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Governance and institutional perspectives on strengthening resource mobilization for the Sustainable Development Goals

Improving public resource mobilization through public financial management reform, fiscal decentralization and innovative development finance

Note by the Secretariat

The Secretariat has the honour to transmit to the Committee of Experts on Public Administration the paper coordinated by Committee members Paul Smoke and Mauricio Rodas in collaboration with fellow Committee members Rolf Alter, Adeyemi Dipeolu, Pamela Mbabazi and Pamela Monroe Ellis.

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Improving public resource mobilization through public financial management reform, fiscal decentralization and innovative development finance

Summary

The current global context of unprecedented debt levels, increasing deficits and weak economic performance in many countries is compelling Governments to revisit and adjust their fiscal frameworks to support effective and sustainable development. A broad and complex range of governance and institutional structures and processes substantially influence how governments mobilize and use resources for inclusive development. The present paper covers three areas essential for financing and implementing the Sustainable Development Goals while strengthening trust and public participation in government.

At the national fiscal and financial level, it is essential that resilience be swiftly improved in fiscal policy frameworks by reorienting public financial management towards Goals-related outcomes, priorities and value for money while reconciling short-term stabilization goals with long-term sustainable development and climate commitments. Also crucial is the enhancement of the legal and operational independence of supreme audit institutions within the public financial management ecosystem to ensure objective financial oversight and credible reporting.

Another fundamental measure for improving Sustainable Development Goal finance and governance is to expand the engagement of subnational governments, which have inherent advantages in promoting local development and are often underutilized. Many countries could productively improve subnational authority and capacity to raise and spend revenues in the context of a well-structured fiscal, institutional and managerial framework that includes strong public financial management performance and subnational government accountability incentives.

A third urgent avenue for action is to increase the volume and improve the allocation of finance for sustainable development investment needs. National public resources and international development assistance will not meet the large and growing global infrastructure investment gaps. Reforms must increasingly attract private capital and deploy innovative mechanisms to ease and share risk and create incentives for borrowers and lenders. Special attention to climate-change response and other global priorities is vital for Goals-related investments at both the national and subnational levels.

I. Introduction

1. Resource mobilization is a foundational element of government performance and for meeting the Sustainable Development Goals globally. A broad and complex range of governance and institutional structures and processes substantially influence how governments mobilize and use resources for inclusive development. The present paper covers three areas that are essential but that might not receive sufficient consideration: selected essential aspects of national fiscal policy and financial management; intergovernmental and subnational public finance and financial management; and innovative development finance mechanisms.

II. Selected essential aspects of national fiscal policy and financial management

2. Much attention has been given by the United Nations financing for development process and a broad range of other global policy initiatives, international development agencies and international finance institutions to the critical importance of improving national resource mobilization and public financial management. The present section covers selected issues that merit additional attention, namely, introducing resilience into fiscal policy frameworks and enhancing the role of supreme audit institutions.

A. Introducing resilience into fiscal policy frameworks

3. Most policymakers and researchers agree that fiscal discipline is necessary for dealing with high and rising public debt and for maintaining fiscal space to be able to react to shocks. In response to calls for discipline, an increasing number of countries have over the past two decades adopted rules-based fiscal frameworks, including both numerical fiscal rules and fiscal institutions, such as fiscal councils, to oversee compliance.

4. Public finances in most countries face an unprecedented dual pressure challenge:[1] Governments must restore fiscal sustainability while simultaneously responding to multiple overlapping crises, heightened geopolitical and geoeconomic uncertainty and escalating demands for the provision of Goals-related public goods and services. These demands also reflect the structural requirements of the climate transition and the implementation of the 2030 Agenda for Sustainable Development. Investments in climate mitigation and adaptation, resilient infrastructure, social inclusion, human capital and security increasingly shape expenditure profiles and fiscal risks, while returns materialize over long time horizons.

5. Some conventional efforts to enhance fiscal discipline, such as across-the-board expenditure cuts or calls to do more with less, are ill-suited to the scale, urgency and intergenerational nature of the 2030 Agenda and the climate agenda. A World Bank initiative known as “Reimagining public finance: making public resources work for development outcomes” underscores the need to reorient public financial management towards outcomes, prioritization and value for money.[2] The current dual

[1] Organisation for Economic Co-operation and Development (OECD), “Sustainability of public finance in OECD countries: from fiscal consolidation to State redesign?”, OECD Papers on Budgeting, Vol. 2025/12, (Paris, 2025); OECD, *Resilient Growth but with Increasing Fragilities*, OECD Economic Outlook, Volume 2025/2, (Paris, 2025).

