

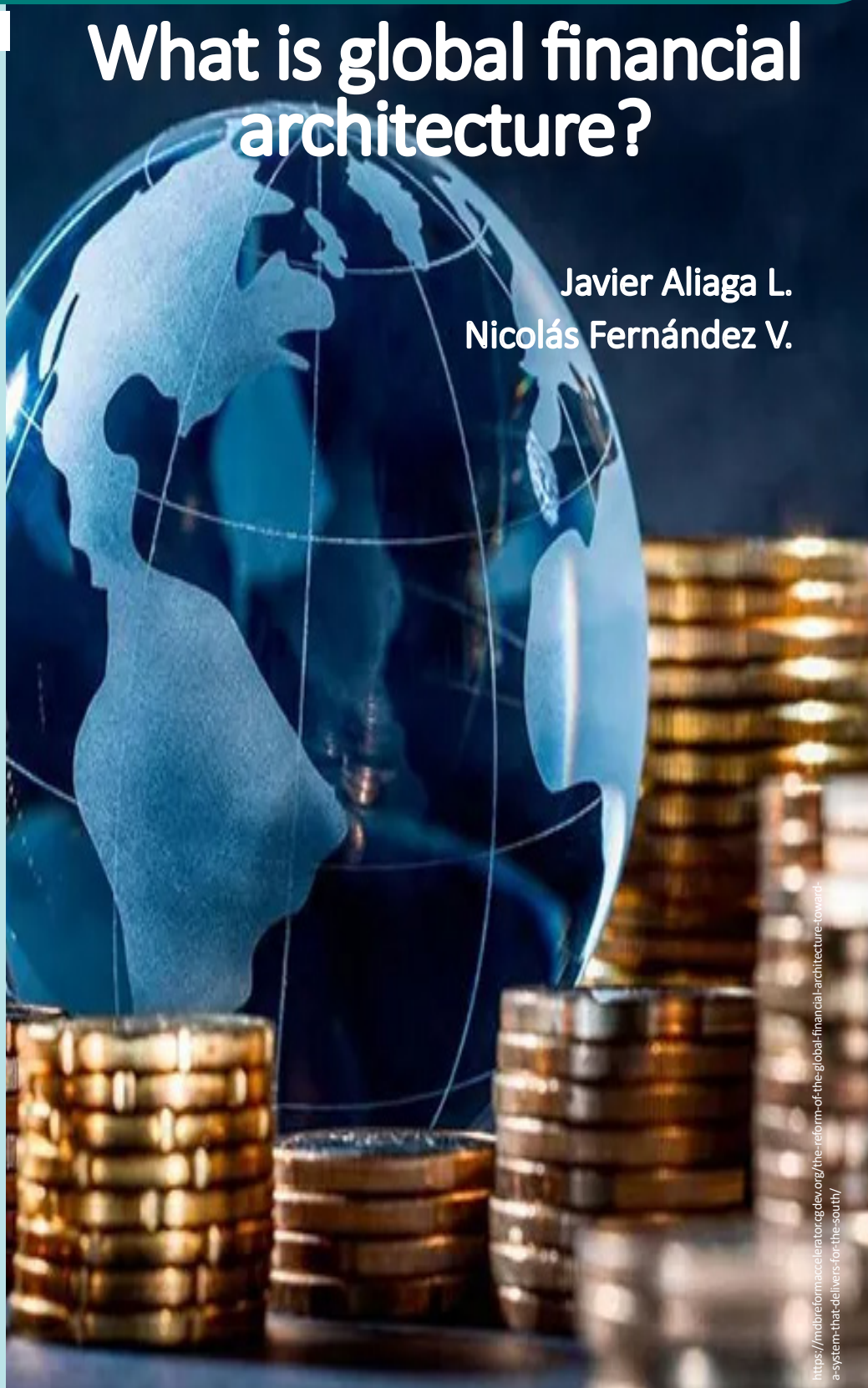


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What is global financial architecture?

