

A World Bank Group Flagship Report

WORLD DEVELOPMENT REPORT
2022

**FINANCE
FOR AN
EQUITABLE
RECOVERY**

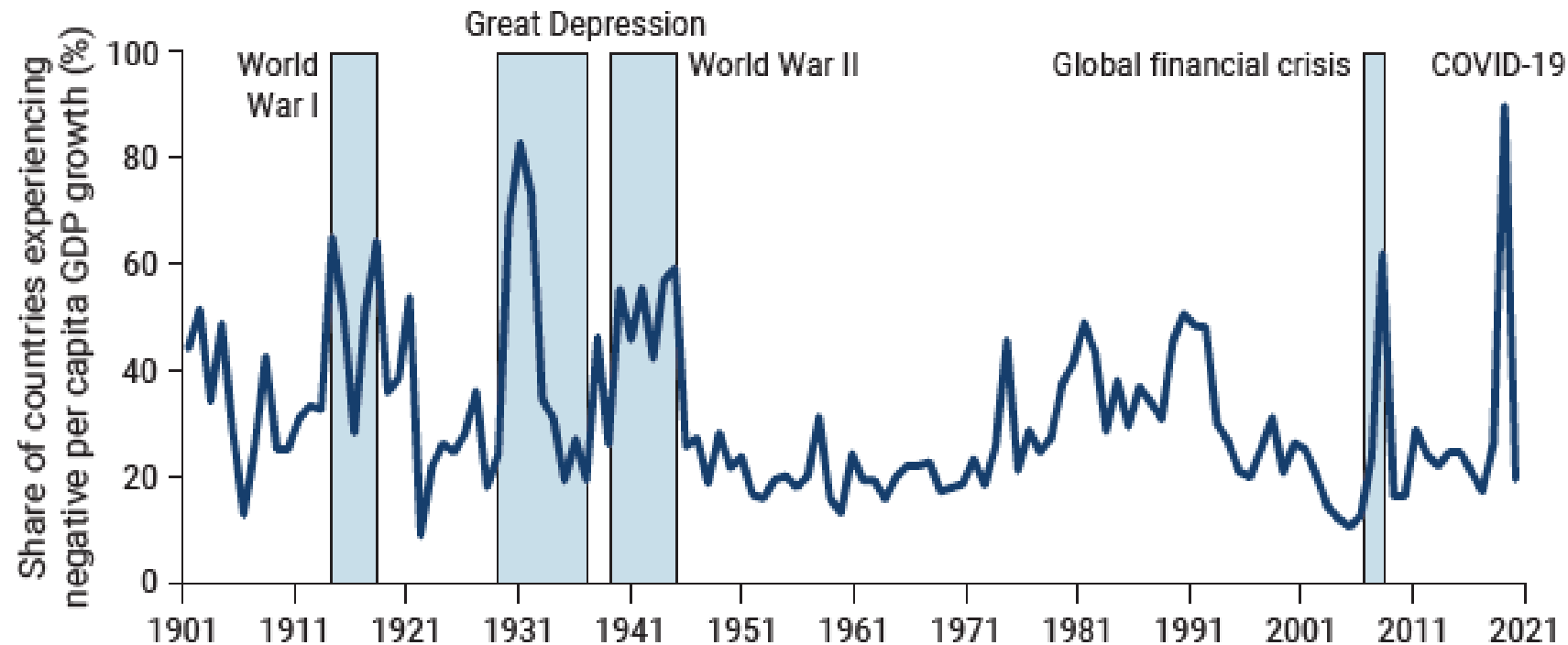
 WORLD BANK GROUP

COVID-19 caused a massive shock to output and income

In 2020, economic output contracted in 95% of countries