[2] Tim Williamson and others, “Reimagining public finance – clarifying the agenda”, IMF PFM Blog, 17 November 2025.

pressure challenge necessitates fiscal frameworks that can reconcile short-term stabilization objectives with long-term development and climate commitments.

6. Key reform priorities therefore include reducing the rigidity of public spending, enabling timely reallocations and institutionalizing continuous reprioritization across policy objectives. Such reprioritization is central to the achievement of the Goals, as progress depends on managing trade-offs (e.g. between social protection and fiscal consolidation) while exploiting synergies (e.g. between climate action, health outcomes and job creation). These reforms must be underpinned by institutional and procedural changes that firmly embed resilience, foresight and risk management into fiscal policymaking and the broader policy cycle.

1. Revisiting rules-based fiscal frameworks through a Sustainable Development Goal and climate lens

7. The redesign of fiscal frameworks requires the reassessment of existing rules and institutions, not only in terms of debt sustainability and macroeconomic stabilization, but also in terms of their compatibility with long-term Goals delivery and climate transition pathways.

8. Rules-based fiscal frameworks, which combine numerical fiscal rules with institutions such as fiscal councils, spending reviews and courts of audit, have been widely adopted to enhance fiscal discipline and credibility. However, many of these frameworks were designed in an era when fiscal risks were more narrowly defined and when climate-related liabilities, transition costs and contingent risks were not systematically integrated into fiscal planning.

9. Fiscal rules, by imposing numerical constraints on deficits, expenditures or debt, can help to anchor expectations and discipline policymaking. Empirical evidence suggests that well-designed rules can mitigate procyclical behaviour and improve fiscal outcomes.[3] Nevertheless, rigid rule designs can constrain the capacity of Governments to scale up green investment, climate adaptation spending or social protection in response to shocks, which are areas central to achieving multiple Goals.

10. The widespread revision of fiscal rules since the pandemic illustrates their limitations and their adaptability. More reliance on escape clauses has allowed Governments to respond to crises, including those related to climate shocks and energy price volatility. Yet the absence of clearly defined pathways to compliance risks crowding out long-term development and climate investment if adjustment pressures fall unduly on capital spending or preventive measures.

11. Correction mechanisms play a crucial role in aligning fiscal discipline with sustainable development objectives. Well-designed mechanisms can support gradual, predictable adjustment paths that protect priority Goal- and climate-related expenditures, rather than forcing abrupt consolidation. However, the limited prevalence of such mechanisms, particularly in emerging and low-income economies, raises concerns about their ability to manage climate-related fiscal risks and maintain investment levels consistent with development needs.

12. Links between fiscal rules and medium-term fiscal frameworks are especially important from a Goals perspective. Medium-term fiscal frameworks provide the natural entry point for integrating climate strategies, nationally determined

[3] Julien Acalin and others, “Fiscal rules, robust correction mechanisms, and sovereign spreads”, International Monetary Fund (IMF) working paper 25/195 (Washington, D.C., 2025); Virginia Alonso and others, “Fiscal rules and fiscal councils: recent trends and revisions since the pandemic”, IMF working paper 25/198 (Washington, D.C., 2025); Julien Acalin and others, “Fiscal guardrails against high debt and looming spending pressures”, IMF staff discussion notes 2025/004 (Washington, D.C., 2025).

contributions and Goal targets into fiscal planning. When such frameworks are weak or disconnected from fiscal rules, Governments struggle to translate long-term commitments such as net-zero targets or adaptation strategies into credible, funded expenditure paths.

13. Although design features such as escape clauses and legislative anchoring have improved flexibility, compliance remains uneven. In practice, repeated suspensions of fiscal rules without transparent adjustment strategies risk undermining both fiscal credibility and the credibility of climate and SDG commitments. Stronger oversight by fiscal councils and courts of audit – particularly scrutiny of climate-related fiscal risks and long-term sustainability analyses – would enhance the resilience and legitimacy of these frameworks.