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Global financial architecture is made up of a group of institutions that play a key role in regulation and support of the international financial system. Among these institutions is the International Monetary Fund (IMF) and the World Bank – entities that emerged following the Second World War as pillars of the Bretton Woods system – which have the mandate of promoting macroeconomic stability and development. Together with these institutions, the multilateral development banks, such as the Inter-American Development Bank (IDB), the African Development Bank (AfDB) and the Asian Development Bank (ADB), provide financing and technical assistance to their member countries. In recent decades, new actors such as Asian Infrastructure Investment Bank (AIIB), and the New Development Bank of the BRICS countries have expanded the institutional spectrum, an indication of the growing role of emerging economies.

In terms of the present financing mechanisms, the IMF operates mainly providing emergency loans, lines of contingency loans and extended

financing agreements, aimed at stabilizing economies with balance of payments trouble or debt crises. On its part, the World Bank and the multilateral development banks channel resources to projects in infrastructure, health, education, and climate change by means of loans, guarantees, subsidies, and financing under concessional conditions. Besides, there are specialized funds such as the Green Climate Fund and the Global Environment Fund, designed for mobilizing resources for climate action, though their scale has been insufficient in the face of the growing needs of developing countries.

Albeit, these mechanisms face considerable challenges: the resources available do not allow covering the financing gaps estimated for complying with the Sustainable Development Goals (SDGs) and the Paris Agreement. Also, criticism persists on the conditional nature of IMF loans and the excessive influence of the advanced economies in the governance of these institutions, which limits their response capacity in terms of the true needs of the most

vulnerable countries. This has prompted a global debate on the need for reforming financial architecture for it to be more inclusive, equitable and capable of mobilizing resources at the scale and speed demanded by the present context.

The global financial system should enable sustainable economic growth, poverty reduction and the financing of global public goods such as climate action. However, the system has shown persistent flaws that generate instability, inequality and vulnerability, particularly in developing countries. The present article examines the main challenges faced by international financial architecture and proposes lines of action that are presently under debate in multilateral forums with a view to reforming the system.

What structural problems does development financing face?

Systemic instability: The 2008 global financial crisis unleashed by the collapse of Lehman Brothers revealed that the

The G7 economies hold more than 40% of the voting power in the IMF, which reduces the influence of low- and middle-income countries in lending decisions.

excessive interrelationship of markets generates systemic risks. According to Minsky (1986), the hypothesis of financial instability holds that prolonged periods of boom foster speculative indebtedness, thus increasing the system's vulnerability to shocks. The theory of financial networks reinforces this view: a collapse in a central node can cause a domino effect, as was the case in the crisis of the assets supported by subprime mortgages.

Inequality in access to credit: Unequal access to financing is another expression of the system's flaws. In Sub-Saharan Africa and rural areas of Latin America, financial exclusion is persistent. Stiglitz and Weiss (1981) explain that asymmetry of information leads to credit rationing: in order to avoid risk, banks restrict the availability of loans for those who need them most, thus expanding the inequality gap. This phenomenon not only hinders development of the local private sector, but also perpetuates dependency on external financing.

Capital flight and illicit financial flows: Illicit financial flows (IFFs) and tax avoidance strategies through the use of tax havens (such as large technology companies employing offshore structures) erode national tax bases. Zucman (2015) shows that the wealth hidden in tax havens distorts the designation of global savings, undermines equity and weakens



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the capacity of States to finance public policies. This causes particular concern in developing economies, where the mobilization of internal funds is essential for reaching the SDGs.

Volatility capital flows: The recent foreign exchange crises in Turkey (2018) and Argentina (2018-2019) illustrate the risks associated with capital flow volatility. According to Calvo et al. (1996), emerging countries are vulnerable to "sudden stops": the abrupt reversion of flows that cause depreciation, inflation and recession. Such volatility reflects flaws in global coordination, lack of effective preventive tools, and an insufficient international regulatory framework.

Over-indebtedness: The accumulation of sovereign and private debt poses risks for macroeconomic stability. Reinhart and Rogoff (2010) have documented the fact that high levels of debt are associated with lower growth and greater likelihood

of financial crises. Recent examples, such as Ghana's over-indebtedness (where debt payment made up over 50% of fiscal income in 2023) show how lack of structural solutions provide temporary relief, but perpetuate the cycle of financial crises and bailouts.

