indicators listed in Table 2 are especially useful.

Table 2. List of key socio-political indicators for transition finance assessments

Indicator	Definition and relevance for transition finance	Data source
Governance and institutional quality		
CPIA (Country Policy and Institutional Assessment)	**Definition:** Rating of countries against a set of 16 criteria grouped in four clusters: economic management, structural policies, policies for social inclusion and equity, and public sector management and institutions. **Relevance:** Used in the aid allocation formula of MDBs to ensure that good performers receive a higher IDA allocation in per capita terms. Reflects the overall institutional environment important in shaping the country's transition trajectory.	WDI (World Bank)
Corruption Perceptions Index (CPI)	**Definition:** Scores countries by their perceived levels of public corruption, as determined by expert assessments and opinion surveys. **Relevance:** Corruption leads to inefficient economic outcomes and constrains long-term foreign and domestic investment by raising transaction costs and uncertainty.	Transparency International
Public Expenditure and Financial Accountability (PEFA)	**Definition:** PEFA provides a standardised assessment of countries' public financial management. **Relevance:** Public financial management determines how effective domestic resources, which are at the centre of development finance, are collected and spent, and is fundamental to ensure transparency and accountability in public expenditure.	PEFA Secretariat
Human development		
Human Asset Index (HAI)	**Definition:** Composite index made up of health and education indicators. **Relevance:** Low levels of human capital are a major structural impediment to sustainable development and is thus one of three criteria used by UNCDP to determine graduation from the list of LDCs (along with the GNI per capita and the EVI).	WDI (World Bank)
Human Development Index (HDI)	**Definition:** Summary measure of 3 key dimensions of human development: a long and healthy life, being knowledgeable and having a decent standard of living. **Relevance:** Emphasises that people and their capabilities should be the ultimate criteria for assessing the development of a country, not economic growth alone.	WDI (World Bank)
Net school enrolment ratio	**Definition:** Net ratio of school age children enrolled to the population of the corresponding age. **Relevance:** Education (human capital) can be an important determinant of a country's long-run development potential. Access to (quality) education is correlated with both income levels and equity in income distribution.	WDI (World Bank)
Maternal mortality ratio	**Definition:** Number of women who die from pregnancy-related causes while pregnant or within 42 days of pregnancy termination per 100,000 live births. **Relevance:** Maternal mortality is negatively correlated with income levels. It is particularly prevalent in poor countries with low levels of investment in health infrastructure and low skilled health workers.	WDI (World Bank)
Inclusiveness		
Gini coefficient	**Definition:** A statistical measure used to provide an indication of income inequality. Ranges between 0 in the case of perfect equality and 1 in the case of perfect inequality. **Relevance:** Empirical evidence shows that income inequality is detrimental to medium-term and	WDI (World Bank)

	sustained economic growth[2].	
Income shares	**Definition:** The share of income held by a certain percentile with respect to all income generated, e.g. the share of total income held by the top 10% of income earners. **Relevance:** This gives a more nuanced understanding of the income distribution than the GINI coefficient (e.g. the Palma ratio) and allows tracking income concentration by income percentiles over time.	WIID (UNU-WIDER)
Poverty headcount ratio at USD 1.90 a day	**Definition:** Percentage of the population living with less than USD 1.90 a day at 2011 international prices. **Relevance:** While this indicator fails to capture the non-monetary dimensions of poverty, it has the advantage of offering a simple way to compare (extreme) poverty levels across countries.	IDS (World Bank)
Unemployment rate	**Definition:** Number of unemployed people as a percentage of the labour force. **Relevance:** High and sustained unemployment tends to indicate serious inefficiencies in resource allocation. Unemployed populations are less able to contribute to national development, domestic consumption and domestic savings.	WDI (World Bank)

In addition to key economic and socio-political factors, the assessment should provide an understanding of a country's main development priorities. Such information can generally be obtained through the country's national development plan. As a complement, country-specific Sustainable Development Goals (SDGs), available from the United Nations' Global SDG Database[3], provide a useful overview of each country's main development goals and targets to 2030. For information related to countries' distance to achieving the SDGs, the UN Sustainable Development Solutions Network's (SDSN) SDG Index and SDG Development Reports offer data updated on a yearly basis. Obtaining an understanding of each country's development priorities is key to ensure alignment of development partners' support, in line with international commitments to foster country ownership (e.g. Paris Declaration 2005[4]).

A2 – Examining the transition context and its implications

This section of the assessment methodology includes an overview of the main transition stages by income group and country features. It also describes the key challenges and opportunities faced by countries as they transition along the development continuum.

The transition finance approach shows that the financing mix available to countries varies according to their level of development. At early stages of their development, countries are typically less able to attract private financing and to mobilise sufficient domestic revenue, and thus rely mostly on foreign aid (Piemonte et al., 2019[1]). As they transition throughout the development continuum, they become more attractive for private investment, and improve their capacity to mobilise domestic resources.

During their transition, countries lose eligibility to specific support measures and instruments, which can impact the level of financing they are able to access. Terms at which they can access loans from bilateral and multilateral institutions also become less favourable. This requires countries to carefully plan for the impact of transition in order to preclude negative repercussions on the country as a whole or on specific sectors of the economy and population.

On the other hand, transition and graduation can also have a signalling effect with positive repercussions on financing for sustainable development. Benefits of transition include positive views

[2] OECD (2014[67]), https://www.oecd.org/social/Focus-Inequality-and-Growth-2014.pdf

[3] The UN Global SDG Database is available at: https://unstats.un.org/sdgs/indicators/database/

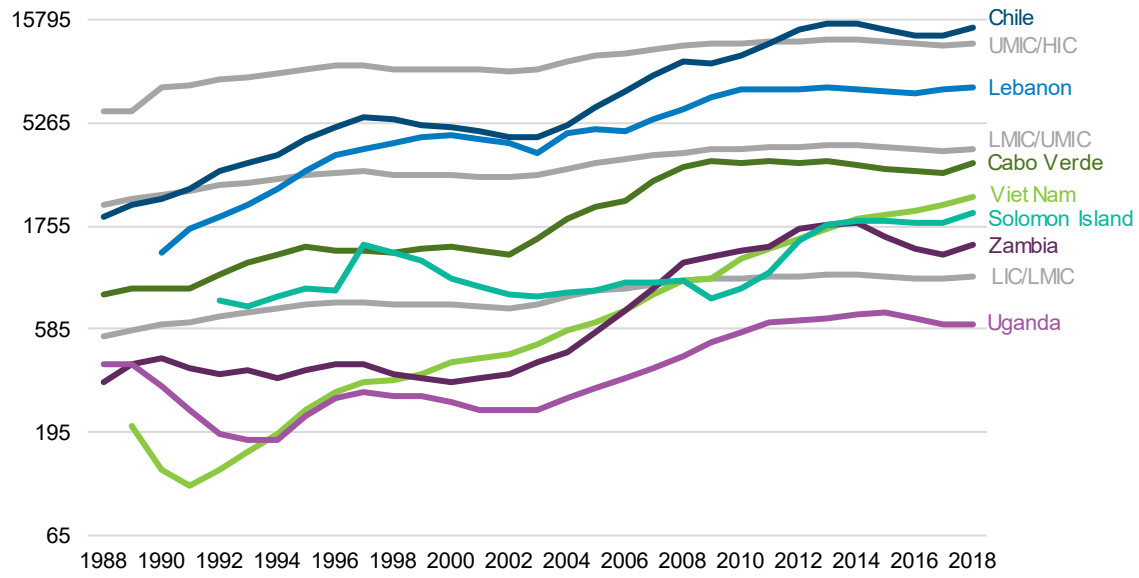
[4] Paris Declaration on Aid Effectiveness, https://www.oecd.org/dac/effectiveness/34428351.pdf

and changes in perception by international financers and investors, potentially leading to increased access to international private sector finance.

Transition is a complex process that does not always imply a linear move towards higher levels of income. As shown in Figure 2 below, development trajectories can vary significantly and it is not rare for countries to stagnate or regress due to vulnerabilities to external shocks or poor economic policy. This reinforces the need for financing strategies to be adaptive and to adjust to the ever-evolving country context.

Figure 2. Non-linearity of development: Income level over time for transition finance pilot countries

GNI per capita, Atlas method, current USD (logarithmic scale)

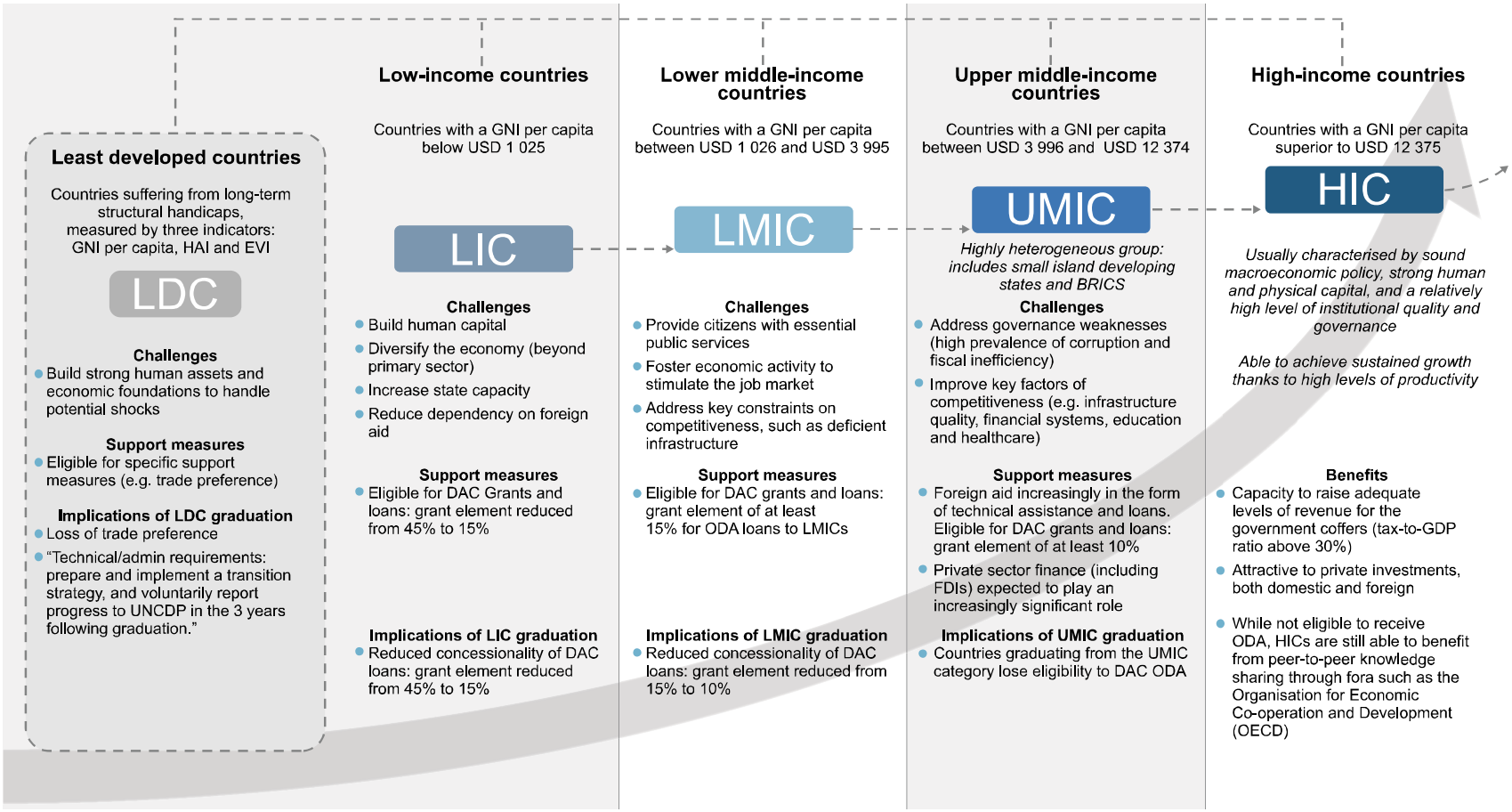


Note: The grey lines represent the evolution of World Bank income level thresholds between 1988 and 2018. The coloured lines represent the income level of the various countries that served as OECD transition finance country pilots.
Source: World Bank (2018[3]), World Development Indicators, Indicator NY.GNP.PCAP.CD, https://data.worldbank.org/indicator/NY.GNP.PCAP.CD and the historical income classification of the World Bank, https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups.