2. Embedding resilience for Goals- and climate-oriented decision-based frameworks

14. Beyond incremental improvements to fiscal rules, achieving the SDGs and managing the climate transition require a more profound shift toward resilient, decision-based fiscal frameworks. They particularly call for strengthening anticipatory risk assessment and authorizing fiscal stance modifications to reduce impacts of emerging crises, accelerate recovery and manage the reprioritization of competing short- and medium-term objectives. Access to quality data, enabling agility and ensuring accountability are underlying principles for decision-based fiscal frameworks.

15. Applying the concept of resilience systematically to fiscal policy implies that foresight, stress testing and risk management capacities will be strengthened, especially with respect to climate-related risks such as natural disasters, stranded assets and transition shocks. The effective use of data, digital tools and scenario analysis can help to shift fiscal policy from reactive crisis management towards anticipatory investment in resilience, prevention and adaptation.

16. Early warning systems that integrate macrofiscal, climate and social indicators can inform political leadership about emerging risks and policy trade-offs. Structured assessments of synergies, such as between climate investment, employment, and regional development, can support evidence-based reprioritization aligned with the Goals. Institutional reforms that promote cross-sectoral coordination are critical to overcoming administrative silos that currently impede coherent climate and development strategies.

17. A gradual transition from strictly rules-based frameworks towards more decision-based approaches must preserve public trust and fiscal credibility. This requires high standards of transparency, open government practices and strong internal controls, complemented by independent external oversight. Courts of audit and fiscal councils can play an expanded role by assessing not only compliance with fiscal rules, but also the consistency of fiscal policy with long-term sustainability, climate objectives and intergenerational equity.

18. Finally, strengthening fiscal literacy is essential for sustaining public support for Goals- and climate-related reforms. Citizens' understanding of fiscal trade-offs, long-term investment returns and climate-related risks remains limited. Targeted initiatives through education, transparent reporting and clear communication can help to align public expectations with the realities of financing sustainable development and the climate transition, thereby enhancing the political feasibility of ambitious yet responsible fiscal reforms.

B. Supreme audit institutions at the core of effective public financial management

19. Supreme audit institutions execute independent reviews that provide assurance that policy is implemented as intended and that elements of governance (accountability and transparency) are secured to ensure that there is efficiency and effectiveness in the outlay of public resources.

20. High quality independent audits can inform policy implementation assessment and correction, a role reaffirmed in General Assembly resolution 79/231. In the resolution, a link is made between independent supreme audit institutions and efficient, accountable, effective and transparent public administration, reaffirming the fundamental need for supreme audit institutions to operate independently of the entities they audit and to be protected from external influence. Such independence is essential for objective and effective oversight and credible reporting. This underscores the role of supreme audit institutions in promoting transparency and accountability in public administration, which is conducive to the attainment of national development goals. Supreme audit institution execution of performance (value for money) and budget credibility audits enable objective oversight of policy execution and outcome assessment.

1. Fiscal oversight and budget credibility

21. Supreme audit institutions can analyse the soundness of macrofiscal assumptions, the causes of persistent underspending or arrears and the effectiveness of cash planning. Such reviews fortify fiscal discipline and improve medium-term planning. In some cases, supreme audit institutions perform statutory functions akin to those of an independent fiscal council. Examples include assessments of macroeconomic forecasts, budget assumptions, fiscal rule compliance, fiscal target achievement and explanations of budget deviation provided by the executive branch of government. Supreme audit institutions with an all-encompassing mandate have a bird's-eye view of public finances and statutory access to records and transactions that enable a full review and perspectives to inform policy implementation monitoring and decision-making that supports the fiscal policy review.

22. This role strengthens budget credibility and public trust. In some cases, the fiscal council function of a supreme audit institution is anchored in law and has a reporting protocol. The fiscal monitoring role should also be protected legally from executive influence. Even if supreme audit institutions do not hold formal fiscal council mandates, independent fiscal institution collaboration can strengthen the budget system: supreme audit institutions' ex-post assurance complements fiscal councils' ex-ante analysis of compliance and forecasts.

2. Assurance audit in support of effective resource mobilization

23. The timely execution by supreme audit institutions of financial and compliance assurance audits enables independent and reliable financial reporting and parliamentary oversight. Supreme audit institutions' assurance of the accuracy and reliability of national accounts, and the timely publication of such assurances, anchors fiscal transparency, enables effective scrutiny and facilitates meaningful debates and decisions. Through audits of procurement, project and programme execution, donor funds, and appropriations, it is determined whether projects are executed and whether funds are applied and recorded in a manner consistent with statutory requirements, thus enabling corrective action to stave off unauthorized appropriation and protecting unauthorized use of scarce resources. Assurance audits confirm that the revenues collected are fully accounted for and transferred to the treasury, reducing risks of

corruption or fraud, and build trust among citizens, investors and development partners, which is critical for sustaining revenue efforts and attracting external financing.