The economic impact of COVID-19: A historical perspective

Percentage of countries experiencing negative per capita annual GDP growth

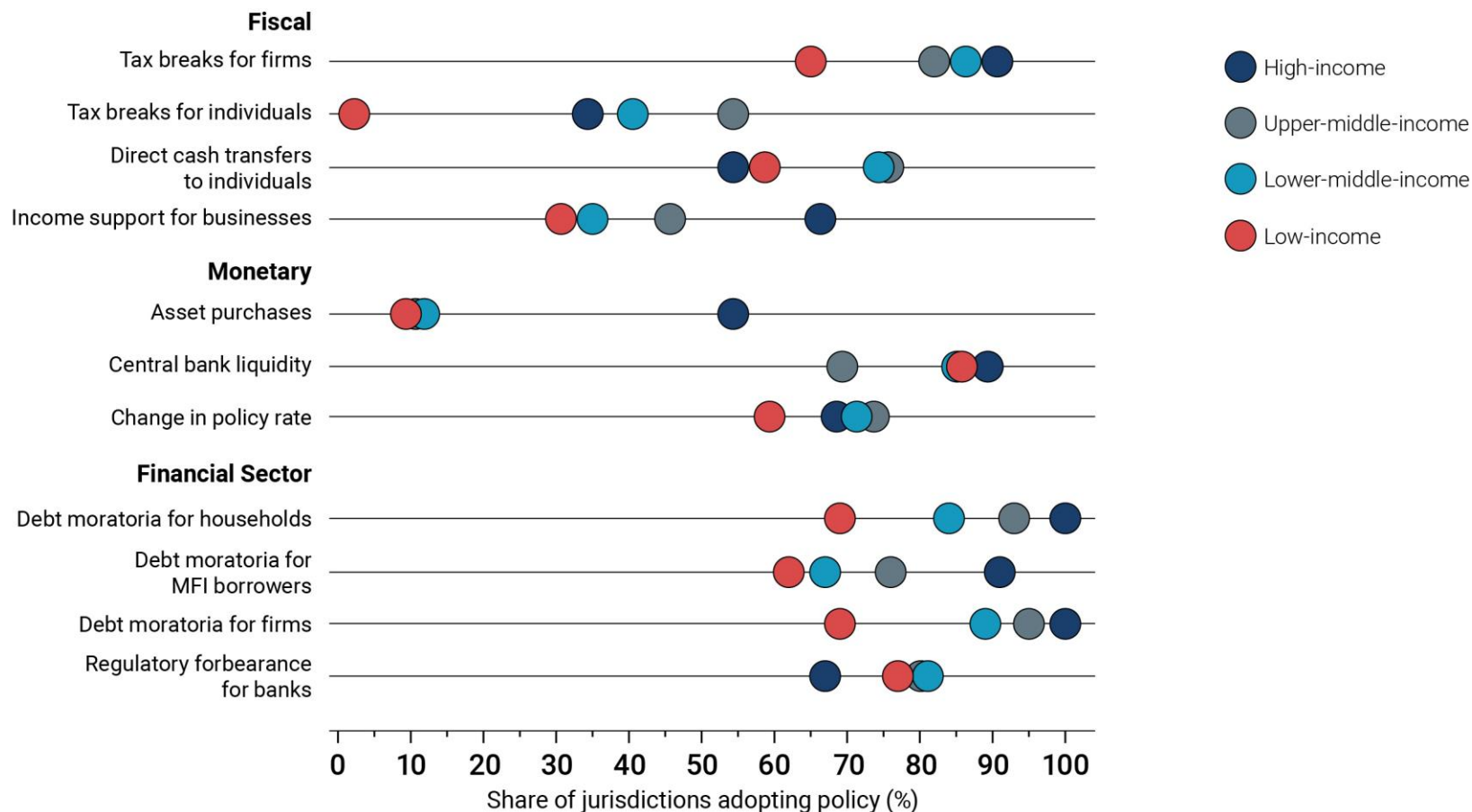


Source: Holston, Kaminsky, and Reinhart (2021) based on data from the IMF World Economic Outlook and the Maddison Project Database (2020).