Figure 3 presents a basic overview of the key transition stages. For a comprehensive analysis of the main transition stages and their implications, refer to the transition finance factsheets as part of the online transition finance toolkit[5].

[5] The transition finance toolkit can be accessed under http://www.oecd.org/dac/transition-finance-toolkit/.

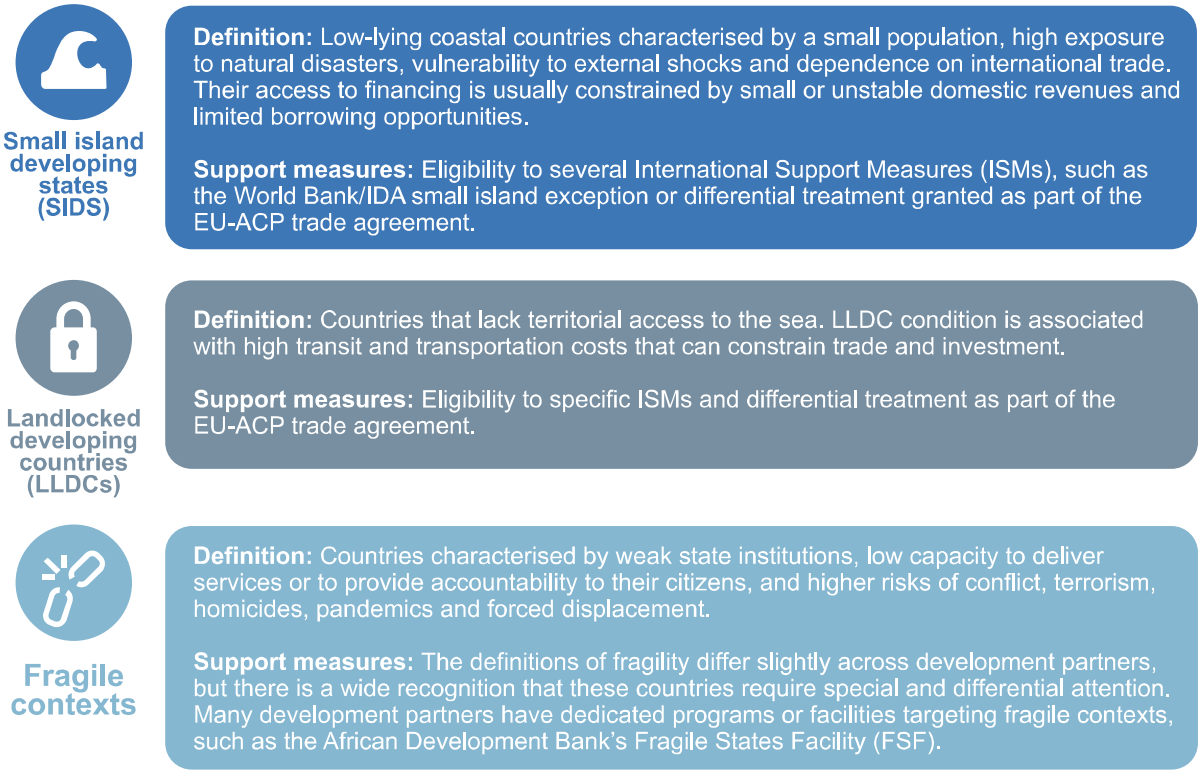
Figure 3. Key transition stages based on income levels



Note: More information is available in the transition finance fact sheets (online at: http://www.oecd.org/dac/transition-finance-toolkit/). The LDC category is not based solely on income level, and includes countries from the following income groups: 28 LICs, 18 LMICs and 1 UMIC.

A number of non-income based country categorisations have emerged over the past few decades, reflecting countries' structural or geographic vulnerabilities that entail distinct transition finance trajectories or challenges (Piemonte et al., 2019[1]). Taking into account these vulnerabilities is particularly important in the context of the Agenda 2030 and the promise made by the international community to "leave no one behind."

Figure 4. Non-income country groups



A3 – Analysing the financing mix

As part of the assessment, the transition finance methodology identifies the main characteristics of a country's financing mix, and studies how transition affects its capacity to access different financing sources. Particularly relevant to the transition finance approach are the exploration of the interaction effects between the various sources.

Description of the financing sources

In line with the holistic approach to development finance promoted by the AAAA, the transition finance methodology looks at all potential sources of financing for sustainable development: public and private, domestic and external (see Table 3 below).

Table 3. Potential sources of finance for sustainable development

	Public	Private
Domestic	Tax Public long-term debt Resource rents and royalties Sovereign wealth funds	Commercial investment Domestic private debt Domestic philanthropy Domestic remittances Impact investing
External	Official development assistance (ODA) Other official flows (OOF) Public long-term debt Public guarantees (external) South-South co-operation Triangular co-operation Climate finance	Foreign direct investment (FDI) External remittances Portfolio equity International market lending International philanthropy Impact investing Corporate Social Responsibility (CSR)

While all of the financing sources listed above are relevant to transition finance, the present methodology focuses on a limited number of variables corresponding to key financing sources that meet the following four criteria:

Figure 5. Data criteria for key financing sources

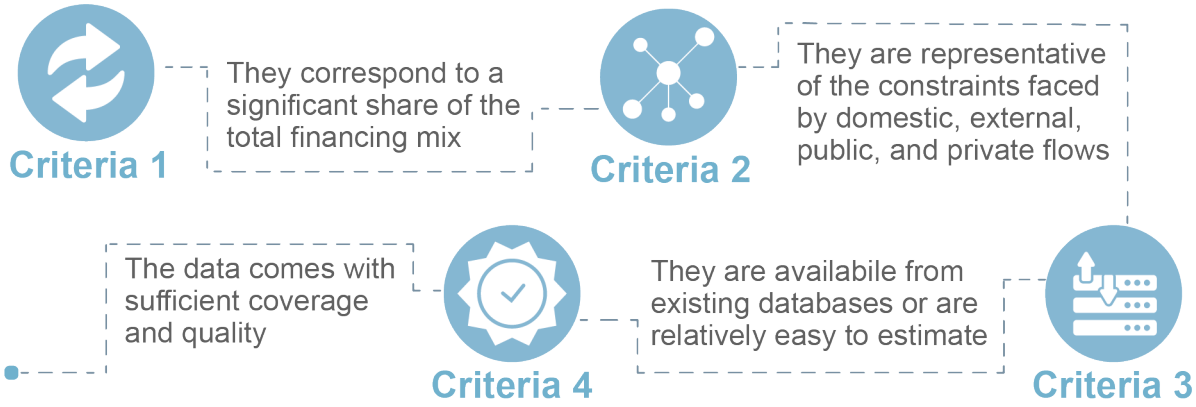


Table 4 below summarises the key variables used to analyse each country's financing mix. It provides a definition, a suggestion on where to access the data, and highlights the relevance of each indicator with regard to the transition finance approach.

Table 4. List of key financing sources used in the transition finance analysis

Variable	Definition and relevance	Data source
	Domestic public finance	
Tax revenue (% GDP)	**Definition:** Share of a country's output that is collected by the government through taxes. **Relevance:** Often regarded as an indication of the government's ability to mobilise domestic resources and be self-sufficient. Among the data sources, GRD provides the largest country sample.	GRD (ICTD/UNU-WIDER) CRS (OECD) WDI (World Bank)
Revenue, excluding grants (% GDP)	**Definition:** Provides a comprehensive representation of government revenue. Includes cash receipts from taxes, social contributions, and other revenues such as fines, fees, rent, and income from property or sales. Grants are excluded. **Relevance:** Particularly relevant for countries that derive a substantive portion of their resources from non-tax revenue (e.g. natural resource rent or fishing licenses in some SIDS).	GRD(ICTD/UNU-WIDER) WDI (World Bank)

Composition of non-grant revenue (%)	**Definition:** The non-grant revenue can be decomposed as direct (personal income taxes, corporate income taxes) and indirect taxes (VAT, excises), resource rent and non-tax revenue. **Relevance:** Disaggregation of the non-grant revenue composition can reveal significant information about the strengths and weaknesses of countries when it comes to mobilising domestic resources. Countries with less developed administrative and fiscal capacity tend to rely more extensively on indirect forms of taxation.	Article IV reports (IMF)
International public finance		
Official development assistance (ODA)	**Definition:** Government assistance designed to promote the economic development and welfare of developing countries. Can take the form of grants and concessional loans; certain criteria on the level of concessionality apply to the latter. **Relevance:** Constitutes a critical resource for the world's poorest countries that are often unable to attract or mobilise sufficient resources to finance their development.	CRS (OECD)
Other official flows (OOF)	**Definition:** Official sector transactions that do not meet official development assistance (ODA) criteria. Include grants to developing countries for representational or essentially commercial purposes; official bilateral transactions intended to promote development, but having a grant element of less than 25%; and, official bilateral transactions, whatever their grant element, that are primarily export-facilitating in purpose. **Relevance:** OOF are a means of assisting countries at rates closer to market terms. OOF tend to progressively substitute ODA as countries achieve higher levels of development.	CRS (OECD)
Official development finance (ODF)	**Definition:** Sum of bilateral ODA, concessional and non-concessional resources from multilateral sources, and bilateral other official flows (OOF) made available for reasons unrelated to trade, in particular loans to refinance debt. ODF figures only include aid provided by donors that report to the OECD DAC. For estimates of aid provided by the People's Republic of China (following "China"), refer to AidData[6] or CARI[7]. **Relevance:** ODF represent a large share of total external resources available to developing countries, in particular for countries considered most vulnerable (LDCs, SIDS, LLDCs, fragile contexts).	CRS (OECD)
Long-term public debt (excl. ODF)	**Definition:** Lending received or guaranteed by the State. For comparisons with other international public flows, subtract ODA and OOF loans from long-term public debt to avoid double counting. **Relevance:** Non-concessional borrowing can be an important source of financing for developing countries, in particular for productive sectors (e.g. infrastructure, industry).	WDI (World Bank) CRS (OECD)
Domestic private finance		
Domestic component of the gross fixed capital formation, private sector (% GDP)	**Definition:** Gross fixed capital formation includes land improvements, plant, machinery and equipment purchases and the construction of roads, railways and schools, offices, industry buildings. The domestic component can be estimated by subtracting FDIs from gross fixed capital formation of the private sector. **Relevance:** Used as a proxy for private domestic investment in physical capital. Capital stock constitutes a key input for economic development.	WDI (World Bank)
Domestic component of the general government debt (% GDP)	**Definition:** Net difference between general government gross debt and long-term public external debt. **Relevance:** Domestic debt issuance generates new financing opportunities and reduces the exposure of borrowers to currency mismatches or external shocks. However, domestic debt overhang can also be costly and expose countries to other risks, such as maturity mismatches.	WDI (World Bank)
Domestic credit provided by financial sector (% GDP)	**Definition:** Includes all credit to various sectors on a gross basis, with the exception of credit to the central government, which is net. **Relevance:** Provides an indication of the strength of a country's financial sector and its contribution to the country's financing needs. Robust financial systems can increase economic activity and welfare.	WDI (World Bank)
International private finance		
Foreign direct investment (FDI) inflows	**Definition:** Refers to long-term capital investment, such as the purchase or construction of machinery, buildings, or manufacturing plants. FDI inflows consist of equity transactions, reinvestment of earnings, and intercompany debt transactions. **Relevance:** FDIs represent the largest source of external funding for developing countries overall. FDI benefits include supplying capital and serving as an important source of growth and productivity, contributing to the creation of value-adding jobs, enhancing the skills base of host economies, providing a source of technology and know-how, and fostering linkages with local firms that can help to integrate them into global value chains.	WDI (World Bank) BOP dataset (IMF)
Portfolio investment, net	**Definition:** Covers transactions in equity securities and debt securities including among others stocks, government bonds, corporate bonds and treasury bills. **Relevance:** Unlike FDI, no significant influence and direct engagement in the firm. Yet, it is a strategic investment that signals investors' expectations over returns and can thus resemble market expectations over the country's development prospects. Foreign portfolio investors generally go for short-term investment to reap the benefits of good economic conditions and they tend to withdraw their investments during the periods of recession.	BOP dataset (IMF)