24. Performance audits, on the other hand, go beyond compliance with laws and regulations to ask whether public resources are being used efficiently and effectively. This means determining whether funds expended on national priorities comply not only with the requisite laws and regulations, but also with the intended purposes of the programmes or projects. It also involves determining whether project decisions are preceded by feasibility studies, whether they are equipped with a holistic implementation plan, whether the intended outcome or outcomes and targeted beneficiaries are clearly outlined, whether project delivery is inclusive and timely and whether the intended recipients in fact benefit. Such audits provide actionable insights that help policymakers to improve systems, reallocate resources and strengthen institutional capacity.

25. The performance by supreme audit institutions of assurance and non-assurance audits allows for an independent report on the performance of the resource mobilization and public financial management ecosystem, enabling the determination not only of compliance with governing legislation, but also of the efficacy of policy implementation. Although effective, such audits constitute a retrospective review or a historical assessment. A dynamic environment requires audit assurance as programmes are implemented. This is especially the case in emergency situations, which require a quick response that often entails the relaxing of rules intended to safeguard public funds. Transparency often becomes hazy, falling victim to speed. Some supreme audit institutions have responded to this risk by introducing real-time audits. In emergencies and major policy priority programme deployment, such as during the coronavirus disease (COVID-19) pandemic, some supreme audit institutions conduct concurrent checks on procurement integrity, eligibility and cash transfers and disbursements, providing timely assurance without unduly impeding legitimate urgency. In these instances, supreme audit institutions can ensure that those charged with governance are informed of deviations and issues while programmes are executed to facilitate corrective action before losses accumulate.

3. Addressing key challenges

26. Supreme audit institutions will be limited in their effectiveness to undertake non-assurance and assurance audits if restricted by mandate, budgetary allocation and/or competent skill set. For example, some supreme audit institutions have no mandate to undertake non-assurance audits; their independence is impaired either legally or by resource constraints. In such cases, they are not equipped to offer independent opinions on budget execution effectiveness, budgetary outcomes and emerging risks and issues such as climate change adaptation. This is especially the case for small island developing States, where there is a high risk of misalignment in budget outlay. On the other hand, there are supreme audit institutions that have a mandate but that lack capacity, as they do not have access to adequate funding to enable the procurement of requisite skill and technology. This may affect stakeholders' confidence in a supreme audit institution's output, owing to the latter's inability to undertake relevant and dynamic audits.

27. Donor partners and the Development Initiative of the International Organization of Supreme Audit Institutions have played a significant role in providing assistance to supreme audit institutions in small island developing States and those operating in challenging and complex contexts.[4] As donor priorities shift and funding declines,

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[4] See the website of the INTOSAI Development Initiative at https://idi.no/.

underresourced supreme audit institutions grow more vulnerable; Governments should be urged to invest in supreme audit institutions as key preventive and monitoring elements within the public financial management ecosystem by strengthening supreme audit institutions' legal and operational independence to ensure objective oversight and credible reporting. Furthermore, supreme audit institutions should be encouraged to expand their use of real-time and performance audits to provide timely assurance and actionable insights during programme implementation, especially in dynamic or emergency contexts. They should also be encouraged to undertake budget credibility audits to enhance the comprehensiveness of their fiscal analyses. These are fundamental to creating robust governance arrangements to promote efficiency and effective resource mobilization.

III. Improving intergovernmental and subnational public finance and public financial management

28. The 2030 Agenda commits the global community to the achievement of ambitious Sustainable Development Goals in a short time. To do this, countries must innovate with new partners and use the full range of governance, fiscal and managerial mechanisms at their disposal. The 2030 Agenda recognizes subnational governments as important actors in ensuring that the Goals are translated into action that is tailored to the needs of their communities with respect to climate change and other global challenges. They must also catalyse local expertise and resources and secure support from domestic and external sources.

