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MULTILATERAL DEVELOPMENT BANKS FOR GLOBAL PUBLIC GOODS

EXECUTIVE SUMMARY: HOW THE WORLD BANK CAN SUPPORT GPGS

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Global goals require local action. Multiple past disasters have forcefully demonstrated that the world faces more and more crises that transcend national borders and affect people worldwide. Often, the root of the crises - be it climate change, the loss of biodiversity, or pandemics - is the underprovision of so-called Global Public Goods (GPGs). Although GPGs require global collective action, their underprovision can only be tackled at the local level. While emerging economies and developing countries are often hit hardest by global crises, they also play a key role in achieving the goals that the world has set itself to approach these crises. GPG provision can require large investments, for example sustainable infrastructure development, but developing countries often lack the financial capacity to stem these investments on their own. Thus, the World Bank can play a key role in preventing these crises by supporting the provision and protection of GPGs in its client countries.

GPGs are defined by cross-country externalities of local action and are consequently underprovided. Many of the crises that the world faces and has faced in recent years derived from the problem of cross-country externalities. Greenhouse gas emissions can be economically fully utilised in the place where they are emitted but exhibit their harm all around the world. Similar logic applies to other GPGs, such as limiting the destruction of ecosystems and incurring the costs of preparing for a pandemic. Because these externalities are present, countries' incentives to provide the global good in averting harm are not perfectly aligned with global needs, and GPGs are underprovided. GPGs thus have special characteristics, as i) they generally produce substantial cross-country externalities, ii) they are costly to provide or have high opportunity costs of protecting them, and iii) they generate opportunities for improving welfare through collective action. Therefore, countries have strong incentives to free ride, i.e., to invest less than what is needed to achieve a global provision level, which was optimal for all countries and was eventually agreed upon multilaterally in international regimes.

Seven GPG themes are considered in this report to analyse which GPGs could be particularly relevant for the World Bank: climate change mitigation, preservation of biodiversity and ecosystems, pandemic preparedness, prevention of violent conflicts, free trade, international tax cooperation, and financial stability. They are examples of how their provision entails substantial externalities on other countries, while they are costly to provide. However, some closely related areas, such as adaptation to climate change, dealing with refugee flows, or domestic resource mobilisation, do not follow a GPG logic. They deal foremost with the national results of the underprovision of GPGs but do not exhibit externalities on other countries themselves.

GPG provision needs to be anchored in international regimes. To solve the coordination problem of GPGs, international agreements or institutions are necessary to pave the way for any GPG activity. They legitimise and guide any GPG-enhancing action by specifying that there is i) a globally acknowledged need for collective action, ii) a common global target to be reached, and iii) – in the best case ambitious – national contribution targets for reaching global goals. The Paris Agreement, the Convention on Biological Diversity (CBD), the International Health Regulations by the World Health Organization, and the trade standards set by World Trade Organization are examples of such agreements, although many more exist.

International GPG regimes alone cannot solve the underprovision of GPGs. Despite several design specificities, international regimes in GPGs in most cases are missing a credible enforcement mechanism. As a result, there remains too little incentive for countries to provide GPGs to the globally desired extent. There are two different ways to further increase this incentive by the global community – "sticks" and "carrots". First, individual countries can leverage their market power in international trade to incentivise their trading partners to provide GPGs – either through GPG-related regulation of the corresponding trade flows (e.g., European Carbon-Border Adjustment Mechanism) or through conditioning preferential market access on the GPG provision by the respective partner countries (e.g., Climate Clubs à la Nordhaus (2015)). Our empirical analysis shows that there is potential for large economies like the US and EU, but also China, for example, to increasingly use these "sticks" to foster GPG provision in their partner countries – as well as their own countries. Second, financial incentives can encourage national contributions to global goals and thereby complement international regimes. Those "carrots" serve as an additional encouragement for countries to provide GPGs.

The World Bank is uniquely positioned to take on the role of the financier of international regimes on GPGs in developing countries. Apart from motivating developing countries to join international regimes, the World Bank has a key role in implementing and disseminating international agreements and standards in developing countries. Adjustments to agreements can be very costly (e.g., costs for a "Just Transition") and developing countries often lack the financial resources to deliver on regimes. Hence, to become a "Bank for the World", the World Bank should position itself as the disseminator and financier of international regimes that align with its mandate. An analysis of core regimes for GPG highlights how the World Bank already bases large parts of its work on international regimes, and its national delivery plans (e.g., NDCs, NBSAPs, WHO Benchmarking documents for International Health Regulations capacities). Furthermore, the World Bank disseminates global minimum standards by applying them to the Bank's safeguards. However, there is room for more strategic and consistent use of international agreements and standards throughout all Bank operations.