Regulators implemented unprecedented measures

Which helped mitigate short-term impacts, yet also revealed longer-term risks

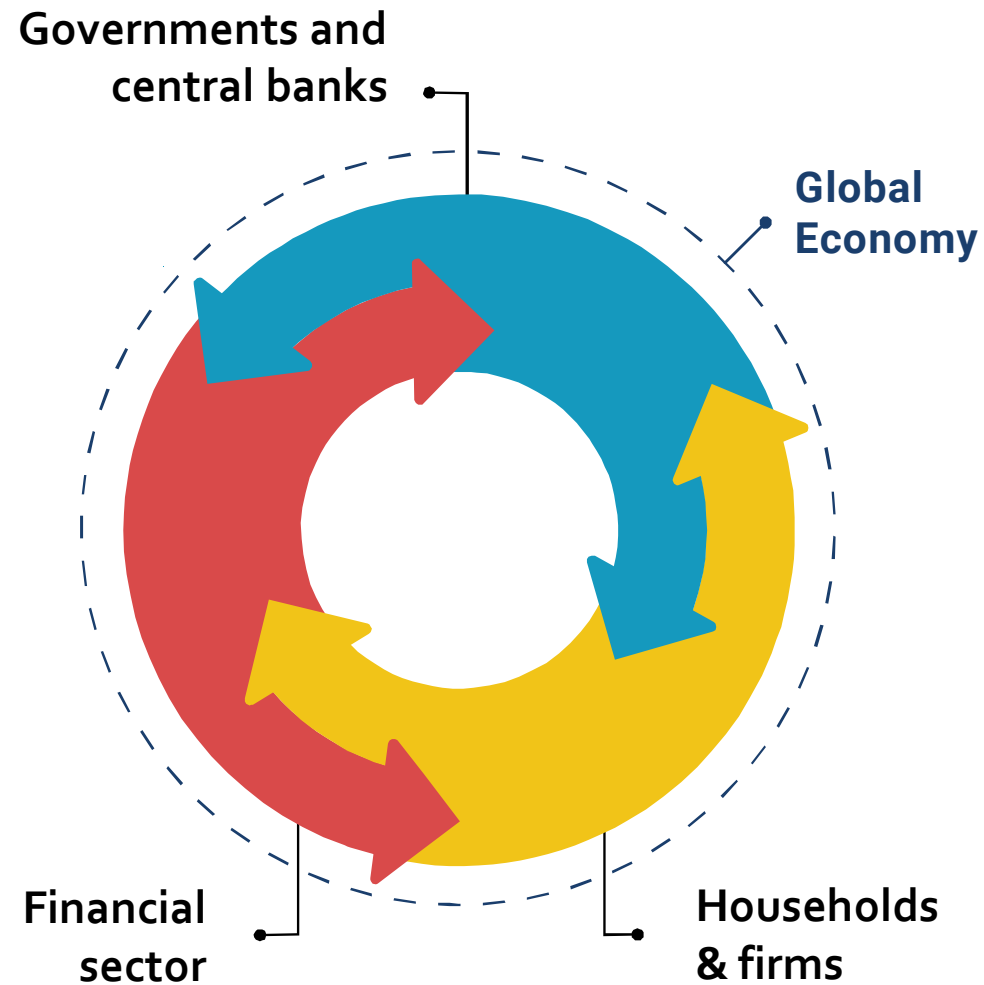
Fiscal, monetary, and financial sector policy responses to the pandemic, By country income group



Source: WDR22 World Bank Crisis Response Survey, 2021.

Note: The figure shows the percentage of countries in which each of the listed policies were implemented in response to the pandemic.

