Public and Private Financing Instruments to Support SDGs: The Case of Albania

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Abstract The purpose of this paper is to identify and promote actions to finance the SDGs by bringing together governments, the private sector and the civil society. Following the rule 'it takes money to make money', the tight fiscal space of Albania is analysed to present potential approaches that can boost private financing leverage. Private finance is the main contributor to support the SDGs, while public finance has a small financing weight in the whole integrated financial framework, so this minor financing weight can be used to leverage private finance sector. This combination of finance instruments aims to provide sustainable financing for SDGs. This paper presents the process to reach a sustainable financing mechanism of SDGs in Albania. Additionally, it presents the tools, like Development Finance Assessment (DFA) and Integrated National Financing Frameworks (INFFs) that lead the country to link finance with results for delivering the SDGs. The paper provides a methodological approach, among others, to support SDGs sustainable financing in order to reach the SDGs targets. This research might bring implications for other developing countries in relation to financing SDGs.

Keywords:
SDGs,
DFA,
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financing instruments,
sustainability

JEL:
E61, O11, O23

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1 Introduction

The Government of Albania is committed to the 2030 Agenda for Sustainable development, which corresponds to the fulfillment of 17 goals and 169 targets. Many challenges are presented in the fulfillment of these goals, 9 out of 17 continues to be significantly challenging. Figure 1 shows Albanian SDG Dashboards and Trends 2022.

1.No Poverty	↑	5.Gender equality	↗	9. Industry, Innovation and Infrastructure	↗	13.Climate Action	↑
2. Zero hunger	→	6. Clean Water and Sanitation	↑	10.Reduced Inequality	→	14. Life Below Water	→
3.Good health and well-being	↗	7.Affordable and Clean Energy	↑	11.Sustainable Cities and Communities	→	15. Life on Land	→
4. Quality education	→	8.Decent Work and Economic Growth	↗	12.Responsible Consumption and Production	↑	16.Peace and Justice Strong Institutions.	→
Red-major challenging; Orange- Significant Challenges; Amber-Challenges remain;						17.Partnerships to achieve the Goal	↗

Figure 1: Albanian SDG Dashboards and Trends 2022
Source: Sustainable Development Report (2022) and Author's illustration

This overview demonstrates the highest need to intervene for complying with Agenda 2030, struggling with five critical dimensions: people, prosperity, planet, partnership and peace, also known as the 5Ps. SDG 8 is one of the most challenging goals, characterized by an economic growth with high volatility which is greatly affected by any shock, such as the Covid 19 pandemic reflected by negative growth in 2020 (see Figure 2).

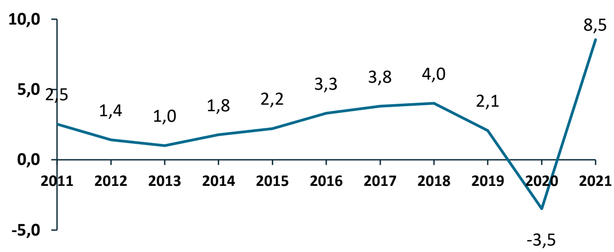

Figure 2: Albanian Real GDP growth in %
Source: Ministry of Finance and Economy (2022).

To achieve SDGs, their alignments with country's social, economic and environmental priorities is required. The accurate assessment and calculation of financial costs as well as the identification of financial options for the fulfillment of development objectives continue to remain a challenge for the Albanian government. Still in the budgeting process of national strategies, deficiencies in the costing process continue, making it difficult to identify the necessary public financial resources, while the contribution of private finances remains even more difficult to calculate. The medium-and long-term national priorities according to a medium term and long-term macroeconomic framework is materialized in the National Strategy for Development and Integration (NSDI) document. 2021-2030 NSDI timeframe, which is under preparation process, corresponds with the European Policy Cycle (7 years), the cycle of the Instrument for Pre-Accession- IPA and the SDGs (due in 2030). Successive crises, such as the November 2019 earthquake and the COVID-19 pandemic, have exacerbated existing weaknesses and tightened the country's fiscal space, making the Sustainable Development Agenda even more urgent. This context demonstrates urgent need of institutions to intervene. The UN Joint Program 'Strategic Policy Options for SDG Financing', which aims to support SDG financing in Albania, has started to be implemented in 2020. It aims to bring evidence on the costs of not investing in the SDGs, as well as identify and evaluate options to catalyze financing to unfunded objectives in and identify innovative approaches, tools and other financing mechanisms to pilot and evaluate the impact of fiscal policies. This paper aims to analyze the potential sources of public and private finance in Albania and to present a roadmap to integrate financial sources for SDGs budgeting.