[6] AidData's Global Chinese Official Finance Dataset, 2000-2014, Version 1.0: https://www.aiddata.org/data/chinese-global-official-finance-dataset

[7] SAIS China Africa Research Initiative: http://www.sais-cari.org/data

Long-term private debt	**Definition:** Corresponds to long-term non-guaranteed obligations from a private debtor with an original maturity greater than one year and repayable in foreign currency. **Relevance:** Access to long-term private debt constitutes an important source of stable funding and an enabler of domestic private sector growth with positive repercussions on countries' productive capacity. Although private nonguaranteed debt is not a contingent liability for governments, large-scale or strategic companies can be deemed 'too big to fail' prompting governments to bail them out.	WDI (World Bank)
Short-term private debt	**Definition:** Corresponds to debt that is maturing within a year, reported net of principal repayments. Interest arrears are also considered to be short-term debt. **Relevance:** A large body of literature associates high levels of short-term debt with a higher occurrence of crises[8]. Short-term debt is generally considered to expose borrowers to rollover risks.	WDI (World Bank)
Remittances	**Definition:** Personal remittances comprise personal transfers between residents and non-residents, and compensation of employees (non-resident employment, non-resident employer entity). **Relevance:** Remittance flows constitute a large source of development finance, ranking only behind FDIs as the largest source of external funding for developing countries. More stable and less pro-cyclical than private capital flows, they are also expected to rise significantly in the long term due to the foreseen increase in international migration.	WDI (World Bank)

Based on the above-mentioned variables, the assessment methodology looks at the composition of the financing mix for each country, and identifies:

- The total level of financing each country is able to mobilise or attract;
- Its level of reliance, or dependency, on each financing source; and
- The specific risks and opportunities posed by each type of financing, and the country's ability to mitigate those.

The goal of this analysis is to study how each country is making use of the various available sources of financing, and managing the associated risks and challenges. The optimal financing mix is the combination of financing sources that maximises a country's financing while minimising the associated risks and challenges.

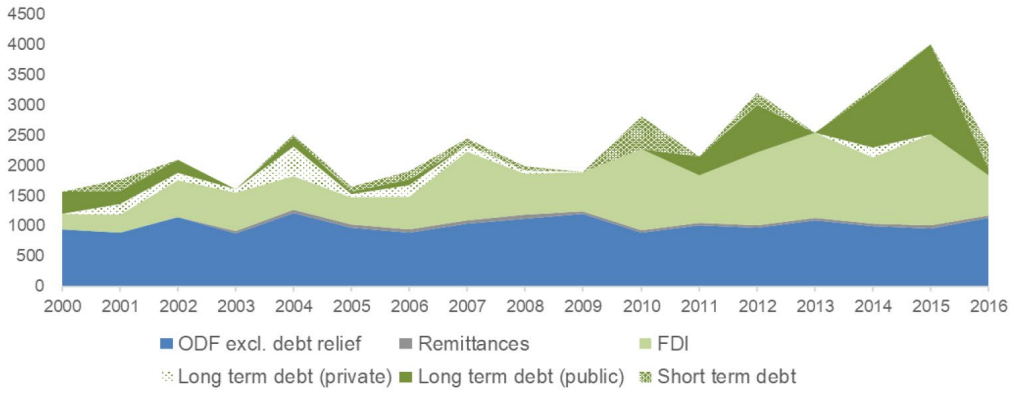
Evolution of the financing mix

To assess and anticipate major shifts in a country's financing mix, the study should also incorporate an analysis of financing trends over time. Figure 1 below represents the variation of Zambia's external financing since 2000. It reveals that the importance of non-commercial debt, in particular official development assistance (ODA), has declined although the amount has stayed stable over time in absolute amounts. On the other hand, the country has experienced a surge in long-term commercial debt and foreign direct investment (FDI). While this evolution is consistent with the pattern observed in countries transitioning towards higher development stages, the surge in commercial debt raises questions regarding the sustainability of the Zambian financing model, which can be easily confirmed by an analysis of the country's debt-related indicators.

[8] See (Brunnermeier, 2009[75]); (Eichengreen and Hausmann, 1999[76]); (Gourinchas and Obstfeld, 2012[77]); (Jeanne, 2009[78]); (Lane and Milesi-Ferretti, 2012[79]); (Rodrik and Velasco, 1999[80]); (Rose and Spiegel, 2011[81]); and (Tirole, 2003[82]).

Figure 6. Evolution of Zambia's financing mix over time

2016 USD million



Note: Adapted from (Kim et al., 2018[4])
Source: (IMF, 2017[5]), "World Revenue Longitudinal Dataset" https://data.world/imf/world-revenue-longitudinal-dat; (OECD, 2018[6]), "Global Revenue Statistics Database", https://stats.oecd.org/index.aspx?DataSetCode=REV; (OECD, 2018[7]), "Creditor Reporting System" (database), https://stats.oecd.org/Index.aspx?DataSetCode=crs1; (World Bank, 2018[8]), "Migration and Remittances Data", http://www.worldbank.org/en/topic/migrationremittancesdiasporaissues/brief/migration-remittances-data; (IMF, 2017[9]), "Balance of Payments" (database) 2017, http://www.imf.org/external/datamapper/datasets/BOP for private investment data.

Breakdown of the main financing flows by type, sector and geographical allocation

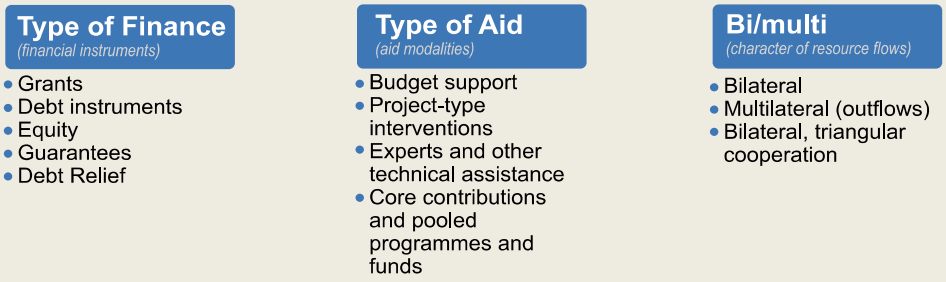
Where appropriate, the analysis should study the composition of the country's major financing flows. Box 1 below provides an illustration based on the decomposition of ODA flows.

Box 1. Disaggregation of ODA flows

The OECD Creditor Reporting System (CRS) database is the internationally recognised source of data on the official development assistance (ODA) and other official flows (OOF) provided by Development Assistance Committee (DAC) member countries and multilateral institutions.

The CRS database provides detailed information on individual aid activities, and has the benefit of offering a high level of disaggregation, allowing for sectoral breakdowns and in-depth analysis of official development finance (ODF) flows.

For the purpose of the transition finance analysis, ODA flows can be broken down by:



Each of these ODA instruments and modalities serves specific purposes and has different monetary and non-monetary impacts on the recipient country. For example, as countries transition towards higher income levels, the relative increase in the share of loans relative to grants (and the reduced concessionality of lending terms) can negatively impact a country's debt sustainability but at the same time foster stronger government ownership.

As part of the transition finance assessment, a review of the sectoral allocation for each financing source and for government expenditure should also be conducted to:

1. Assess alignment with the country's development priorities (as expressed in its national development plan or in its international commitments);
2. Identify financing gaps, both geographical and sectoral.

For some financing sources, such as ODA (OECD CRS), the sectoral allocation is readily available from existing datasets. For others, such as government revenue and expenditure, open budget databases such as BOOST[9] can provide the desired level of granularity although they are not available for all countries.

In order to assess the allocation against the country's SDG targets, some novel methods are now available to the public. For example, the OECD SDG Financing Lab has recently developed a machine learning solution that allows estimating to what specific SDGs foreign aid projects are contributing[10]. While initially developed to track SDG contributions in official development finance, this tool can also be applied to other sources of finance. Figure 7 shows the SDG-related distribution of ODA flows to Afghanistan which reveals that 37% of inflows are targeting SDG 16 on peace, justice and strong institutions.

[9] (World Bank, 2019[68]), "Open Budget Portal", http://boost.worldbank.org/

[10] The SDG Tracker API can be access through the (OECD, 2019[10]), "OECD SDG Financing Lab", https://sdg-financing-lab.oecd.org/

Figure 7. Share of ODA received by Afghanistan for each SDG



Note: The chart provides estimates of the share of ODA received by Afghanistan for each SDG. Estimates are based on the SDG Financing Lab, a deep learning solution developed by the OECD that maps OECD CRS project descriptions to the SDGs.
Source: (OECD, 2019[10]), "SDG Financing Lab", https://sdg-financing-lab.oecd.org/

To learn more: List of operational resources

OECD material:

- Transition Finance Interactive Dashboard: Users can conduct their own assessments using the key metrics presented via the online transition finance dashboard, which offers companion tools to this methodology. The main tabs for assessing are: Overview, Key Indicators, Financing Mix, and Sectors.
- SDG Financing Lab, (OECD, 2019[10])
- States of Fragility 2018, (OECD, 2018[11])

Other material:

- A Guide to Least Developed Country Graduation, (UN-OHRLLS, 2017[12])
- Handbook on the Least Developed Country Category: Third Edition, (UN/DESA, 2018[13])
- LDC Portal (Support Measures Portal for Least Developed Countries), (CDP Secretariat, 2019[14])
- Gradjet web portal, (CDP Secretariat, 2019[15])
- Global Partnership Monitoring on effective development co-operation, (OECD/UNDP, 2019[16])

B - Benchmarking

This chapter provides pointers to identify countries that share similar structural characteristics (peers). The purpose of the benchmarking exercise is to understand how a country fares compared to its peers in terms of capacity to attract finance for sustainable development. It allows exploring how peers addressed key challenges or made use of their comparative advantages. Finally, the methodology also suggests looking at the best practices and lessons learned from other country contexts, in particular to learn from high performers and avoid common pitfalls.

Benchmarking – Core questions and discussion points:

B1 – Transition finance peers

- What are the characteristics to identify transition peers?
- What countries share these characteristics?