Economic risks – and strengths – accumulate due to interconnections between sectors



PRE CRISIS

COVID-19 PANDEMIC

CRISIS RECOVERY

Recommended: Timely action in four key policy areas

- Managing and reducing loan distress
- Improving the legal insolvency framework
- Managing increased levels of sovereign debt
- Ensuring continued access to finance

Risk: **Rising Non-Performing Loans**

Policy Priorities:

- Ensuring clear, consistent practices for reporting on asset quality
- Developing the capacity to manage nonperforming loans
- Dealing with problem banks swiftly

Risk: Delayed Resolution of Distressed Loans

Policy Priorities:

- Strengthening formal insolvency mechanisms
- Facilitating alternative dispute resolution systems such as conciliation and mediation
- Establishing accessible and inexpensive in-court and out-of-court debt resolution procedures for micro-, small, and medium enterprises
- Promoting debt forgiveness and discharge of natural person debtors

Spotlights: Focus on inclusive and sustainable finance

- Financial inclusion and financial resilience
- Strengthening the regulation and supervision of microfinance
- Supporting MSMEs and informal businesses through recovery requires concerted efforts to support MFIs
- Public credit guarantees to support MSME's, designed to mitigate the risks of moral hazard, politicization
- **Greening of capital markets: Issuance of sovereign sustainable bonds**

Risk: Elevated Levels of Sovereign Debt

Policy Priorities:

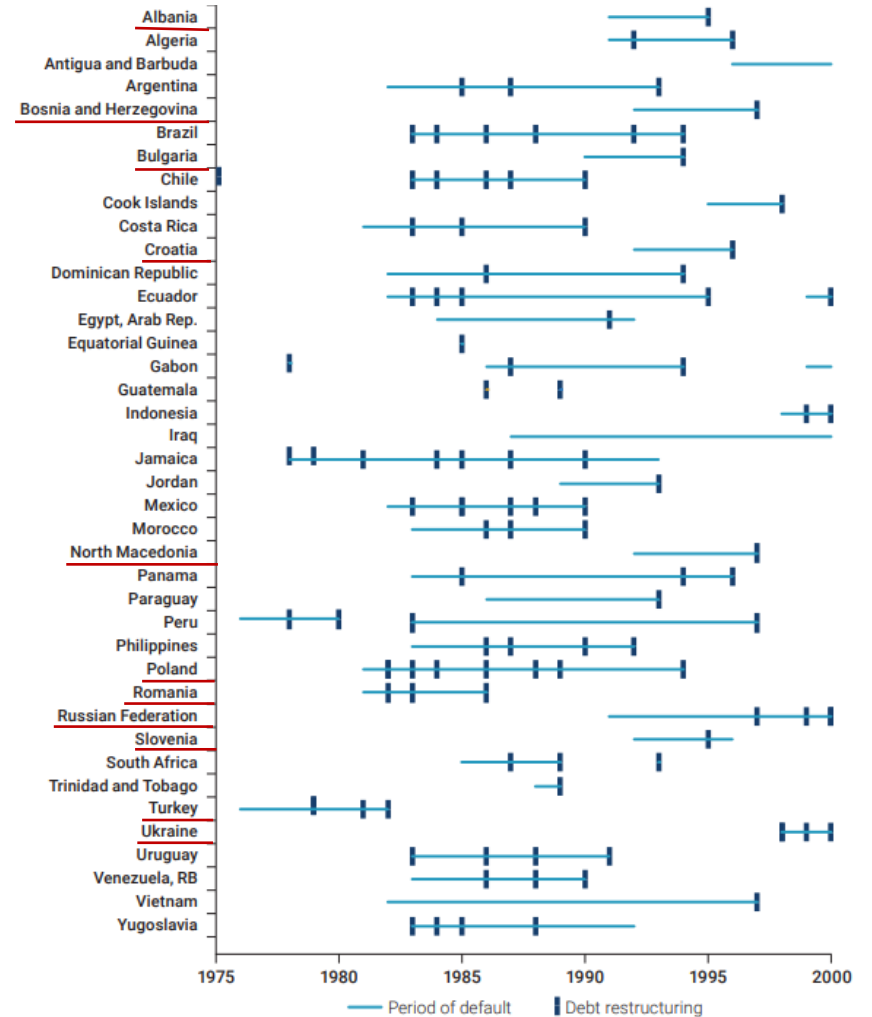
- Governments at high risk of debt distress can pursue proactive debt management approaches
- Governments in debt distress must coordinate with creditors to restructure debt
- Governments and their creditors can benefit from improvements in sovereign debt transparency
- Contractual innovations can help overcome coordination problems and speed up the resolution of unsustainable debts
- Well-developed tax policy and investments in tax administration can support debt sustainability in the longer run