2 Literature Review

Success in achieving the SDGs is hampered by severe financial constraints facing developing countries and not only, constraints that have been severely exacerbated by the Covid-9 pandemic and the war in Ukraine. In addition to maintain peace and reducing geopolitical tensions, the key to achieving the SDGs is to devise a plan for financing them (UN, 2022).

As presented by Hege & Brimont (2018), a starting point for the integration of Agenda 2030 and in national policies and to implement the Sustainable Development Goals (SDGs), is the integration of SDGs into national budgeting processes.

For developing countries, costing the SDGs is essential to secure the investment and development assistance needed to achieve the SDGs. this process can help governments, donors and international organizations develop strategies for achieving specific SDG targets (Vorisek & Yu, 2020).

The implementation of the UN 2030 Agenda, according to a UN study, is estimated to cost between USD 3.3–4.5 trillion per year to fund different projects, development programs and various initiatives which help countries achieve these ambitious goals. Developing countries face an average annual funding gap of USD 2.5 trillion.

Government-driven or multilateral aid institutions-led support needs to be complemented by the private sector and the abundant funds that are available on the markets. The task for policymakers and private sector investors is, therefore, to coordinate and look for more innovative approaches. As far as the European region is concerned, the adoption of the European Green Deal is a game changer which sets the stage by introducing clear goals and investment needs to turn the economy around by 2050 (Lukšić et al., 2022).

According to several international assessments, investment needs for the SDGs are huge, with the bulk in developing countries and their infrastructure. The scale of current financial flows is considered insufficient: as public finance is in scarce supply, while private finance is constrained by risk and return requirements. If this resulting financing gap remains unresolved, investment needs will grow over time because of a cumulative effect. Several doubts could be raised: should we conclude that the SDGs are beyond reach, or could business models be rethought in ways that would increase SDG serving financial flows, but also make them less risky, and could the cost of achieving the SDGs be brought down? Figure 3 shows SDG annual financing gap - advanced vs. EMDEs (in trillion $).

In advanced countries, about 90% of investment needs can be met in advanced countries under current conditions, and public sector could cover only a third of the financing needs, with the private sector covering most of the rest. In developing and emerging countries, only 48% of SDG investment needs are being met, while public and private financial flows are of comparable size and the share of private finance in these countries would need to double to approach that of advanced countries. (UNEPFI, 2018,10-11,).

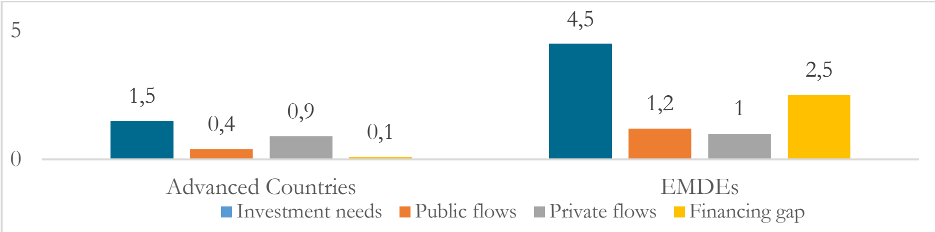

Figure 3: SDG annual financing gap - advanced vs. EMDEs (in trillion $)
Source: UNEPFI (2018)

In Albania, there is no identification of what part of investment needs can be met. All the findings presented above demonstrate as a starting point for achieving the SDGs: assessing their costs, integrating them into the national budgeting process and exploring innovative financing instruments, beyond traditional finance such as public funds. The following sections briefly present: paper methodology, results found and concluding remarks.

3 Methodology

A general quantitative and qualitative analysis of public and private finances has been carried out to provide a methodological approach to the steps that a country like Albania is following to finance the SDGs. The limitation of this work is the lack of determining the amount of private finance funds needed to finance the SDGs, while public finance goes all without exception to their financing. This task requires a later stage, such as the drafting of a strategy for the integrated national financial framework. Using secondary data on key indicators of public and private finances in the country provided by official institutions such as: Bank of Albania, Ministry of Finance and UN Albania, an overview of the financial resources that have the most potential to support sustainable financing of the SDGs that a developing country needs to undertake is provided.