29. The New Urban Agenda subsequently contained a call for a new model of urban development to integrate all aspects of sustainable development to support equity, welfare and inclusive prosperity. Furthermore, the Sevilla Commitment on financing for sustainable development includes a commitment to strengthening subnational finance; improving accounting systems and reporting mechanisms; and boosting intergovernmental coordination. It also promotes the diversification of revenue and financing sources, including through the exploration of municipal bond markets, as applicable, and promote stable and transparent intergovernmental financial transfer systems and equalization mechanisms (see General Assembly resolution 79/323, annex, para. 27 (o)).

A. The fiscal and development role of subnational governments

30. Despite recognition of the subnational dimension of the Sustainable Development Goals, the roles that subnational governments can play and capacities and resources required have received relatively limited attention. To ground the need for action, it is useful to recall why subnational governments can be key players in sustainable development.[5]

- High-income countries – and many low- and middle-income countries – expect subnational governments to perform certain functions. Subnational governments in high-income countries account for nearly a third of public spending and over 40% of public investment.[6] Fiscal decentralization is uneven in low- and middle-income countries, but even in low-income countries, subnational governments account for 12% of spending and 18% of investment.

[5] David Jackson, editor, Local Government Finance is Development Finance, United Nations Capital Development Fund (New York, 2022).

[6] OECD and United Cities and Local Governments, *2022 Synthesis Report: World Observatory on Subnational Finance and Investment* (Paris, 2022).

- Many countries have large gaps in infrastructure that are critical for the Goals. Needs will surge with population growth and urbanization.[7] Filling gaps requires planning and investment related to functions that subnational governments do or could play a role in. Subnational governments can contribute by raising resources, investing and delivering services to advance local and national goals.
- Many Goals include components that must be addressed together in specific jurisdictions, as embodied in Goal 11. Given their proximity to local residents, subnational governments have more potential and motivation than national actors do to consider territorial development holistically.[8] Over 60% of Goal targets are linked to cities or require local action,[9] and subnational governments are estimated to have responsibility for over 70% of climate infrastructure needs.[10] National actors offer frameworks and support, but subnational governments often play a role in action related to the Goals.
- Many Goals are centred on alleviating global challenges, including climate change, financial instability, energy deficiencies, health crises and food insecurity. While international and national measures are essential, subnational governments already take action in some countries and could do more to support climate adaptation, energy conservation and green growth.[11]

B. The subnational revenue landscape

31. Central Governments have advantages when it comes to revenue generation, given the nature of productive revenue bases and administrative scale economies, while subnational governments often have an edge when it comes to providing certain services due to spatial variations in needs. This makes intergovernmental transfers and how they are shared critical. However, there is a strong case for having subnational governments raise some funds, which reduces pressure on national budgets; links the costs and benefits of local services; covers debt service on infrastructure investment; and frees up national resources for fiscally weaker subnational governments.

1. Subnational own-source revenues

32. The often high demand for and restrictions on own-source revenue generation results in great differences between the responsibilities and revenue capacities of subnational governments. Subnational governments in middle- and high-income countries may collect 30% or more of their revenue. This figure is lower in low-income countries, although there are outliers and variations within countries. While the revenue bases and capacity of urban governments may offer these governments more fiscal autonomy, the autonomy of federal systems can be constrained by State controls. There is broad agreement that many central Governments, especially in low- and middle-income countries, decentralize fewer revenue sources than is justified by fiscal principles and the needs of subnational governments. Still, a range

[7] See www.worldbank.org/en/topic/sustainableinfrastructurefinance/overview.

[8] European Commission, Supporting Decentralisation, Local Governance and Local Development through a Territorial Approach, Tools and Methods Series, reference document No. 23 (Brussels, 2016).

[9] Solomon Greene and Brady Meixell, “Hacking the Sustainable Development Goals: can US cities measure up?”, Urban Institute (Washington, D.C., 2017).

[10] OECD, World Bank and United Nations Environment Programme (UNEP), Financing Climate Futures: Rethinking Infrastructure (Paris, 2018).

[11] Paul Smoke and Mitchell Cook, *Administrative Decentralization and Climate Change: Concepts, Experience and Action*, World Bank (Washington, D.C., 2022).

of own-source revenue options is often available to subnational governments.[12] These include property taxes, fees and charges; licences; economic activity taxes; and, at times, other sources of revenue at intermediate or urban levels.