B2 – Comparative analysis

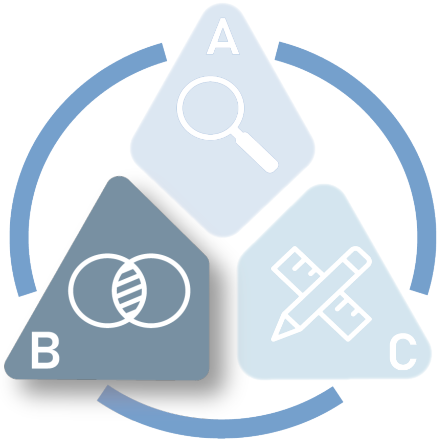
- How does the financing mix compare with that of peer countries? Do my peers fare better or worse in terms of access to financing for sustainable development? Why?
- How does a potential substitution of broader flows compare with country peers undergoing similar transitions?

B3 – Lessons learned

- What lessons and best practices can be drawn from other country contexts?
- What can we learn from outliers?
- What are the traps and pitfalls to avoid?

The objective of the benchmarking exercise is to compare and contrast the target country with its peers. This requires to identify country groups or individual countries that share similar structural characteristics, study the strengths and weaknesses of the target country relative to its peers, analyse potential risks and opportunities associated with transition and gather evidence of good practices that can serve as reference and inspiration.

Benchmarking



1. Determine countries' structural (exogenous) characteristics to identify peer countries with similar features.
2. Identify the strengths and weaknesses of each country relative to its peers, as well as risks and opportunities related to potential substitution effects.
3. Gather evidence of performance among peers that can serve as inspiration and shed light on good practices and pitfalls to avoid.

B1 – Identifying peer countries in the transition finance landscape

The ABC methodology suggests the selection of at least two types of peers to conduct the benchmarking exercise[11]:

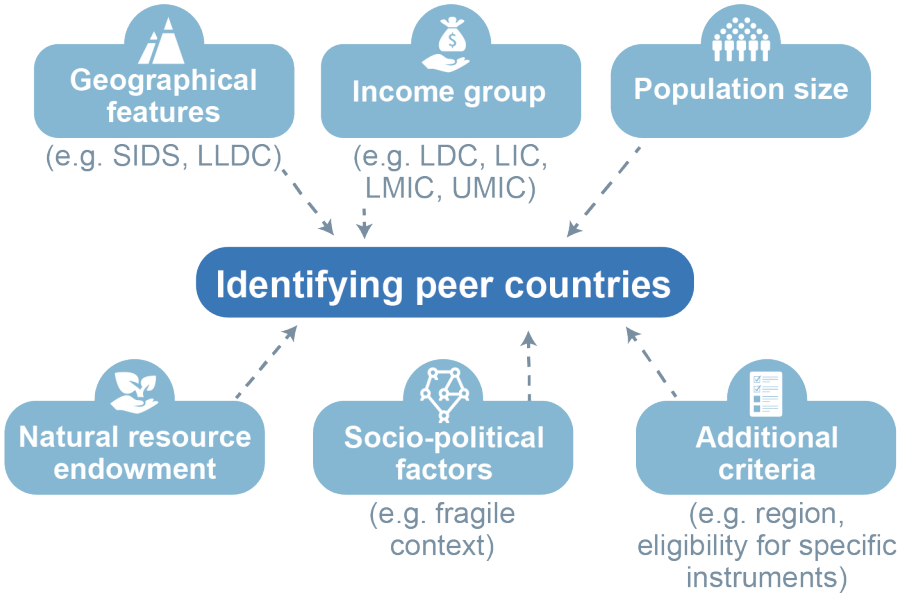
a) **Structural peers:** countries that can serve as comparison for the present transition stage; and

b) **Aspirational peers:** countries that provide a forward-looking, aspirational dimension.

The OECD's work on transition finance highlights that income levels are insufficient to explain differences in countries' transition finance mix. In fact, most outliers in the analysis appear to be resource-rich or have an exceptionally small or large population (Piemonte et al., 2019[1]).The selection of peer countries should thus rely on factors reflecting best the countries' common structural characteristics and vulnerabilities.

Figure 8 below introduces a key set of variables used to identify and cluster countries into peer groups for the transition finance analysis. The transition finance interactive dashboard provides an online tool to facilitate the benchmarking exercise (see link provided at the end of the chapter).

Figure 8. Key structural factors for the identification of peer countries



Previous studies analysing the socioeconomic performance of the country or in the region more generally – for example conducted by the OECD, World Bank, IMF, or UNDP – can provide a useful pre-selection of peer countries. Moreover, countries themselves might have specific peers that they consider as their benchmark or that they look forward to for inspiration.

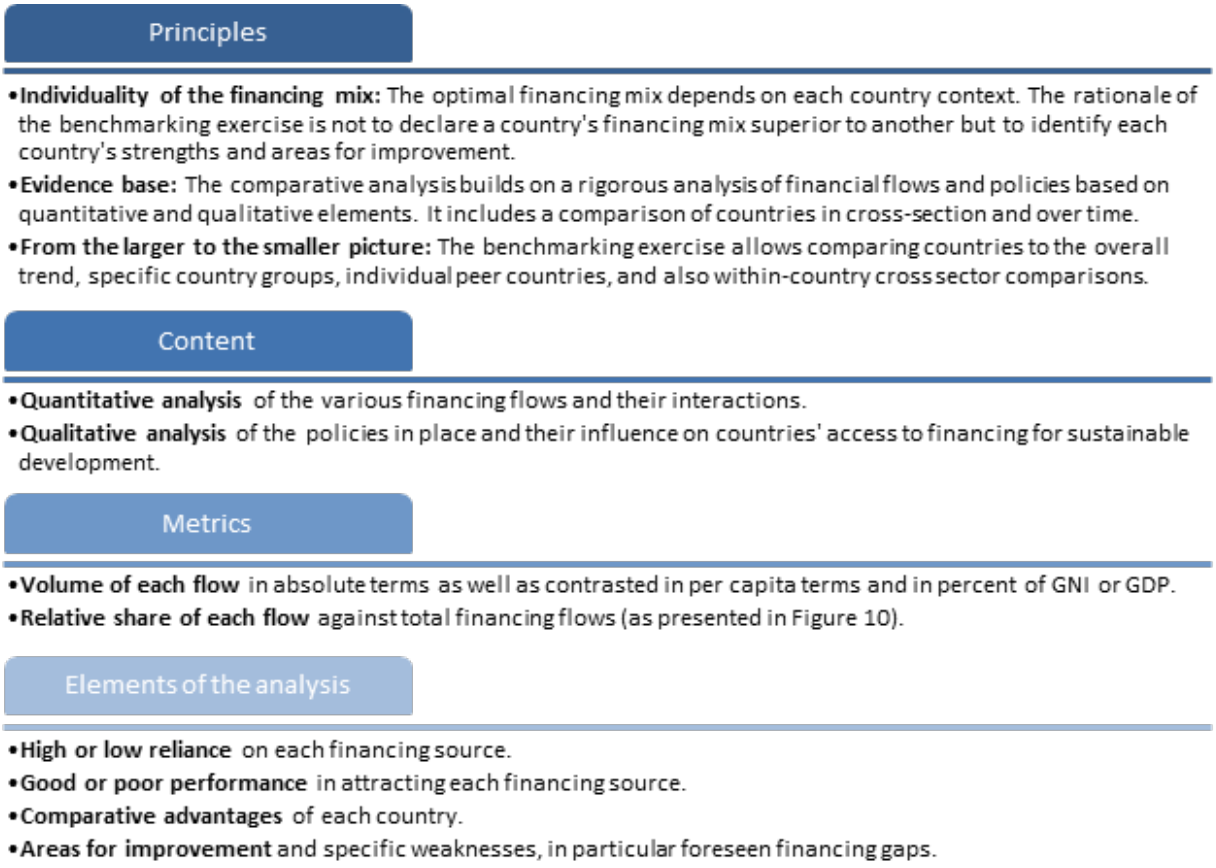
[11] This method follows the approach suggested by (Morris, Cattaneo and Poensgen, 2018[19]), which group benchmarking countries among structural and aspirational peers.

B2 – Conducting a comparative analysis

About the comparative analysis

The comparative analysis aims to shed light on similarities or differences in the country's current financing mix with respect to the overall trend and to its peers. It entails both quantitative and qualitative analysis and seeks to inform on strengths, weaknesses and lessons learned from other contexts. Eventually, it seeks to inform the transition finance counselling (Chapter 3). Figure 9 below presents the main principles, content, metrics and elements of the comparative analysis.

Figure 9. Framework for the comparative analysis



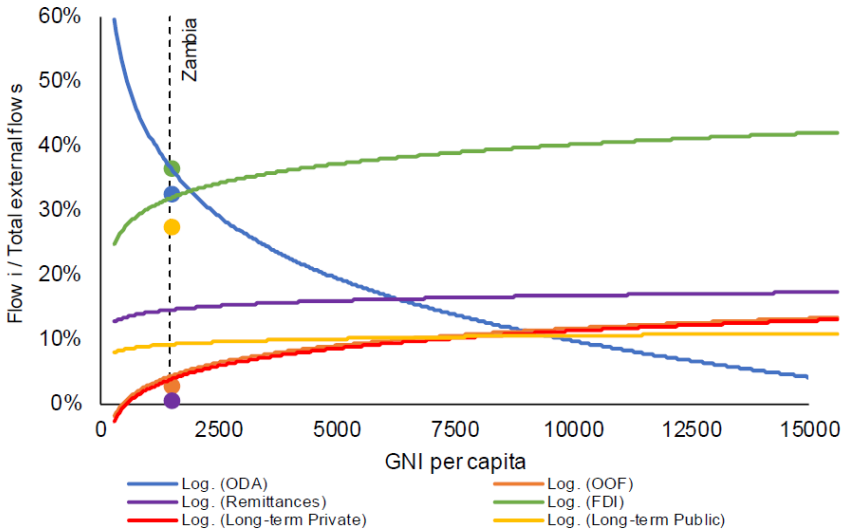
In line with the above-mentioned key principles, the following sections of the chapter present the different steps of the benchmarking exercise from the bigger to the smaller picture, comparing first to the overall trend, then to country groupings and, lastly, contrasting to individual peers and on a sectoral level.

Comparing against the overall trend

Objective: Comparing against the overall trend allows to benchmark financing relative to the country's income level as well as to anticipate changes in the financing mix as countries transition. This analysis enables the identification of countries' relative strengths and weaknesses in terms of access to different types of financing sources compared to the overall trend.

Analysis: Figure 10 below provides an overview of the main trends observed in the interactions of various external sources of financing for sustainable development. The trend lines presented in the graph indicate the general trend of financing available to countries at each level of income. As explained in the assessment section, income per capita remains an important factor to explain countries' access to finance. The lines do not represent the optimal financing levels since the latter depends on the distinct characteristics of each country. However, this methodology provides a useful reference to identify the relative strengths and weaknesses of each country and can provide a visual representation of the substitution effects at play between the different financing sources. The benchmarking conducted for Zambia reveals insightful patterns about the strengths and weaknesses of its financing mix: while the share of ODA and FDI received by the country seems to be close to the overall trend for its income level, the level of remittances is very low, and the country appears to rely heavily on long term public debt, raising concerns about the sustainability of its financing strategy and possible macroeconomic consequences (Figure 10).