4 Results

Considering above finding for developing countries, where Albania belongs, less than half of financing needs for SDGs fulfilment are in place. Also, private finances, which should cover the major investments needs, remains lower than public findings. In order to follow advancing countries model, most effort should be undertaken to leverage and mobilize private financing.

4.1 Public Finances

Governments and public finances have an important role in creating the conditions and incentives that can unlock domestic and international private financing, and to promote business strategies and operations that are aligned with priorities for recovery and sustainable development. Unlocking and boosting private capital for SDG related investments requires policy and regulatory shifts, better access to information on investment opportunities, and clear standards on the criteria for identifying SDG aligned investments. The development of an integrated approach to public policies for private finance is at the heart of the innovation of the integrated national financing framework.

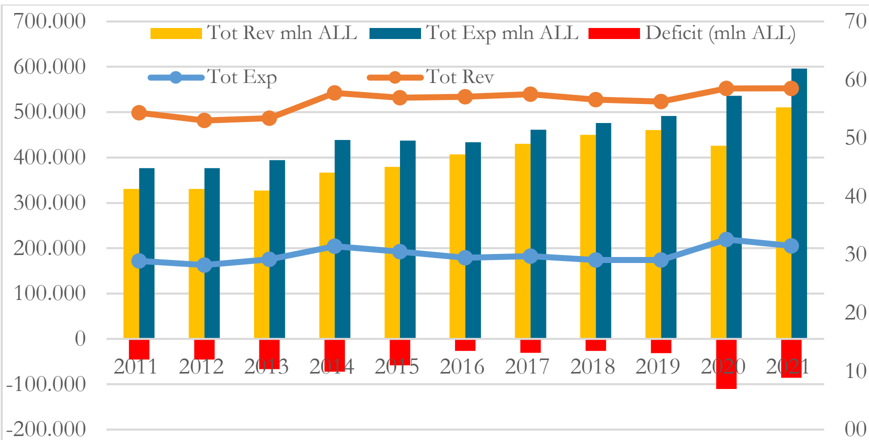

Figure 4: Public Revenue and Expenditure (in% of GDP)
Source: Albanian MoFE (2022)

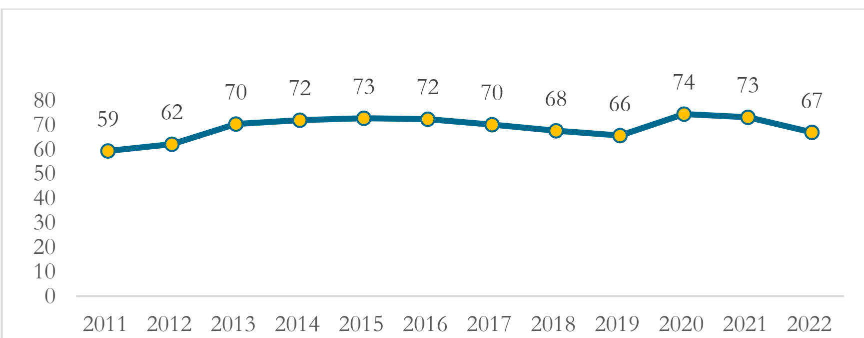

Figure 5: Public Debt (stock) % of GDP
Source: Albanian MoFE (2022)

As presented in Figure 4, public income does not exceed 30% of GDP, of which about 80% is collected from tax revenues, which are dominated by indirect taxes, namely 1/3 of the income is collected by Value added tax. If by 2013, public finances were based on resources such as privatization income, after this year the exhaustion of this source led to a higher attention of the government to mobilize internal future, though as seen from the graph above, weight Public income to GDP does not exhibit expected improvements, continues at about 27% of GDP, this is mainly explained by the complicated tax system in our country. On the other hand, in addition to the poor mobilization of income, there is also a budget of utilitarian functions, as about 60% of budget expenditures go for functions such as: social protection, education and health. While remains a very small portion of expenses to allocate to support priority sectors that will impact the business climate in the country. In summary, as reflected by the data above, Albania, as a developing country, is characterized by narrow fiscal spaces. The only instrument remains the debt for supporting public spending on the function of our spaces, which explains more than 10% increase in a decade, as illustrated in Figure 5.