33. Even when subnational government revenues are allowed, they are often underutilized. Intergovernmental transfers can create disincentives for local revenue generation, data and capacity limitations generate administrative challenges, and local political dynamics can weaken enforcement. In addition, as central regulations are common, full local revenue autonomy is rare. Subnational government own-source revenue and tax-sharing provisions are diverse, as are the conditions in which they operate. Some countries have adopted positive reforms related to subnational government revenue that involve fresh approaches to managing conventional subnational government sources. Others create new subnational government sources, such as land value capture to raise funds from land value increments generated by infrastructure (e.g. roads, sewerage and transit).[13]

2. Intergovernmental fiscal transfers

34. Subnational governments in most countries, whether high-, middle- or low-income, significantly rely on intergovernmental fiscal transfers given the imbalance between subnational government expenditure and revenue responsibilities, although urban areas can be more independent.[14] Transfers can improve subnational governments' autonomy and access to resources, as well as help to meet priority aims related to national development, service delivery and equity, including those embodied in the Goals. Multiple considerations are important.

35. First, given own-source revenue constraints, subnational governments require reliably sufficient intergovernmental fiscal transfers. As there are many demands for public revenues, central Governments cannot fully provide for all subnational governments, and they also need the flexibility to respond to changing macroeconomic conditions. Nevertheless, there has been a movement to define the total volume (pool) of intergovernmental fiscal transfer resources in a relatively predictable way to limit disruptive or politicized variations in the amount of national funds shared with subnational governments.

36. Second, it is important, and increasingly common, to allocate intergovernmental fiscal transfer funds on the basis of objective criteria, which improves transparency. Intergovernmental fiscal transfer formulas allow the centre to meet key goals, such as improving resources (and equity if intergovernmental fiscal transfers are redistributive), increasing autonomy (unconditional intergovernmental fiscal transfers) and targeting priority functions (conditional intergovernmental fiscal transfers), including Goal targets. A key policy decision with respect to intergovernmental fiscal transfers is to identify priority goals and what that implies for how funds should be allocated.

37. Third, if intergovernmental fiscal transfers are large and create problematic incentives, they may weaken subnational government tax effort and borrowing. Unnecessary intergovernmental fiscal transfers to creditworthy subnational governments reduces funds for fiscally weaker subnational governments. In addition, conditional intergovernmental fiscal transfers may create incentives to overspend on certain sectors. In practice, intergovernmental fiscal transfer systems are diverse.

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[12] Roy Bahl and others, *Fiscal Decentralization and Local Finance in Developing Countries: Development from Below* (Cheltenham, United Kingdom of Great Britain and Northern Ireland, Edward Elgar Publishing, 2018).

[13] OECD, Global Compendium of Land Value Capture Policies, (Paris, 2022).

[14] A synthetic review of intergovernmental transfers is provided in Bahl and Bird, 2018.

The key concern is arriving at the right balance among types of transfers and creating incentives for subnational governments to behave developmentally and responsibly.

3. Subnational development finance

38. Across countries at all income levels, subnational governments face escalating investment demand. However, available capital – from domestic public resources, multilateral development banks, development finance institutions, institutional investors and climate funds – remains elusive to subnational governments due to structural and institutional barriers. A core challenge is the inability of subnational governments to prepare bankable projects. Many lack the technical capacity, procurement systems or long-term investment planning needed to generate financeable pipelines. Financiers also face constraints: multilateral development banks often require sovereign guarantees even if subnational governments are creditworthy, and private investors have high transaction costs and limited credit data on subnational governments and are subject to regulations preventing direct lending to subnational governments. These factors result in a mutually reinforcing cycle that preserves the disconnect between supply and demand,[15] delaying developmental investment, raising infrastructure costs and jeopardizing goals related to climate and other issues.

39. This situation results from multiple demand-side factors. National-level institutional design often restricts the ability of subnational governments to mobilize resources. Key constraints include the issues noted above with weak revenue authority of subnational governments; inadequate, unpredictable or discretionary transfers, which undermine multi-year planning; tight borrowing restrictions requiring central authorization; and rigid public-private partnership and procurement regulations that increase transaction costs. These constraints disproportionately affect small and intermediate cities carrying large service burdens but lacking fiscal tools.

40. Even when they do have autonomy, subnational government capacity deficits limit finance. These include the public financial management issues noted below; low creditworthiness (less than 20% of the 500 largest cities in low- and middle-income cities are deemed creditworthy in local markets, and only 4% internationally[16]); deficient capacity for project preparation; fragmented long-term planning that misaligns capital strategies with land-use and climate plans; and political turnover that disrupts investment continuity and increases perceived risk to lenders.