Figure 10. Comparative analysis of Zambia's external financing sources



Note: The plotted lines represent predicted values at each GNI per capita level. The predicted values result from a logarithmic regression where the share of flow over total external flows is regressed on the logarithm of GNI per capita. The underlying values are average values for the years 2012-16.
Source: Kim et al. (2018[4]) using OECD (2018[7]), Creditor Reporting System, https://stats.oecd.org/Index.aspx?DataSetCode=crs1

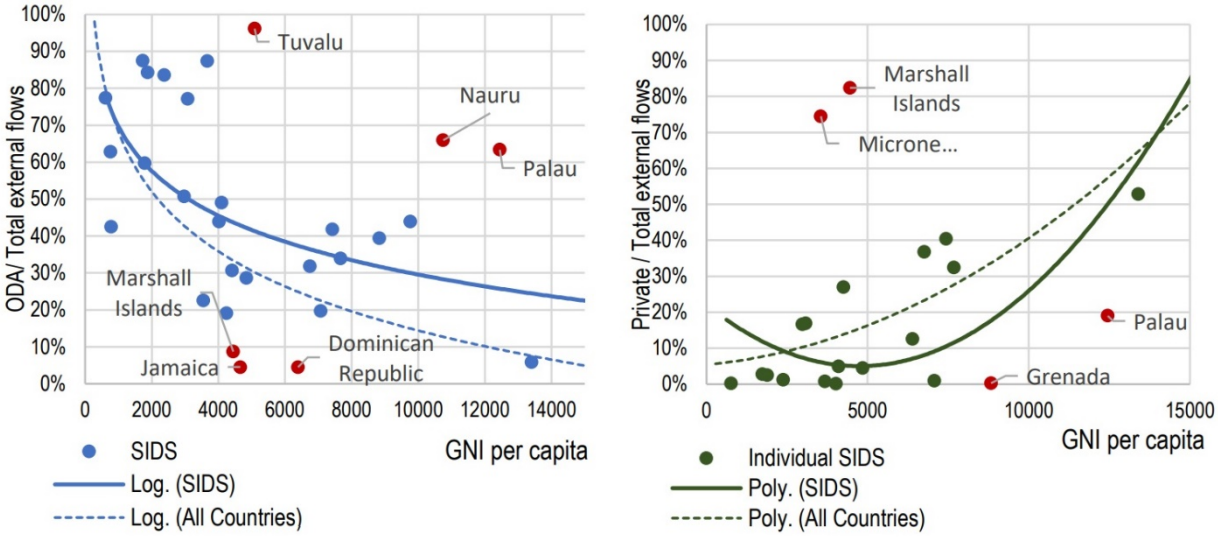
Comparing against relevant country groups

Objective: Comparing a country's financing mix to the trends of specific country groupings can help explain differences in countries' access to the various financing sources. For example, countries facing similar vulnerabilities, such as SIDS, LLDCs and fragile contexts, tend to exhibit singular patterns and trajectories.

Analysis: The financing mix trends introduced before can be tailored to specific country groupings to conduct comparisons with peer countries with similar characteristics. Figure 11 below highlights the different trends observed in terms of reliance on ODA and capacity to attract private investment between the SIDS and the overall trend across the income spectrum. It confirms that SIDS are more dependent than other countries on ODA, and that they struggle more to attract external private finance such as FDI. These graphs also reveal the existence of outliers among the SIDS. For example, the left hand chart shows that the Pacific islands of Tuvalu, Nauru and Palau received a larger share of ODA than the average for SIDS. The right-hand chart shows that some SIDS struggle to attract private finance flows: Palau, for

example, receives a small share of private finance, even for a SIDS with its level of income, whereas a country like the Federated States of Micronesia counts a large share of private finance flows.

Figure 11. Access to ODA and private financial flows (SIDS vs all countries)



Note: The charts illustrate the share of ODA and private flows on total external finance at each stage of development. The solid line corresponds to the trend line of SIDS, the dotted line corresponds to the trend line of all countries, and red data points correspond to outliers.
Source: Piemonte et al. (2019[1]) using OECD (OECD, 2018[7]), Creditor Reporting System database, https://stats.oecd.org/Index.aspx?DataSetCode=crs1.

Benchmarking against relevant country groupings is particularly important since exogenous factors such as natural resource endowment, or geographic characteristic such as small-island status, significantly influence countries' capacity to access various sources of financing for sustainable development. For example, previous OECD work on transition finance (Piemonte et al., 2019[1]) finds that:

- Natural resource endowment (commodities) and market size are key determinants of a country's capacity to attract OOF and private finance, especially FDI;
- Small island developing states (SIDS) are more dependent than other countries on ODA while the share of OOF and private finance is below the common trend at all stages of transition;
- The share of ODA in external flows is higher for LDCs than for other countries while the share of OOF and private sector finance in the financing mix is lower;
- Landlocked developing countries (LLDCs) have difficulty in attracting foreign investments in early stages of transition, the share of remittances in external finance is below the common trend while the share of ODA is only slightly higher;

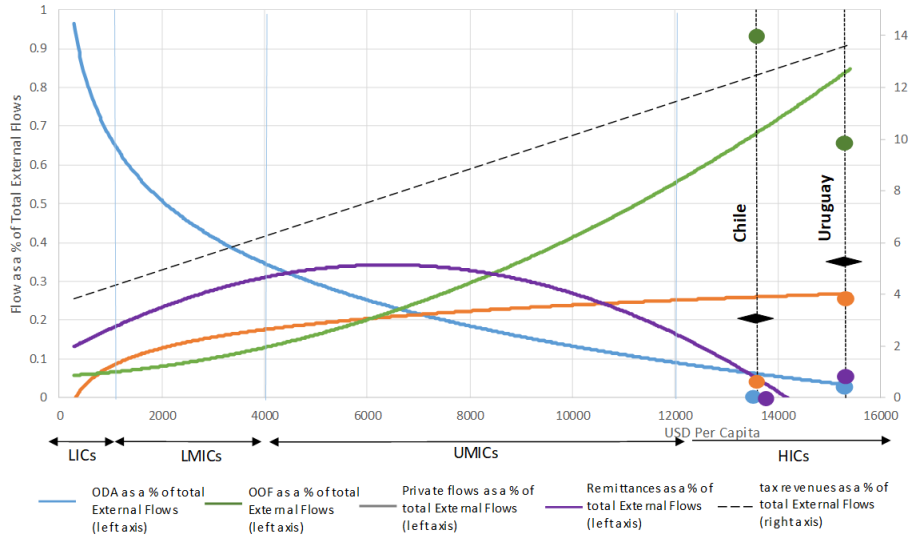
Comparing against individual peers

Objective: Structural peers can provide a useful benchmark to identify a country's relative performance in mobilising or attracting financing, and to understand whether it is more dependent than others on certain sources of finance. Hence, this exercise can help in identifying specific weaknesses relative to peers that need to be addressed by development stakeholders to support a country's journey towards sustainable development. The underlying assumption is that once most structural factors are accounted for, varying

performance in accessing certain sources of financing can be attributed to the specific policies and practices in place in each country.

Analysis: Figure 12 below shows Chile's performance in terms of access to various financing sources compared to Uruguay as well as relative to all developing countries (trend lines). Both countries graduated from the DAC list of ODA recipients in 2017 although their financing mix differs significantly. Both countries receive very low levels of ODA and remittances, but while Chile seems to receive a higher share of private flows (in large part due to foreign investments in its copper mining industry), Uruguay's tax revenues relative to external inflows are higher. Chile's high reliance on external private finance, coupled with its relatively low tax revenues, raises the question of the country's capacity to sustain its financing needs in case of external shocks (e.g. sudden decline in copper prices).

Figure 12. Chile's and Uruguay's external financing and tax revenue



Note: Coloured dots correspond to Chile and Uruguay and should be compared to the respective coloured lines (trend for all ODA recipients).
Source: (Piemonte, Catteneo and Poensgen, Forthcoming[17]) using (OECD, 2018[7]), Creditor Reporting System, https://stats.oecd.org/Index.aspx?DataSetCode=crs1 for ODA and OOF flows; DAC database (private flows); (World Bank, 2018[3]), World Development Indicators, https://datacatalog.worldbank.org/dataset/world-development-indicators for remittances; (ICTD/UNU-WIDER, 2019[18]), Government Revenue Dataset, https://www.wider.unu.edu/project/government-revenue-dataset for tax revenues.

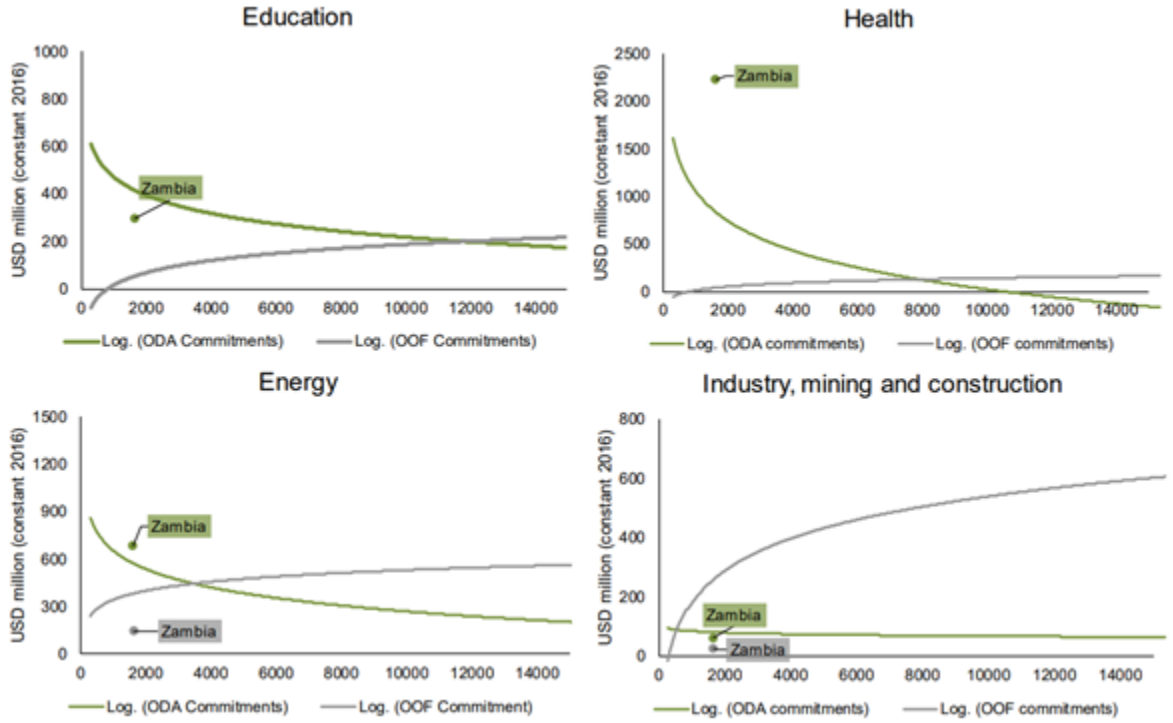
Substitution effects: financing gaps and surpluses

Objective: Along their transition journey, countries simultaneously gain and lose access to different types of resources. Previous work by the OECD on transition finance has highlighted two major trends in this respect: first, a substitution of external with domestic resources; and, second, a substitution of public with private resources. This section aims to investigate the interaction among the various financing sources, and to anticipate when substitution effects and financing gaps (i.e. insufficient substitution of one resource with another as the former declines) are likely to occur.

Analysis: Figure 13 shows that ODA and OOF inflows tend to fluctuate significantly as countries transition through different development stages and that the interaction and substitution of flows is highly dependent on the sector. Social sectors such as health and education, for instance, require special attention since they are particularly prone to funding gaps. The sectoral disaggregation of the official development finance (ODA + OOF) received by Zambia also reveals that the country's sectors face different financing challenges. The Zambian health sector receives large inflows of ODA compared to the average trend (top-right hand chart). On the other hand, some of its productive sectors, such as energy, mining, industry and

construction, clearly fail to attract significant volumes of OOF. Zambia's example illustrates both the challenge of transitioning from concessional to non-concessional financing, and the fact that substitutions may happen at different times across a country's sectors.