4.2 Private financing

Albania is among the countries with low development of the financial system. As illustrated in Figure 6, its contribution to GDP has been below 3% over years and has marked a decreasing trend after 2017 from 2.9% of total economy value added to 2.5% in 2019 and 2.1% in 2020.

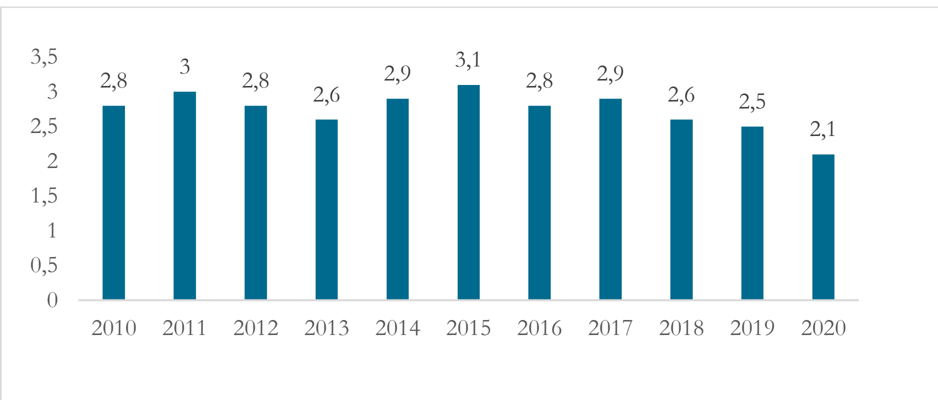

Figure 6: Contribution of financial sector % GDP
Source: INSTA and BoA (2022), author's calculation

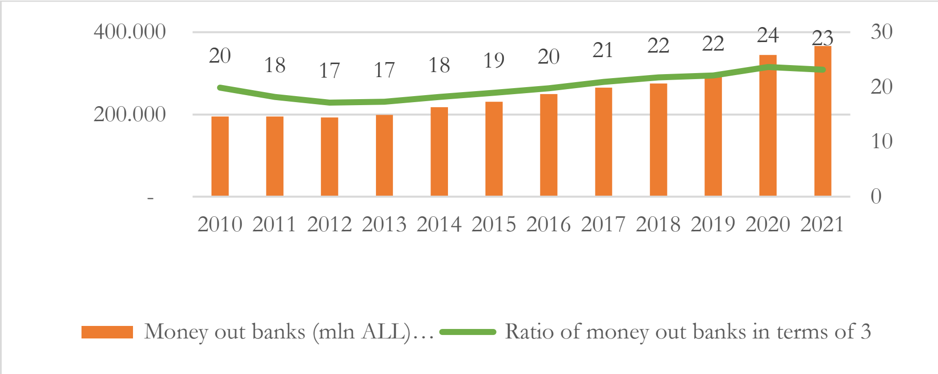

Figure 7: Ratio of Money outside Banks % of M3
Source: INSTA and BoA (2022), author's calculation

This low contribution of the financial sector in GDP, which remain less than 3% in 2021, is highly explained also by high weight of money outside depositary banks, which makes difficult to measure its effect on GDP. Considering, the ratio of money outside depository corporations with general money M3 it is observed that 30% of the money in Albania in 2021 results outside the banking system, an increasing trend after 2012 (21% in 2012), as shown in Figure 7. This demonstrates the presence of high financial resources for investment and support of economic developments.

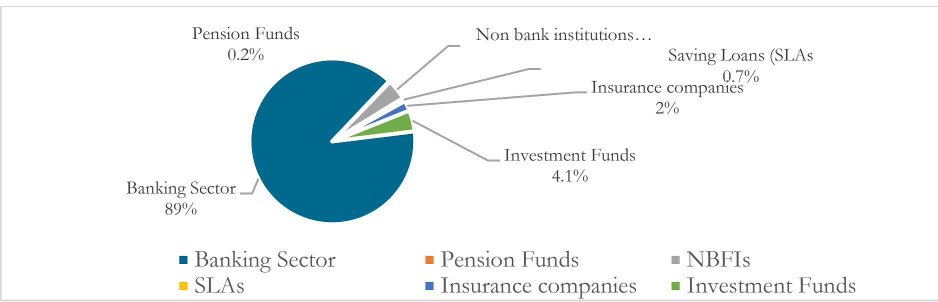

Figure 8: Share of financial system segments/ total assets of the financial system
Source: BoA (2022), Author's calculation