Regulatory challenges of new technologies: The collapse of FTX in 2022 exemplifies how lack of regulation in the domains of crypto-assets and fintech can lead to fraud, collapses and systemic risks. Financial innovations surpass the capacity of regulators, generating gaps that translate into losses for small investors, and potentially confidence crises in markets.

Concentration and market power: The concentration of power in large banks and funds ("too big to fail") and the predominance of the Big Four in auditing generate moral hazard risks. According to the theories of monopolies and oligopolies (Bain, 1956), these structures

limit competition, raise costs for users and increase the likelihood of public bailouts in cases of crises.

Credit ratings: They play a pivotal role in influencing the cost and availability of external financing for countries. Rating agencies such as Standard & Poor's, Moody's and Fitch, assess the credit risk of debt-issuing countries, and their opinions directly affect the interest rates that these countries face in international markets. For many developing countries, a low rating implies greater indebtedness costs and limited access to capital under favorable conditions, which can perpetuate dependency on costly financing and hinder investment in sustainable development. Besides, these ratings tend to be pro-cyclical: they tend to worsen in periods of crisis, thus aggravating conditions in countries by further increasing the cost of credit precisely when they need it the most. In this sense, the concentration of power in these agencies and the lack of transparency as to their methodologies has generated growing criticism, underscoring the need for reforming the rating system for it to be fairer and adequately reflect the realities and structural challenges of the most vulnerable countries (UNCTAD, 2025; IMF, 2025).

It is not enough to simply spend more: the real challenge is to direct every dollar toward projects that generate productivity and foreign exchange, avoiding crowding out and closing structural gaps.



Crowding out, expenditure quality and strategic alignment of financing

A critical aspect of the design of development financing strategies is to avoid the crowding out phenomenon between public and private investment. This occurs when the expansion of public investment absorbs resources — capital, land, scarce inputs — which would otherwise have been employed by the private sector, thus reducing the latter's capacity to contribute towards economic development. In the context of the Global South, this is observed in economies where the public sector prompts large-scale projects under inadequate coordination with the private sector.

The need for improving expenditure quality

Increasing the volume of financing does not suffice; an improvement in expenditure quality is needed. This implies prioritizing high-productivity projects and generating foreign currency; avoiding concentrating expenditure in non-tradable sectors that create bottlenecks in the balance of payments; ensuring impact assessment and cost-

effectiveness mechanisms; reducing physical costs and the costs of transition by means of planning frameworks, reducing infrastructure cost overruns and resource waste.

Derisking and alignment of financing terms

Reducing risks (derisking) for attracting private capital for sustainable development projects is fundamental. Notwithstanding, this must be done in such a way that reduces transition costs (for example, supporting the reconversion carbon intensive industries without generating mass unemployment or social tension); coordination of short-, medium- and long-term financing instruments: short-term green financing centered on immediate mitigation and adaptation projects, aligned with the NDCs (Nationally Determined Contributions); sustainable medium- and long-term financing aimed at supporting long-term strategies (long-term decarbonization and sustainable development strategies); very long-term financing for biodiversity and positive nature focused on conserving and restoring ecosystems, in alignment with the Kunming-Montreal Global Biodiversity Framework.

What challenges exist for mobilizing resources at the large scale?

Financing gaps for the SDGs

The financing gap for reaching the SDGs is one of the most critical challenges of global financial architecture. According to recent OECD (2025) and UNCTAD (2025) estimates, the annual deficit is over 4.3 trillion dollars, which increased compared to the 2.5 trillion estimated prior to the pandemic. The interrelated crises – the pandemic, climate change, geopolitical conflicts – have increased investment needs, and at the same time limited the capacity of many countries for mobilizing internal resources or accessing external financing under fair conditions.