Risk: Elevated Levels of Sovereign Debt

The importance of timely sovereign debt restructuring

- Evidence from past debt crises shows that the average default spell lasts eight years, and the indebted country typically goes through two debt restructurings before it emerges from default
 - Poland engaged in seven debt restructuring deals with private external creditors before resolving their default spell
- Postponing debt resolution efforts until economic conditions improve can deepen and prolong an economic downturn having a far-reaching social and economic consequences in which development goals suffer significant setbacks, delaying an equitable recovery
- Creditors and debtor governments should thus view debt restructuring as part of the initial resolution and recovery plan rather than as a subsequent step

Sovereign debt restructuring and time spent in default, selected countries, 1975–2000



Source: WDR 2022 team, based on Cruces and Trebesch (2013); Farah-Yacoub, Graf von Luckner, and Reinhart (2021); Meyer, Reinhart, and Trebesch (2019); Reinhart and Rogoff (2009).

Note: The figure shows a timeline of sovereign defaults and debt restructuring from 1975 to 2000. The figure excludes countries covered by the International Development Association (IDA) and the Heavily Indebted Poor Countries (HIPC) Initiative.

Risk: Elevated Levels of Sovereign Debt

Rwanda, HIPC Initiative success story

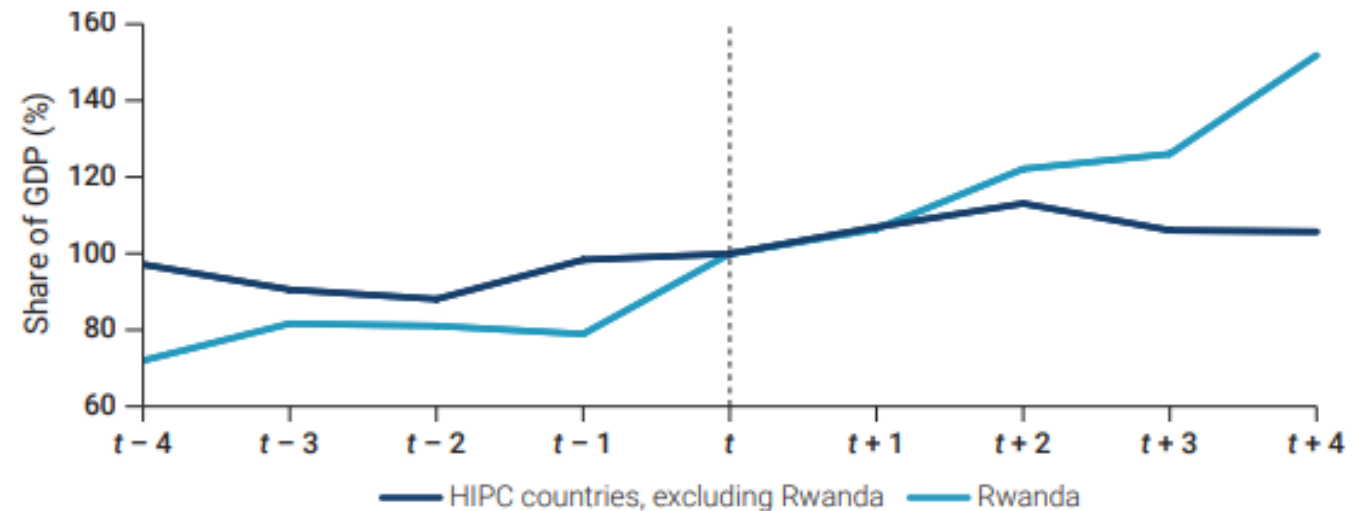
Rwanda used the HIPC Initiative, receiving full debt relief and committing to developing and implementing poverty reduction strategy in April 2005.