Better GPG provision is key to achieving the Twin Goals set by the World Bank. Positioning the World Bank as "Bank for the World" comes with substantial synergies to its mandate – reducing poverty and supporting shared prosperity in a sustainable way – as well as significant benefits to its client countries. Not only do emerging economies and developing

countries play a key role in the global provision of many GPGs, but they are often the ones particularly affected by their underprovision. Since the underprovision of GPGs limits the developing countries' abilities to achieve national development goals (Lankes, Soubeyran, & Stern, 2022) and therefore the Twin Goals of the World Bank, a strategic shift – making GPG provision a centrepiece of a transformed country-based engagement model – is a logical consequence to preparing the Bank as well as its client countries for the future.

Economic and non-economic returns to investments in GPGs are immense. To assess which GPGs are relevant for developing countries and where the World Bank should focus its operations, the global and national costs, and the benefits of GPGs need to be reviewed. An analysis of the quantitative aggregate benefits and costs of the GPGs shows that the benefits to investments in GPGs tend to be immense, at comparably low costs. At the same time, financing needs – especially in developing countries – still exist. Averting climate change alone would result in yearly economic and non-economic benefits in the dimension of up to the equivalent of 10% of global GDP in 2100; the costs for averting it account for around 5% of global GDP until 2050 only. As emerging markets and developing economies are particularly affected by the risks of climate change, the benefits of climate change mitigation largely accrue to the developing world. Preserving biodiversity can even be more beneficial to the world, with more than 50% of yearly global GDP at risk in economic and non-economic equivalents by 2050 if the loss of ecosystems cannot be stopped. Yet, preservation would cost the world less than 1% of the global GDP per year. Pandemic prevention can bring benefits through avoiding pandemics such as the Covid-19 pandemic, but also other, more regional pandemics with global effects. The Covid-19 pandemic alone caused an estimated harm of the equivalent of 4% of global GDP over six years, and pandemics before Covid-19 had negative effects of US$237 billion per year on average. In contrast, improving pandemic prevention would cost only up to US$45 billion per year, which is less than 0.1% of the global GDP. Although estimates of the benefits and costs of GPG provision come with some uncertainty, the dimensions of the returns to investment in GPGs alone make a strong case for scaling them up.[1]

The selection of GPGs supported by the World Bank should be based on clear criteria. A positive cost-benefit ratio of GPG investments is not a sufficient reason for the World Bank to take on a more central role in its provision. Additional selectivity criteria need to ensure that the World Bank focuses on the most urgent challenges, to concentrate resources and not overtax the capacities of developing countries. More importantly, the World Bank should leverage its comparative advantages as just one yet important piece of the global GPG delivery system. Thus, we propose certain criteria to select GPGs that the World Bank should focus on. These criteria are based on the aggregate benefits and costs of the GPGs, they can be linked to a ratified global regime, and they are in line with the Bank's mandate as their provision

[1] The costs and benefits displayed are based on a literature review. The sources and additional calculations can be found in Chapter **Fehler! Verweisquelle konnte nicht gefunden werden.** of the main report.

would benefit developing countries. Furthermore, there should be a GPG-specific financing gap in the World Bank's client countries, where catalysing resources and partnerships can have an impact, and there should be an institutional gap at the nexus of translating global goals into local action. In GPGs that do not meet these criteria, the World Bank should continue to play a strong role in supporting developing countries in (the Just Transition to) meeting international minimum standards and mitigating structural weaknesses, without the need to change instruments and operational procedures for this purpose.

The World Bank should mainstream GPG considerations into operations. Through its safeguards, its knowledge work, and its convening power, the Bank can play a significant role in disseminating global standards and pivoting for GPG support in developing countries. Although much is already done in that regard, GPGs have to become central to all operations. As a prerequisite, GPGs need to be mainstreamed into all aspects of the World Bank's work by aligning the Bank's safeguards with international minimum standards. It has to be ensured that World Bank-financed projects do no excessive harm to the GPGs in question. Consequently, certain core WBG country diagnostics and Advisory Services and Analytics (ASA) products must be mandatory for country engagement. Furthermore, the World Bank should include the targets set by international regimes for the selected GPGs in its High-Level Outcomes (HLOs) as they inform country programming and the Country Partnership Frameworks (CPF) – the most important strategic planning tool in the country engagement model. In the CPF, client countries and country managers negotiate projects at the intersection of the client country's national development objectives, the Bank's comparative advantages, and the HLOs. Including GPGs in the HLOs will force country directors to systematically prefer projects with positive GPG externalities over projects with no such externalities at similar levels of client-country benefits.

Ambitious GPG projects or policies need additional concessional funds resulting in a price differentiation between GPG and non-GPG projects. The starting point of any re-allocation of concessional financing should be the core problem of GPGs, namely their structural underprovision that stems from the fact that a (varying) part of the benefits from GPG provision does not benefit the providing country but other countries (cross-country externalities). Given the ongoing critique of client countries on the re-allocation of concessional finance away from national development priorities, we suggest maximising the synergies between national development goals and GPG provision in the case of a given country envelope. This would maximise the cross-country externalities among projects that have a positive national profit. These projects already benefit from implicit concessionality – i.e., ASA and reduced interest rates due to the Bank's AAA rating.