The financing that is mobilized poses issues in terms of quantity and quality. A considerable part of the financial flows aimed at sustainable development are in the form of loans that increase the debt burden of vulnerable countries. This limits their capacity to invest in sectors such as health, education, sustainable infrastructure, and climate resilience (Brookings Institution, 2024). Subsidies and concessional instruments are still insufficient, underscoring the need to redesign the global financial mechanisms.

Table 1. Financing indicators

Indicator	Estimate prior to the pandemic	Present (2025) estimate
Annual gap in financing the SDGs	USD 2.5 trillion	USD 4.3 trillion
Climate financing pledged	USD 100 billion	Not fulfilled (in 2023, only USD 83.3 billion)

Source: Own preparation with OECD and UNCTAD data

Closing this gap demands a transforming approach which combines public, private and multilateral resources in a strategic way. Although there are promising initiatives – such as green bonds, debt-for-nature swaps, and climate guarantee funds – they continue to represent a marginal fraction of the financing needed. It is indispensable for the reforms of global financial architecture to mobilize capital at a large scale and direct it towards the SDGs with criteria of equity and sustainability (UNCTAD, 2025).

Institutional and political obstacles

Institutional and political obstacles limit the effectiveness of efforts for financing sustainable development. The governance of global financial institutions such as the IMF and the World Bank continue to show an imbalance of power in favor of the advanced economies. For

example, the G7 economies control over 40% of votes at the IMF, while low- and middle-income countries have scant representation (IMF, 2025). This situation restricts the capacity of developing countries to influence the decisions that directly affect their access to financing and the associated conditions.

Lack of political will on the part of the principal donors is also a hindrance. Despite repeated promises, the commitment to mobilize 100 billion dollars annually for climate financing has not been fully realized: in 2023 the amount reached was approximately 83.3 billion. International negotiations progress slowly, dominated by short-term interests and national agendas, which hamper the creation of more agile instruments adapted to the needs of developing countries (Reuters, 2025a).

Table 2. G7 control in international institutions

Institution	% of votes controlled by the G7	% of votes controlled by low-income countries
IMF	42%	< 10 %
World Bank (IBRD)	39%	< 12 %

Source: Own preparation with IMF data

The global gap of USD 4.3 trillion per year to meet the SDGs requires the coordination of public, private, and multilateral capital based on criteria of equity and sustainability.

Promises to contribute USD 100 billion annually for climate action remain unfulfilled: in 2023, only USD 83.3 billion was disbursed, evidence of the lack of political will to scale up resources.

On the side of the receiving countries, internal institutional limitations, such as weak regulatory frameworks, low administrative capacity and governance problems obstruct the absorption and efficient use of external resources. This feeds a vicious circle where lack of trust on the part of donors and investors limits financing, which in turn inhibits the strengthening of local institutions (OECD, 2025). Overcoming these obstacles requires sustained investment in institutional development and in strengthening technical and regulatory capacities.



The roles of donor and receiving countries

Donor countries play a key role in reforming global financial architecture. It is they who have concentrated in their hands the resources and political weight needed for fostering significant changes. However, their contributions have been fragmented and insufficient, and in many cases conditioned to strategic or geopolitical interests. The

fulfillment of financial pledges – such as support for climate action or sustainable development – must go from being a declaration of intent to a verifiable reality, through applying additional quality resources (greater proportion of subsidies and concessional loans) (Milken Institute, 2025).

On their part, the receiving countries face the challenge of strengthening their institutional and governance frameworks for maximizing the impact of resources



obtained. This includes improving project planning and execution, ensuring transparency in the use of funds, and aligning external financing with the own development priorities. Only thus will fragmenting of efforts be avoided, as well as the risk of excessive dependency on external financing (IDB, 2025).

Finally, the dialogue between donors and receivers must transform into a relationship of veritable cooperation and trust. This implies progressing towards a new global financing pact based on co-responsibility, with respect for the priorities of developing countries and seeking innovative solutions jointly. Financial reforms must come with

clear commitments in terms of fiscal justice, trade, and technology transfer, so that financing is able to contribute development that is inclusive and sustainable (E3G & Mistra, 2024).



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