

GLOBAL DEVELOPMENT BONDS

Global Development Bonds (GDBs) would increase and improve finance for sustainable development by mobilizing larger flows of private capital from institutional investors, who are currently unable to invest in such activity because rated securities for such projects do not exist.

Traditional public foreign aid is too scarce and too ineffective by far to meet the developing world's urgent need for investment in sustainable development. Meeting the United Nations Millennium Development Goals (<http://www.un.org/millenniumgoals/>) with public foreign aid alone would require an additional \$50 billion a year, roughly double the current amount. GDBs would enlist instead the vast resources and the efficiency, judgment, skills, and creativity of private capital-market money managers in the effort to meet the world's development goals. Economic development abroad will also open up new export opportunities for U.S. businesses, create U.S. jobs, and generate tax revenue.

To date, the worldwide financing of sustainable development has been largely the domain of public-sector agencies. While private-sector investment in the developing world has surpassed official development assistance since the end of the 1980s, debt and equity flows have been volatile, trending downward since the late 1990s, and focused on selected regions. Engaging capital markets more broadly is a major challenge, especially tapping the large pools of capital managed by institutional investors that, by fiduciary duty, invest conservatively. Public-sector risk mitigation programs often are cumbersome and expensive because they are applied case-by-case and lack a systematized approach.

GDBs would be a new category ("asset class") of investment security, comparable to municipal bonds, for example. Like all bonds, GDBs would be long-term, interest-bearing debt instruments providing a fixed return to the investor. GDBs would be issued by private entities, and the money raised from GDB sales would go through commercial banks to qualifying uses in qualifying countries. Qualifying uses would include projects associated with sustainability, such as water and clean energy development. Country qualifications would pertain to, at a minimum, free markets and the rule of law. Additional country eligibility criteria, for example, those associated with the Millennium Challenge Account, could also be adopted.

As a private financial product, GDBs must offer buyers an attractive risk-adjusted rate of return in order to compete with other investment products in the market. The rate of return is basically a function of the soundness of the underlying project investments. The private sector is well-equipped to make evaluations of soundness. The private financial sector is also adept at managing many types of risks. Like other bonds, GDBs would reduce their risk through diversification and other sophisticated financial arrangements.

Private investment in the developing world poses unique types of risk. Insuring against political and foreign exchange risks has historically been expensive enough to discourage private investment. The U.S. government would play a limited but critical role in GDBs by mitigating these types of risk, e.g., by providing political risk insurance and foreign exchange coverage. With the proper private-sector arrangements and public-sector enhancements, GDBs could receive the investment-grade bond ratings needed to qualify for purchase by institutional investors, providing a pathway to engage their assets in sustainable development. U.S. pension funds alone totaled \$6.4 trillion in 2001.