In the next 4 years, Rwanda increased poverty reducing expenditures by ~50%.

GDP per capita almost doubled, from \$465 in 2005 to \$849 in 2020, and the share of people living in poverty fell from 69% in 2005 to 56% in 2016.

However, Rwanda's external debt has been steadily increasing to levels close to the pre-HIPC number, putting it at a moderate risk of debt distress.

Debt relief is not sufficient to ensure long-term debt sustainability.



Source: IMF and World Bank 2019.

Note: In the figure, t represents the year of the completion point (full debt relief received). The data for year t are normalized to 100. The other years should be read in reference to this. GDP = gross domestic product; HIPC = Heavily Indebted Poor Countries (Initiative).

Risk: Elevated Levels of Sovereign Debt

The case of Benin

Proactive debt management by effectively combing and optimizing commercial funding and financing instruments from international financial institution, helped Benin meet the urgent financing needs of COVID-19

- In response to the growing financing needs during the COVID-19 pandemic, Benin reentered the bond market and mobilized €1 billion by issuing a new Eurobond in January 2021
- In 2018, it obtained a commercial loan for €260 million (\$312 million) through the World Bank's Policy-Based Guarantee and bought back shorter-term domestic debt.
- In July 2021, Benin issued Sovereign Sustainable Development Goals (SDGs) Bonds which mobilized €500 million (\$600 million) to be used towards the achievement of SDGs.

Opportunity: Leverage Tech to Improve Access to Credit

Policy Priorities

- Creating an enabling environment to leverage alternative data
- Embracing responsible innovations in product design and embedded finance
- Providing well-tuned guarantee programs
- Advancing the regulatory framework and financial infrastructure

Risk: Tighter Access to Credit

Financial sector was showing strong signs of recovery as of late 2021.

Insights from survey of 197 IFC client financial institutions – Nov/Dec 2021

61% Lending returned to pre-crisis levels

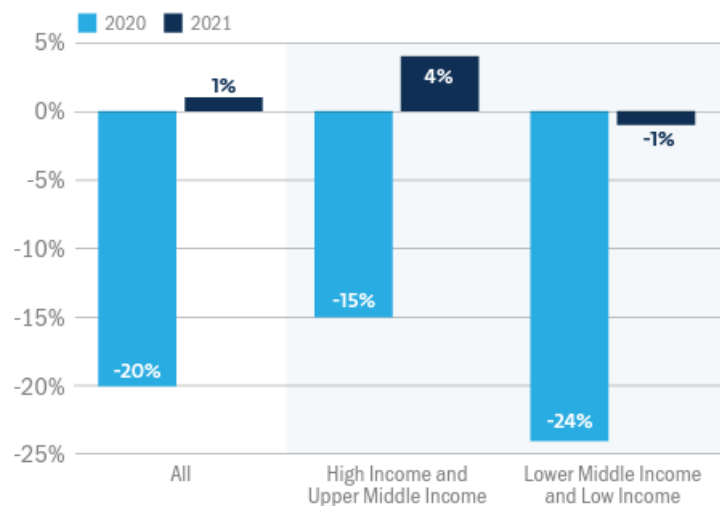


FIGURE 1 Change in average loan disbursement levels across institutions (2019–2021)