This shows that in a similar fashion to other developing countries, the banking sector in Albania has outpaced the growth of the equity and bond markets in the country. However, capital markets have a high potential to play in the long run a key role in the country's economy, in the long term. The financial market is dominated by banks. Despite having several types of financial institutions, about 90% of assets are possessed by banks, 4.1% by Investment Funds, 4% by non-bank financial institutions, 2% by Insurance companies, and others. While the Albanian Capital market is at an initial stage of development in terms of size of the market as measured by market capitalization, the ratio of market capitalization to GDP, volume and value traded of financial instruments. There is no public issuance of securities other than government bonds and a limited (but increasing) volume of privately placed bonds. The banking sector is a primary lending source for the economy. Banks remain the main debt-holder in the country, more than 60% of the total burden of the sovereign debt is held by them. Total credit to the economy (2021) is around 5.4 billion EUR or 35% of GDP. Businesses are the economic agents which hold the higher share of credits in the economy, 63% of credits is received by businesses sector, individuals have received 33% of credit and the rest of 4% is held by public sector. The sector with the largest weight of lending in the economy is in Private non-financial corporations, accounting for about 50 percent or about 3.2 billion EUR, composed by Wholesale and retail trade sector (17 percent or 1.1 billion EUR) followed by "Construction" about 8 percent, "Manufacturing industry" by 7 percent, "Electricity, gas supply, steam" by 4 percent, "Accommodation and food service" by 4 percent, "Other service activities" by 2 percent, etc. The loan according to the sectors does not match the priority government sectors, because the electricity or tourism represent a minor weight of crediting, even being a governmental priority policy.

5 Discussion and Conclusion

Presence of major challenging SDGs invites us (and emerging countries) to reformulate the approach followed until today and look not only at how to increase financial flows, but also how to work out on how to reduce the cost of achieving the SDGs. For this purpose, it should be considered not only how public funds can de-risk private finance, but also look for other ways to reduce risk. Therefore, some steps are suggested to achieve the following two objectives:

- Development Finance Assessment (DFA), which is designed to support countries to build a more integrated, public and private approach to financing through an INFF.
- To assist the process of achieving the SDGs, the Integrated National Financing Framework (INFF) is offered as a tool to help map the landscape

for financing sustainable development and design a strategy to increase and use as effectively as possible the all types of finance for sustainable development. Albania is still in the early stages, it has just started the process supported by UN Program.

The complex agenda involving EU accession, infrastructure and SDG needs requires innovation in the SDG financing. Although there is no proper study for Albania on the amount of financial resources needed to fulfill the SDGs, international assessments determine that a developing country faces an average annual financial gap of 2.5 trillion dollars. It demonstrates that SDGs appear unattainable, and countries should rely not only on new strategies for SDG budgeting, but also on how to reduce SDG financing costs. Emerging and developing countries need to focus more on developing and mobilizing private funding as the main potential to finance existing gaps in their SDG investment needs, while public finances should focus on policies that improve business environment, rather than directly to finance SDGs, because as illustrated in case of Albania, most of the State Budget supports a few SDGs, while most of them relies on private funding. The private financial sector, besides being underdeveloped in Albania, demonstrates that lending according to sectors does not correspond to priority government sectors, showing a lack of reconciliation of public and private finances. Unprecedented shocks and risks violate the achievement of SDGS at a limited time as defined on Agenda 2030, so developing countries should follow a full and rigorous process, from determining financing needs (DFA), SDG budgeting, design of a financing strategy (INF), implementation and monitoring of the strategy, predicting in any step potential risks that may violate the continuity of the process. To succeed in implementation of Agenda 2030 need to establish a roadmap for the SDG, identifying roles and responsibilities of the key institutions and other stakeholders in the process, and include financial implications deriving from the national commitment to the SDGs and ensure further mainstreaming of implementation alongside the national policies and strategies, including monitoring and reporting mechanisms.

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