Figure 13. Financing gaps and surpluses across sectors in Zambia



Source: Kim et al. (2018[4]) using (OECD, 2018[7]), Creditor Reporting System, https://stats.oecd.org/Index.aspx?DataSetCode=crs1 for ODA and OOF flows; (World Bank, 2018[3]), World Development Indicators, https://datacatalog.worldbank.org/dataset/world-development-indicators for GNI per capita.

This analysis investigates the change in the financing mix on a sectoral level. Previous work by the OECD has identified sector-specific patterns in the interaction of ODA and OOF as countries transition:

- In some sectors the phase-in of OOF exceeds the phase-out of ODA (surplus), in others it matches the reduction in ODA (compensation), and in others the increase in OOF is insufficient to account for the decrease in ODA (gaps).
- Certain categories of countries are particularly exposed to the risk of financing gaps, such as countries exhibiting structural economic vulnerabilities, among them the LDCs, SIDS, LLDCs and fragile contexts.
- Due to data limitations, the analysis of sectoral substitution effects only incorporates flows from official development finance providers. However, it signals to partners the need for other financing resources such as tax revenue or private finance to meet potential financing gaps.

B3 – Learning from good (and bad) practices

Lessons learned from structural peers

The final aim of the benchmarking section is to isolate and identify non-structural factors affecting the performance of each country in terms of access to financing for sustainable development.

Exploring the lessons learned from peer countries can help inform the Counselling section of the transition finance methodology by singling out specific policies and practices that contribute to the strong performance among the considered countries. Equally relevant to the transition finance approach is learning of potential traps and pitfalls to avoid based on other country experiences. Box 2 below provides a lessons learned example taken from the Cabo Verde country pilot.

Box 2. Realising the opportunities of the ocean economy in small island developing states

Cabo Verde and the lessons learned for upgrading fishery value-chains and debt-for-nature swaps

Cabo Verde relies largely on tourism and travel, which account for roughly half of its economic activity[12]. At the same time, the small island developing state that graduated from the LDC category in 2007 and that is classified at "high risk" of debt distress has the potential to better reap the benefits of the ocean economy. The Cabo Verde country pilot (Morris, Cattaneo and Poensgen, 2018[19]) highlights how its peers, the Maldives and the Seychelles, can provide a best practice example to enhance sustainable fishery and protect the environment while restructuring debt.

The Maldives, having graduated from the LDC category in 2011, promotes the blue economy by encouraging environmentally sustainable fishing and fishery production. Relying on a traditional one-by-one fishing technique called “pole and line” and with the certification of the Marine Stewardship Council (MSC) ecolabel for the most important local species, the Maldives promotes its fishery exports as niche, leading to a price mark-up for its fishermen. More so, the country promotes the recovery of the local ecosystem by restricting coral mining and protecting turtles and sharks (UN environment, 2018[20]).

In 2008, the Seychelles defaulted on its debt. Fishery, tourism as well as oil and gas exploration, in the meantime, pose a threat to its rich marine areas. Supported by the US-based conservation group "The Nature Conservancy" and the French government, the Seychelles reached an agreement with its Paris Club creditors to restructure its debt in return for scaling-up protection of its marine areas. The Nature Conservancy bought up nearly USD 22 million of the country's outstanding debt. In exchange, the Seychelles designated a third of its marine area as "protected" area, limiting fishery, oil exploration and large-scale developments. The debt swap also freed up capital that can be directed toward climate change adaptation and other marine conservation activities.

Source: Morris, Cattaneo and Poensgen (2018[19]), Cabo Verde Transition Finance Country Pilot, https://dx.doi.org/10.1787/1affcac6-en

Lessons learned from aspirational peers

In addition to learning from structural peer countries, donors and developing countries can learn from other country contexts, including high performers that have experienced successful transitions. Aspirational

[12] According to World Bank data and the World Travel & Tourism Council (WTTC), the total contribution of tourism and travel to the GDP of Cabo Verde amounted to 44.44% in 2018, up from 7.5% in 1995.

peers do not necessarily share many structural or geographical commonalities with the countries they serve as benchmark for, and should thus not be used to make hasty conclusions or recommendations.

The main value added of the lessons learned from aspirational peers is to provide a forward-looking perspective and a reference of what countries can expect to experience, or aim to achieve, over the long term. Exploring case studies of successful transitions in different contexts can also help countries and development partners challenge local policy assumptions and reveal untapped opportunities, as well as identify policies that proved efficient at optimising countries' financing mix. Box 3 below provides an example of lessons learned from an aspirational peer.

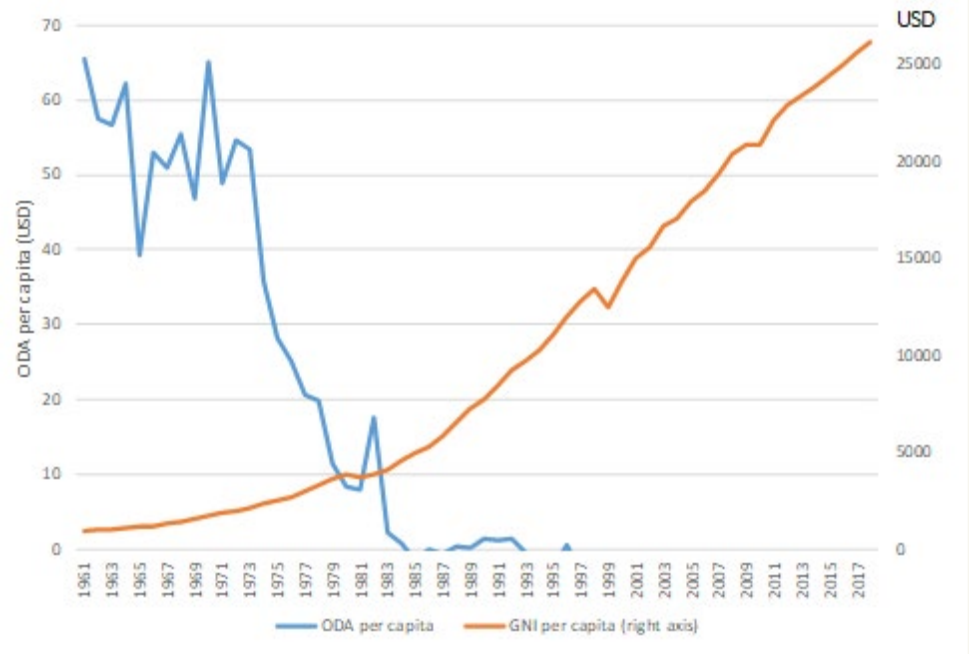
Box 3. Chile and the aspirational case of Korea

Korea became an OECD member in 1996 and a DAC member in 2010. It was removed from the DAC list of ODA recipients in 2000. Figure 14 below shows how its GNI per capita grew from the 1960s onward.

Central to Korea's success story was the high level of innovation the country was able to achieve, mostly through private investment. The country's R&D benefitted from an abundant pool of highly educated workers that could meet the increasing demand in this area arising from the private sector. Korea's case study provides interesting takeaways for ODA-graduating countries such as Chile, when designing public policy to incentivise innovation investments.

Figure 14. Korea: an impressive success story

ODA per capita (constant USD 2017 prices) and GNI per capita, Atlas method, constant 2010 prices



Source: Piemonte, Cattaneo and Poensgen (Forthcoming[17]), Better Mangaging Graduation from ODA Eligibility - A transition Finance Study of Chile, http://www.oecd.org/dac/transition-finance-toolkit/

Chile has multiple initiatives to help people, SMEs and larger firms to invest in R&D. Nevertheless, investments in R&D remain far below the OECD average, at 0.35% of its GNI. If, as highlighted in the Korean case, there is a minimum educational level still not reached by the Chilean society in order to be able to absorb R&D investments, tackling major educational constraints should be a priority to eliminate the bottleneck to R&D transformational investments. This 'educational momentum' could be a source of additional research that the DAC community could help facilitate.

Learning from the Korean experience, DAC members could in particular focus on helping build – together with partner countries that approach HIC levels – a solid education sector. This would help countries absorb massive innovative investments and set up modern, forward-looking economies.

Source: Piemonte, Cattaneo and Poensgen (Forthcoming[17]), Better Mangaging Graduation from ODA Eligibility - A transition Finance Study of Chile, http://www.oecd.org/dac/transition-finance-toolkit/

To learn more: List of operational resources

OECD material:

- Transition Finance Interactive Dashboard: Users can conduct their own benchmarking using the online transition finance dashboard, which offers companion tools to this methodology. The main tabs for benchmarking are: Peers, Benchmarking and Sectors.
- States of Fragility 2018, (OECD, 2018[11])

Other material:

- Global Benchmarking Database (University of Warwick, April 2019[21]), Center for the Study of Globalisation and Regionalisation
- The Vulnerability of Landlocked Developing Countries to External Shocks, (UN-OHRLLS, 2014[22])
- State Fragility and Economic Vulnerability: What is Measured and Why?, (Guillaumont and Guillaumont Jeanneney, 2011[23])
- Assessing the Economic Vulnerability of Small Island Developing States and Least Developed Countries. (Guillaumont, 2010[24])

C - Counselling

This chapter aims to identify available policy options and instruments to address the financing challenges faced by countries in their journey towards the achievement of the SDGs. It aims to support the design of country-specific transition finance strategies by DAC donors and to provide a roadmap for implementation of the transition finance approach. Finally, the chapter also describes the main implementation and co-ordination challenges that call for a renewed partnership, and identifies the main roles and responsibilities of DAC and non-DAC donors.

Counselling – Core questions and discussion points:

C1 – The co-operative approach

- How to leverage socioeconomic progress and avoid financing gaps in social sectors?
- How can development partners use official development finance to reduce the risk of transition setbacks?
- What policy options are available to ensure debt sustainability?

C2 – The competitive approach

- How can partners foster private sector development?
- What can be done to create an enabling environment for private investment?
- How can infrastructure development be enhanced?

C3 – Renewed partnerships

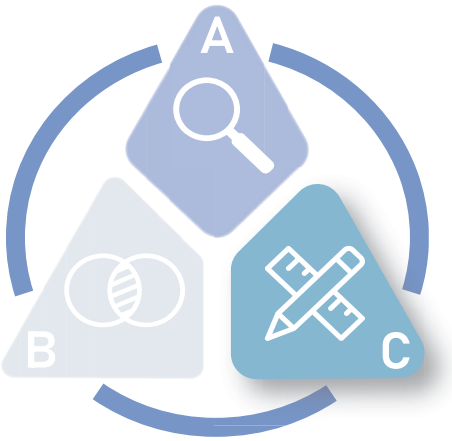
- What co-ordination challenges occur as countries transition?
- How can development partners improve partnerships and use of new instruments?
- When should partners shift their relationship from development to economic partners?

The counselling section seeks to inform development partners on four key areas:

1. Tools, policies and partnerships that help increase the effectiveness of ODA along the development continuum and best serve the financial needs of transitioning countries;
2. Ensuring long-term sustainable financing and debt sustainability by supporting progressive growth of other financing sources while phasing out ODA;
3. Capacity building, promotion of transfers (e.g. private investment, technology and knowledge), and domestic resource mobilisation that can be fostered by ODA in anticipation of transition;
4. Design of long-term support strategies beyond ODA that preserve achievements after countries' graduation from ODA while avoiding development setbacks.

This calls for the implementation of transition finance strategies that combine a co-operative and competitive approach, as well as a call for improving co-ordination and renewing partnerships.