However, ambitious, transformative projects which tend to be very costly to the providing country and exhibit significant cross-country externalities would probably reveal a negative national profit. To support ambitious GPG provision and not divert resources from efforts towards national development goals, we propose the allocation of additional, explicit GPG-

specific funding. If a significant share of the benefits occurs to other countries than the one providing it, it can only be perceived as fair and just to increase financing accordingly. This concessionality should aim to support GPG projects with high cross-country externalities and a remaining financing gap. The more additional specific GPG funding is available, the more ambitious projects can be supported in the Bank's country engagement.

Specific GPG funding should be strategically allocated to "buy cross-country externalities" based on cost-benefit reasoning. To assess the financing gap and the cross-country externalities, every GPG project in need of additional concessionality should be supposed to develop a cost-benefit analysis (CBA). Depending on the type of project, it may be sufficient that projects or policies estimate the externalities that they provide or at least substantiate their financing needs with cost-benefit reasoning to prove their eligibility. Based on the cost-benefit reasoning, concessional finance to spur GPG provision in client countries needs to be allocated following a rules-based approach – either through financing the project-specific financing gap or through a uniform subsidy per externality. Aside from the pros and cons of different allocation principles, any grant funds should be strategically used for "buying cross-border externalities", i.e., allocating grants according to the measurable degree of cross-border externalities as opposed to the flat subsidy rate in the GPG Fund. Any re-launch of the GPG fund should consider this.

The costs of spurring GPG provision can be much lower than their benefits. The good news is that the required financing for GPG provision in the World Bank is much less than the benefits they generate, i.e., the monetary value of the externalities produced. First, it is sufficient to support projects by the additional costs of GPG provision, not the value of the externalities. These costs can be low – and significantly lower than the value of externalities produced – in many cases. The financial support could even be lower than the additional costs of providing the GPG. This is because, second, due to their commitments in international agreements, countries have their own incentive to keep them, implying that only partial support against the additional costs should often be sufficient to incentivise the consideration of cross-country externalities in designing policy programmes and investment projects. Thus, "sticks" as trade benchmarks can reduce the "carrots" MDBs have to offer their client countries.

The Bank's knowledge work should form the basis for an evidence-based GPG delivery system in developing countries. How to best provide GPGs in alignment with national development strategies and the SDGs is a major obstacle in the current GPG discourse. The knowledge work of the Bank should help overcome the perceived dichotomy of objectives between national development goals and GPGs. Knowledge of national benefits alone could already significantly increase GPG provision, particularly regarding the preservation of ecosystems. Furthermore, the World Bank can assist in knowledge creation and analytics on translating global goals to the country level as well as in the measurement, reporting, and verification (MRV) on the ambition of national targets, compliance with international standards, and the actual implementation of national obligations. Through its global reach and

the collaboration of country operations and Global Practices, the World Bank gathers knowledge that can be central to an efficient provision of GPGs in its client countries. Sharing best practices could also greatly contribute to even further lowering the aggregate costs of GPG provision, for client countries and the World Bank.

Systematic incorporation of GPG considerations into World Bank operations is needed. The World Bank already is in a good position to support GPG provision. It has a comparative advantage vis-a-vis other multilateral institutions in that it has ample experience in translating global goals into local action, and good knowledge of individual country needs to create synergies of GPG provision with national development goals. Its activities in the respective GPG areas are well-founded in comprehensive knowledge through its Global Practices and beyond. Its potential to finance on-the-ground operations makes it an ideal partner for its client countries to help finance their activities to keep their international commitments. On the other hand, GPG provision is key to the World Bank achieving its own goals as set by the Twin Goals. However, to make use of its comparative advantage and to tap the potential that lies in a global provision of GPGs for achieving the SDGs, it has to incorporate GPG considerations into its model much more systematically.

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Authors: Johanna Neuhoff, Hannah Zick, Dr. Yann Girard, Helene Schüle (Oxford Economics)
Dr. Jakob Schwab, Dr. Peter Wolff, Dr. Hanns-Peter Neuhoff (Consultants)

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To discuss the report further please contact:

Johanna Neuhoff: jneuhoff@oxfordeconomics.com

Yann Girard: ygirard@oxfordeconomics.com

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Federal Ministry
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Global headquarters
Oxford Economics Ltd
Abbey House
121 St Aldates
Oxford, OX1 1HB
UK
Tel: +44 (0)1865 268900

London
4 Millbank
London, SW1P 3JA
UK
Tel: +44 (0)203 910 8000

Frankfurt
Marienstr. 15
60329 Frankfurt am Main
Germany
Tel: +49 69 96 758 658

New York
5 Hanover Square, 8th Floor
New York, NY 10004
USA
Tel: +1 (646) 786 1879

Singapore
6 Battery Road
#38-05
Singapore 049909
Tel: +65 6850 0110

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