51% Reported collection levels still affected

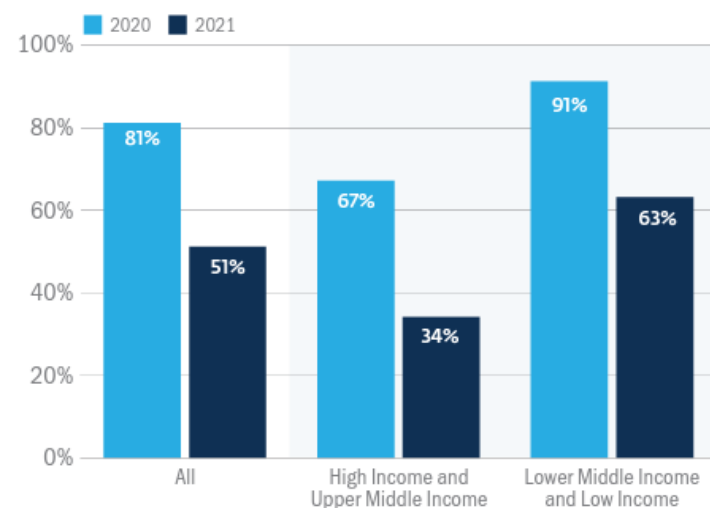


FIGURE 3 Change in the share of institutions with collections below pre-crisis levels (2019–2021)

1.2p Avg. increase in NPL (+25%, Jun 19-Jun 21)

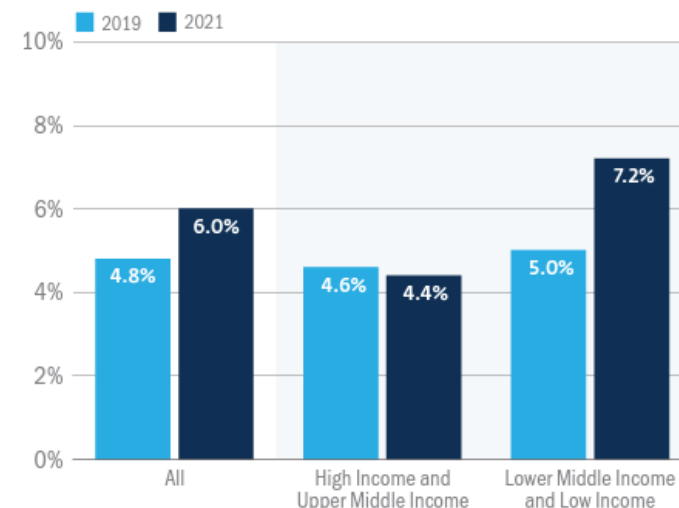


FIGURE 4 Change in average nonperforming loan rates across institutions (2019–2021)

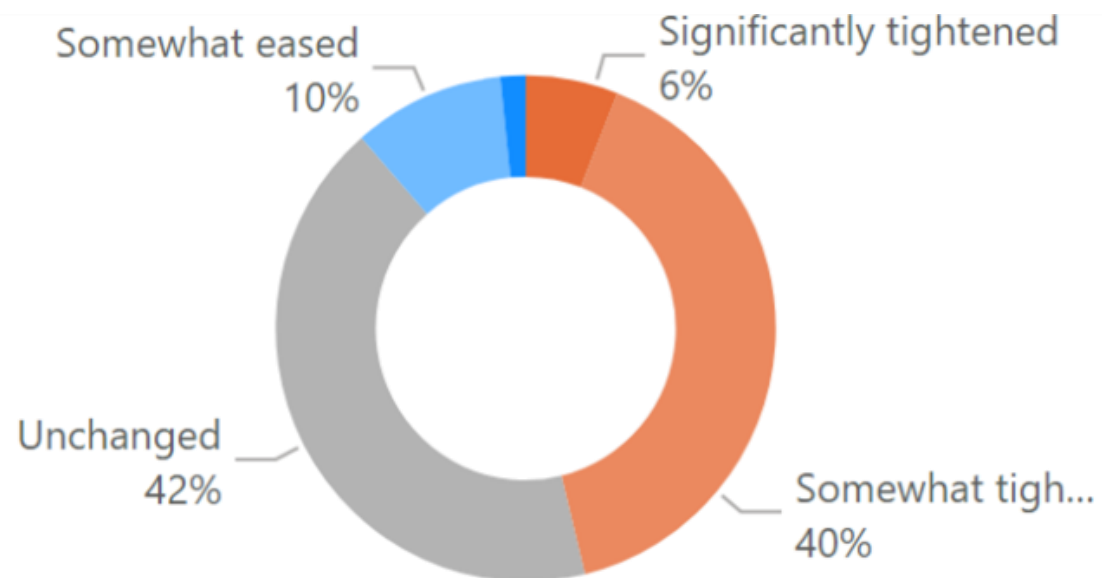
Risk: Tighter Access to Credit

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CHANGE IN CREDIT STANDARDS

(Share of institutions, change in standards compared to precrisis)