Counselling



Co-operative approach: Ensuring economic progress, avoid development setbacks, strengthen governance and domestic resource mobilisation

Competitive approach: Private sector development and business environment, infrastructure investment, PPPs

Reviving partnerships: co-ordinating with domestic and international actors in the development field

The design of financing strategies that address the transition challenges faced by each country requires a hybrid approach that combines support along the three following dimensions:

1. **Co-operative approach**: supporting the country to achieve socioeconomic progress by building resilience against possible transition setbacks and ensuring that social and economic vulnerabilities are adequately addressed;
2. **Competitive approach**: supporting the country's efforts to achieve sustained economic growth by investing in the economy's competitiveness and increasing its attractiveness to private investment.
3. **Renewed partnership:** promoting enhanced co-ordination and synergies on all aspects of sustainable development finance.

The hybrid approach allows articulating how each financing source can best contribute to the country's development objectives. Each type of financing has specific characteristics, advantages and limitations, which should be taken into account to make the most of the limited resources available to each country. This can in turn improve co-ordination among development partners, allowing each one of them to focus on their value-added.

The policy recommendations emanating from the ABC methodology for transition finance should be realistic and actionable rather than aspirational: they should be developed in light of the country's current economic and socio-political context and be focused on informing a specific decision to ensure that they translate into concrete impact.

The recommendations emanating from the counselling section should also be forward looking. By outlining how countries and development partners can best prepare for, and manage, the transition challenges and opportunities lying ahead at each stage of their development journey, the ABC methodology complements existing diagnostics on development finance, such as UNDP's Development Finance Assessments (DFAs). While DFAs advise country planning, the transition finance approach aims to guide development partners' allocations and co-operation. Both, however, contribute to the INFF process.

C1 – The co-operative approach

The co-operative approach aims at building domestic capacity in social sectors, enhancing domestic resource mobilisation and maintaining debt sustainability. It seeks to build capacities to secure development gains and to promote resilience against possible transition setbacks.

Elements of the co-operative approach can include:

- Addressing social vulnerabilities such as high inequality, low social infrastructure, and informality;
- Preventing sectoral transition finance gaps, especially in social sectors such as health and education (see above), and mitigating the volatility of financing for sustainable development flows;
- Ensuring that countries have enough capacity to mobilise domestic resources, which can be used for redistributive purposes (national solidarity) and to finance public investment in social sectors and human development;
- Strengthening public financial management to ensure efficient public expenditure;
- Improving debt management and public investment efficiency to prevent or overcome debt distress and achieve debt sustainability;
- In fragile contexts, promoting more coherent co-ordination, programming and financing in line with the DAC Recommendation on the Humanitarian Development Peace Nexus.

Table 5 below provides examples of policy options relevant to the co-operative approach that can help address selected challenges and constraints faced by transitioning countries.

Table 5. Key challenges relevant to the co-operative approach and examples of policy options

Challenge	Examples of available policy options
Address social vulnerabilities	– Support the strengthening of domestic resource mobilisation (DRM) systems to ensure a stable stream of government revenue that can be used to invest in social infrastructure (UNCTAD, 2009[25]). – In contexts where domestic resource mobilisation is insufficient, DAC donors can play an important role in financing socioeconomic progress through ODA (Kim et al., 2018[4]). ODA allocation can particularly target social sectors with lowest share of available funding, such as education (Guillaumont, 2014[26]). – Invest in governance reforms (e.g. anti-corruption, public expenditure reviews, public financial management (PFM) reforms (Mustapha et al., 2019[27])) to ensure government revenue is raised and spent efficiently (both for tax and non-tax revenue, such as natural resources rent).
Prevent transition finance gaps and mitigate the volatility of financing for sustainable development flows	– Prevent transition gaps by providing targeted funding and technical assistance to countries and sectors facing reduced support at specific stages of their transition (Piemonte et al., 2019[1]). – Ensure ODF plays a stabilising (or countercyclical) role along the transition continuum to address the volatility of other financial flows (e.g. private capital flows) and sources of income (e.g. fluctuations in commodity prices) (Chauvet and Guillaumont, 2004[28]).
Consolidate domestic resource mobilisation to increase fiscal space for social investment	– Provide technical assistance to strengthen the capacity of the revenue authority (Brautigam and Fieldstad, 2008[29]) (Morrissey, 2015[30]) (Yamada, 2016[31]) and implement specific tax reforms (e.g. with the assistance of Tax Inspectors Without Borders). – Provide support to widen the tax base (e.g. limit tax exemptions/evasion, formalise informal economy) and make the tax system more equitable at the national level (UNCTAD, 2009[25]). – Assist countries in the design and introduction of new taxes (Junquera Varela et al., 2017[32]), particularly taxes with social outcomes (e.g. excises on tobacco or alcohol) and earmarked revenues for social expenditure. – Introduce electronic tax payment systems to increase the efficiency of tax collection and monitoring. – Support the adoption/implementation of international transfer pricing rules and OECD/G20 Inclusive Framework on Base Erosion Profit Shifting (BEPS) (OECD, 2015[33]). – Support research on individuals' behaviour and response to tax collection procedures and re-design the collection process accordingly (Moore, 2019[34]). Make more visible the equity and good use of collected resources to increase overall tax revenue (UNCTAD, 2009[25]).
Debt sustainability	– Increase transparency and co-ordination among actors, in particular with non-Paris club donors and the private sector (Morris, Cattaneo and Poensgen, 2018[19]). – Tackle informality to strengthen domestic resource mobilisation to generate the fiscal revenue necessary to achieve fiscal and debt sustainability (Sepulveda and Syrett, 2007[35]). – Support the establishment of a new debt governance framework that allows easier monitoring of public sector debt sustainability at the country level to improve fiscal discipline (World Bank Group; IMF, 2019[36]).

	– Provide technical assistance on debt management to strengthen developing countries' negotiation skills for more favourable lending terms and potential debt restructuring (Kim et al., 2018[4]). – Support efforts to improve public spending efficiency in order to create additional fiscal space: conduct public expenditures reviews to identify inefficiencies and assist countries in the enhancement of public financial management systems and the design of accountability mechanisms (Shah, 2005[37]).
Humanitarian, development, peace nexus	– Minimise the volatility of humanitarian assistance and support longer-term development interventions in parallel that guarantee the sustained provision of basic services in the post-conflict phase and provide partner countries with increased predictability of ODA flows (Devinit, 2018[38]). – Foster synergies between humanitarian and development activities, for example by implementing social programs in the health and education sectors that target both refugees and the most vulnerable among the local population (Chiofalo, Poensgen and Rockenfeller, 2019[39]).

Box 4. The co-operative approach: an example from the Cabo Verde country pilot

Cabo Verde's LDC graduation, driven by income per capita, has led to the withdrawal of certain donors and a quick phasing out of ODA in key SDG-related sectors, not always substituted by OOF. The transition finance study conducted by the OECD in November 2018 found that there is in fact a continuous need for public sector intervention and official development finance (ODF) after the country's LDC graduation in 2007, in particular to address its persisting economic and environmental vulnerabilities.

The pilot study recommended that development partners support domestic resource mobilisation to build resilience and avoid financing gaps in social sectors. It highlighted that urgent action is also required from development partners to address the country's risk of debt distress and help transform the current, unsustainable financing model (debt-to-GNI ratio of 130%).

OECD DAC members were encouraged to play a role to help monitor reforms of the investment and tax regimes, which should be designed in support of Cabo Verde's sustainable and inclusive development. Finally, the study warned that with growing foreign investments in the country's economy, there is a risk of the emergence of a dual economy, which requires efforts from all development stakeholders to fight rising inequalities (e.g. geographical – across islands, rural/urban, unemployment, gender, youth).

Source: Morris, Cattaneo and Poensgen (2018[19]), Cabo Verde Transition Finance Country Pilot, https://dx.doi.org/10.1787/1affcac6-en

C2 – The competitive approach

The competitive approach seeks to foster private sector development and promote an enabling environment for private investment. Its overall aim is to build capacities in productive and service sectors.

Elements of the competitive strategy can include:

- Promoting a sound business climate and regulatory framework to attract private investment;

- Developing the physical infrastructure required to increase the competitiveness of the economy, reducing the cost of production and transportation of goods and services, and increasing the productivity of input factors ;
- Supporting and diversifying the local economy;
- Increasing the contribution (quantitative) and enhancing the development footprint (qualitative) of dominant sectors to sustainable development through increased alignment with the SDGs;
- Adopting and implementing OECD transfer pricing and BEPS capacity building programmes;
- Loosening credit constraints and improving financial risk management.

Table 6 below provides examples of policy options relevant to the competitive approach that can help address selected challenges and constraints faced by transitioning countries.

Table 6. Key challenges relevant to the competitive approach and examples of policy options

Challenge	Examples of available policy options
Developing the basic physical infrastructure required to increase the competitiveness of the economy	– Invest in and crowd-in private investment to key physical infrastructure programs to increase connectivity and lower the cost of inputs required for productive activities (e.g. electricity) (Morris, Cattaneo and Poensgen, 2018[19]) (Asiedu, 2002[40]) (Gurara et al., 2018[41])
Promoting a sound business climate and regulatory framework to attract private investment	– Support the development of sound business and private investment regulatory framework, in particular on aspects related to cost of entry, investor protection, property rights, access to credit and customs (Kirkpatrick and Parker, 2006[42]), (World Economic Forum, 2018[43]). – Help establish and implement regulatory framework for Public Private Partnerships (PPP) to leverage public resource and mobilise private investment for development projects (World Bank Group, 2017[44]). – Support reforms aimed at improving governance, in particular in the areas of open and transparent government, voice and public accountability (Morrissey and Udomkerdmongkol, 2012[45]). – Assist central bank capacity building and monetary policy to ensure price stability as well as overall sound macroeconomic management (Senga, Cassimon and Essers, 2018[46]).
Loosening credit constraint and improving financial risk management	– Provide funding and technical assistance to increase access to financial services, particularly by supporting policies that target population groups most strongly affected by financial exclusion (Zins and Weill, 2016[47]). – Support the development of domestic financial markets in terms of depth (size and liquidity of markets), access (ability of individuals to access financial services), and efficiency (ability to provide financial services at low cost and with sustainable revenues) (Sahay et al., 2015[48]). This will in turn permit to intermediate funds from savers to investors (Hermes, 2003[49]) and allow local and foreign firms to implement hedging strategies that reduce their exposure (e.g. derivatives to manage foreign exchange risk). – Support the implementation of capital market regulations aimed at reducing volatility and incentivising longer-term investment, allowing resources to be allocated where they are needed to promote productive investment (Henry, 2003[50]).

Supporting and diversifying the local economy	– Invest in key sectors of the local economy with high growth potential and comparative advantage (Papageorgiou and Spatafora, 2014[51]). – Reduce tied aid to ensure ODA generates local spillovers in the economy (Clay, Geddes and Natali, 2009[52]) and mainstream policy dialogue with the private sector in development assistance programmes (Morris, Cattaneo and Poensgen, 2018[19]).
Increasing the contribution of dominant sectors to sustainable development	– Foster linkages between trade-oriented FDI sectors and local sector value creation, for example by identifying local sourcing opportunities (Kim and Poensgen, 2019[53]) (Buzdugan and Tüselmann, 2018[54]; Amendolagine, Presbitero and Rabellotti, 2017[55]). – Strengthen domestic resource mobilisation through tax reform and public financial management to increase tax and non-tax revenue generated by dominant sectors (e.g. extractive industries, tourism, etc.) (Junquera Varela et al., 2017[32]). – Encourage and track CSR activities to reach the full potential of such programmes and align initiatives with the national development plans (Schönherr and Findler, 2017[56]).
Enhancing the integration in the global economy	– Strengthen trade relationships, including through aid for trade programmes (OECD/WTO, 2019[57]). – Extend existing differential treatment available to countries with structural (exogenous) vulnerabilities for a period appropriate to the development situation (Guillaumont, 2011[58]). – Provide technical assistance to increase trade openness and support the implementation of standards in FTAs (UNCTAD, 2013[59]).

Box 5. The competitive approach: an example from the Viet Nam country pilot

Balancing the financing mix by promoting private sector investments

While Viet Nam has been successful in initiating a shift from external towards domestic sources of finance over the past few decades, the transition finance pilot conducted by the OECD observed that a concurrent shift from a high level of reliance on public towards private financing would be required to ensure a balanced transition. The counselling section of the study thus called on the country's government and its development partners to strengthen the enabling environment for the private sector.

For example, the lack of a comprehensive and clear legal framework for public-private partnerships appears to be a key constraint. Through their dialogue with the government, international partners, in addition to providing technical assistance, could help to elevate the PPP agenda on the list of government priorities, and could also use concessional finance strategically to crowd in private finance.

Enhancing the development quality of private finance

Another key recommendation addressed to international development partners was to help promote financial sector development and to scale up their support to link SMEs with the growing FDI sector in order to allow for more opportunities for local value creation. This would contribute to fill the considerable gap existing between the burgeoning FDI sector and an underdeveloped domestic private sector, which often lacks access to finance.

In addition to increasing fund and facilities for SMEs, the study stressed the need to simplify access to finance: while a number of funds for SMEs already exist, their effectiveness is hampered by a lack of awareness and complex administrative procedures.

Finally, the study expressed concern that private investment is often promoted at the cost of the environment, and thus called on all stakeholders to support the creation of an enabling legal and regulatory framework that increases the sustainable development footprint of private sector investments.

Source: Kim and Poensgen (2019[53]), Transition Finance Country Study Viet Nam: On the Threshold of Transition, https://doi.org/10.1787/3cb86a6c-en

C3 – The case for a renewed partnership

Transition is a joint effort that requires co-ordination and planning among domestic and international, public and private actors. As countries move along the development continuum, financing instruments and actors change. More so, the financing landscape has become increasingly complex in recent years with more instruments and actors involved (OECD, 2018[2]). While this holds great opportunities to maximise financing for sustainable development, it also requires more co-ordination and knowledge to materialise its benefits.

Successful implementation of the co-operative and competitive strategy thus depends on renewed partnerships and new modes and channels of co-operation as outlined in Table 7 below.

Table 7. Key issues relevant to renewed partnerships and examples of policy options

Challenge	Examples of available policy options
Co-ordination, monitoring and planning	– Co-ordination helps development partners complement each other and allows partners to focus on value-added and comparative advantage; – Co-ordination can increase leverage among development partners to advocate for common objectives and reforms; – Monitoring financing to key sectors helps predict financing needs and enables stakeholders to counteract/preclude sectoral transition finance gaps; – Phasing out or scaling down of development co-operation should be guided by a longer-term strategy including timely consultation with relevant stakeholders and clear objectives and tasks (Engen and Prizzon, 2019[60]) (Rose, Collinson and Kalow, 2017[61]).
Use of innovative instruments	– Mobilise private resources through blended finance, social impact bonds, and PPPs; – Promote investments in climate finance (e.g. green bonds, access to the Green Climate Fund) and the blue economy (e.g. blue bonds); – Facilitate partnership on decentralised level (OECD, 2019[62]); – Other instruments (e.g. diaspora bonds, debt for nature swap).
Transparency for debt sustainability	– Promote enhanced transparency of lending terms and conditions to better monitor debt levels and lending terms from different sources; – Support policy reforms aimed at improving debt data reporting to restore trust among actors and enable better co-ordination (Morris, Cattaneo and Poensgen, 2018[19]).

Shared responsibility for global public goods	– Support countries affected by forced displacement, natural disasters, health epidemics, security risks, environmental vulnerabilities; – Increasing role of middle-income countries in the international system in the provision of global public goods (Alonso, Glennie and Sumner, 2014[63]).
Adjusted type of co-operation	– Phasing-out of bilateral programmes still allows diverse forms of co-operation (ODI 2019) including continued collaboration through multilateral providers of development finance (Rose, Collinson and Kalow, 2017[61]). – Transition, especially moving up the income spectrum, can imply a shift from development to economic partnership, sometimes reflected in the emergence of new free trade agreements (Kim and Poensgen, 2019[53]); – Partnership and co-operation can continue after ODA graduation (Piemonte, Catteneo and Poensgen, Forthcoming[17]); partners can establish post-presence tools such as enterprise funds and binational foundations and commissions (Rose, Collinson and Kalow, 2017[61]).
Guided by aid effectiveness principles	– Allow for sufficient time in transition strategies to hand over responsibilities to the government (Engen and Prizzon, 2019[60]); design and delivery of remaining grant assistance should be driven by country ownership, for example by using country-led results frameworks, indicators and data when developing new interventions and programmes (Rose, Collinson and Kalow, 2017[61]); – Support the integration of national development plans within Integrated National Financing Frameworks (INFFs); – Facilitate the alignment of graduation processes and national development plans, ensuring that national strategies include plans to mitigate negative graduation impact.

Box 6. The case for a renewed partnership: an example from the Chile country pilot

The Chilean case illustrates a number of key lessons learned from the transition of UMIC to HIC status, and the subsequent loss of ODA eligibility. In particular, it shows the need to carefully plan for a strategic phasing out of ODA and a progressive shift towards other forms of collaboration, such as technical co-operation and peer-to-peer learning.

The pilot transition finance study conducted in Chile recommended that the DAC community ensure, before it leaves newly-graduated countries, that central authorities are anticipating, and appropriately budgeting for, potential transition gaps, but also that new forms of partnerships are gradually promoted to replace development co-operation. In the case of Chile, many DAC members seem to have left the country rather abruptly without a formal exit strategy.

Technical co-operation from DAC members would be particularly useful to improve domestic resource mobilisation, an area where Chile is lagging behind its peers. For example, the analysis showed that Chile's tax revenues at 20.2% of GDP in 2017 are substantially lower than the 30.9% mobilised in Uruguay, Chile's regional peer, and the overall OECD average of 34.2%.

As an OECD member (since 2010), Chile can take full advantage of the opportunities for peer-to-peer learning offered by the Organisation for Economic Co-operation and Development (OECD) in order to tackle persisting transition challenges. The OECD DAC can support the development of mechanisms

to help new OECD members make the most of the organisation's international expertise and best practices.

Source: Piemonte, Cattaneo and Poensgen (Forthcoming[17]), Better Mangaging Graduation from ODA Eligibility - A transition Finance Study of Chile, http://www.oecd.org/dac/transition-finance-toolkit/

Renewing partnerships requires commitment and co-ordination from all stakeholders. Information on partners' activities is key to take initiatives and ensure value-added of one's own contribution. The following sources provide a useful reference point to map the engagement of various actors:

- The OECD Creditor Reporting System (CRS) includes information on each project implemented by development partners using ODA. Purpose codes on the specific project target as well as project descriptions provide useful variables to filter projects;
- The OECD SDG Financing Lab (2019[10]) mentioned in Chapter 1 provides estimates on DAC donors development finance with respect to the 17 SDGs;
- DAC donors' development agencies provide detailed information on the country's engagement in the respective recipient countries;
- The Global Partnership for Effective Development Co-operation (GPEDC) Dashboard allows to understand better how effectively development co-operation is delivered at the country level
- AidData, a research lab at William & Mary, and the CARI institute at the John Hopkins University each provide estimates on Chinese development finance.

To learn more: List of operational resources

OECD material:

- OECD/UNCDF (2019), Blended Finance in the Least Developed Countries 2019
- OECD/UNDP (2019): Global Partnership for Effective Development Co-operation Country Profiles

Other material:

- UNCTAD (2018): Achieving the Sustainable Development Goals in the Least Developed Countries – A compendium of policy options, United Nations.
- UNCTAD (2009): Enhancing the role of domestic financial resources in Africa's development – A policy handbook, United Nations.
- UNCTAD (2015): Making trade work for Least Developed Countries: A Handbook on Mainstreaming Trade, United Nations.
- UNCTAD (2016): The Least Developed Countries Report 2016 – The path to graduation and beyond: Making the most of the process, United Nations.
- UNDESA/CDP (2017): Expanding productive capacity – Lessons learned from graduation Least Developed Countries, United Nations.
- ODI (2019): Exit from aid – An analysis of donor experiences.
- Rose, Collinson and Kalow (2017): Working Itself Out of a Job: USAID and Smart Strategic Transitions, CGD Policy Paper 113.

Annexes

Glossary

ABC methodology

A guiding framework for the implementation of transition finance approaches. The ABC methodology includes operational guidance to **A**ssess country contexts, **B**enchmark country performance, and **C**ounsel development partners on the design of specific strategies to optimise countries' access to finance.

Addis Ababa Action Agenda (AAAA)

Negotiated at the Third Financing for Development Conference in Addis Ababa, Ethiopia, in July 2015, the AAAA sets out a strategy for implementing the global sustainable development agenda adopted in September 2015. It includes more than 100 measures covering all sources of finance and includes co-operation on a range of issues include technology, science, innovation, trade and capacity building.

Agenda 2030 or the 2030 Agenda for Sustainable Development

The 2030 Agenda for Sustainable Development is centred on the 17 Sustainable Development Goals (SDGs) agreed in September 2015. It is also conceived as a broad agenda that includes the AAAA as a framework for implementation and the Paris Agreement on Climate Change, and that builds on a history of multilateral agreements such as the Universal Declaration of Human Rights.

Financing gap

In the context of transition finance, financing gaps are the result of imperfect substitution among different financing sources, whereby the decline of a particular source is not (or insufficiently) compensated by an increase in other sources, resulting in reduced overall availability of financing for sustainable development.

Financing mix

The mix of financial resources available to countries to finance their development and the achievement of the SDGs. The Addis Ababa Action Agenda classifies financing sources into a 4 x 4 matrix: domestic/external and public/private (see Figure 5, page 14).

Financing source

See the list and definition of key financing sources in Figure 3, page 15.

Financing surplus

In the context of transition finance, financing surpluses are the result of imperfect substitution among different financing sources, whereby the increase of a particular source results in higher overall availability of financing for sustainable development.

Graduation

In the context of transition finance, the term “graduation” refers to the loss of eligibility of a country to specific concessional instruments or support measures, resulting from the achievement of certain development criteria (such as reaching a threshold based on income level, but not only). Graduation often has a prescriptive dimension (legal or regulatory), and can come with financial, technical and administrative implications.

Substitution

In the context of transition finance, substitution refers to the interactions observed between financing sources, whereby the decline/increase of inflows from one source is compensated by the increase/decline in another financing source. Research shows that imperfect substitution can lead to financing gaps (see Financing gap) or surpluses (see Financing surplus).

Transition

In the context of transition finance, the term “transition” refers to the different development stages that countries go through in their journey towards sustainable development and the achievement of the SDGs.

Transition finance

The OECD defines transition finance as the financing of countries’ journey towards sustainable development (Piemonte et al., 2019[1]). Transition finance posits that countries’ access to financing varies according to their development stage: as countries transition towards higher development levels, they gain access to a broad variety of financing sources, but also loose eligibility to specific financing tools and instruments. The term of transition should not be mistaken for the concept of graduation (see Graduation).

Tipping point

Point in time where major substitutions occur, generally leading to financing gaps or surpluses. In visual analysis, tipping points are denoted as the intersection of the curves representing the different financing sources (see Figure 13).

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