TOP FORMS OF CREDIT TIGHTENING

INCREASING COLLATERAL REQUIREMENTS	55%
REDUCED AMOUNTS	38%
REDUCED UNSECURED LENDING	36%
INCREASE OTHER APPLICATION REQ.	34%

TOP CHALLENGES FOR REACHING MSMEs

RISKY BUSINESS OUTLOOK	49%
IMPACT OF LOCK-DOWNS ON SMEs	44%
DIFFICULTY IN CREDIT ASSESSMENT	34%
LOW QUALITY OF COLLATERAL	34%

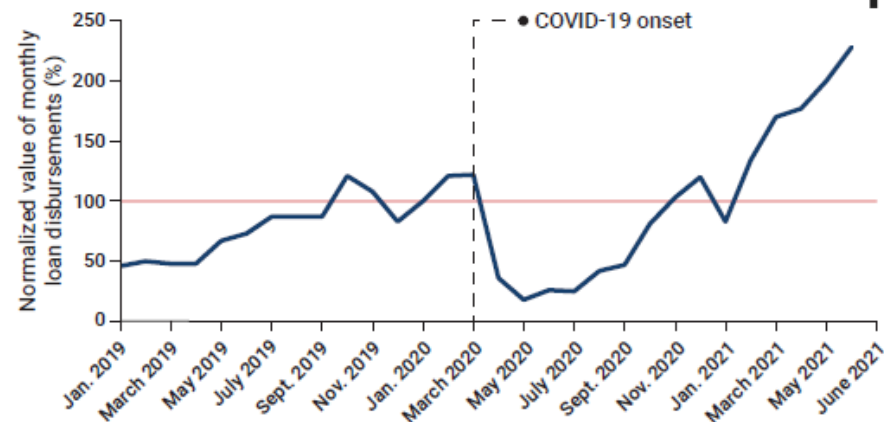
Opportunity: Leverage Tech to Improve Access to Credit

	Improve visibility	Strengthen recourse	Reduce risk
Risk measurement			
Alternative data	●	○	○
Enhanced analytics	●	○	○
Product choice and design			
Loan tenor	●	○	○
Secured credit	◐	◐	○
Embedded finance	●	◐	◐
Supply chain finance	◐	◐	◐
Insuring risk			
Credit guarantees	○	●	●

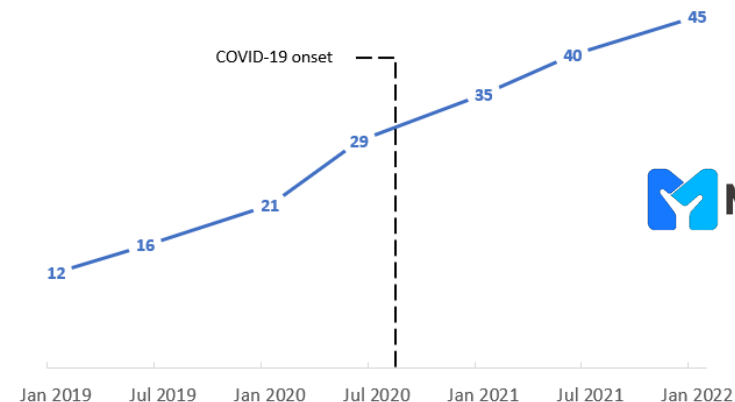
Source: WDR 2022 team.

Note: Shaded circles indicate the increasing relevance of each solution for the respective challenge, from not applicable (○) to degrees of relevance (◐◑◒) to highly relevant (●).

Figure B4.1.1 Growth in loan disbursements by Konfio, 2019–21



Cumulative # of SME served by MYBank, 2019-2021 (millions)



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Further questions or comments are welcome -
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