41. There are also supply-side constraints. Finance institutions face structural barriers that limit supply: mandatory sovereign guarantee requirements create bottlenecks; high fixed transaction costs make small-to-medium municipal loans uneconomical; absence of instruments tailored to subnational governments; and multilateral development bank operational frameworks that are designed for sovereign lending, which leads to lengthy approval processes, high minimum thresholds and inadequate methodologies for assessing the creditworthiness of subnational governments.

42. Beyond institutional barriers, suppliers face information asymmetries and risk assessment challenges. Private financiers lack consistent local data and legal protections, making lending to subnational governments appear to be high-risk even if credit quality is adequate. The absence of standardized financial reporting, credit ratings and fiscal data on subnational governments prevents lenders from properly

[15] Mauricio Rodas and Sandra Villars, "How Quito has raised crucial finance for nature-positive urban development", *World Economic Forum*, 23 December 2024.

[16] Graham Floater and others, "Financing the urban transition: policymakers' summary", Coalition for Urban Transitions (Washington, D.C., and London, 2017).

assessing risk. In addition, supply is constrained by underdeveloped municipal bond markets, lack of credit rating agencies, weak frameworks related to borrowing by subnational governments and limited secondary market liquidity.

C. Strengthening operational processes

43. Public financial management reforms are considered central for subnational governments, given their role in promoting managerial efficiency, transparency and subnational government accountability to both higher-level governments and local constituents. There is consensus on the need for improved public financial management, although there may be debates about how it relates to other reforms.[17] One such debate is centred on the relationship between public financial management and decentralization. Ideally, reform would be pursued in tandem with decentralization, but this is challenging if public financial management and decentralization are led by different national agencies. Assessing public financial management requires documentation of how subnational government budgets are created, executed and monitored and how assessments are used. When there is central control over subnational government budgets, there are often concerns about limited discretion.[18] The role of subnational governments in the budget process is often unclear or mis-timed (i.e. input from subnational governments is too late to be considered). Top-down approaches often dominate budgeting, even if input from subnational governments is solicited. Overly centralized approaches may use allocation criteria that are insufficiently tailored to the needs of subnational governments.

44. Budget execution is also a major concern. It is commonly claimed by subnational governments that they have limited discretion to adjust the use of service-delivery fiscal transfers. There is little evidence regarding whether limiting the flexibility of subnational governments when it comes to transfer use has a positive (meeting national standards) or negative (difficulty in targeting local needs) impact on service delivery. It is important to document both the extent and effects of discretion, including whether existing constraints are beneficial and whether they may need modification.

45. Beyond budgeting and reporting, other processes protect the use of public resources by subnational governments. These include auditing, procurement, and public-private partnership frameworks. Procurement by subnational governments may be centralized even for legally devolved functions, and in other cases it may be done locally, with insufficiently regulation. Similarly, public-private partnerships undertaken by subnational governments may be largely managed by a central agency, but in other cases they may be left to subnational governments that do not have the expertise to negotiate or enforce the relevant agreements.

46. Funds for service delivery by subnational governments – whatever the source and allocation criteria – may be managed using various systems and processes. Subnational public financial management is often integrated into national systems. In cases where separate systems exist, they may use various budget categories, standards and processes, which complicates sector finance management and creates challenges

[17] Marco Cangiano and others, editors, *Public Financial Management and Its Emerging Architecture* (Washington, D.C., IMF, 2013); Tom Hart. and Bryn Welham, "Fiscal decentralisation: a public financial management introductory guide", Overseas Development Institute (London, 2018).

[18] Paul Smoke and Gundula Löeffler, An Intergovernmental Perspective on Managing Public Finance for Service Delivery (New York, NYU Wagner Initiative on Reforming the Aid Architecture for Public Finance Reform, 2021).

for central Governments in assessing the performance of subnational governments and determining appropriate action on deficiencies.

47. Equally important, the institutional path through which resources move can vary, flowing from one or more national agencies through one or more government levels before reaching service providers. At each stage, actors may have authority over how and when to pass funds to the next level, resulting in misallocations and delays. In addition, special-purpose funds managed separately by parallel systems (within government or by international agencies) may be off-budget, and they may even flow directly to subnational governments or to service delivery units.

IV. Enhancing resource mobilization through innovations in development finance

48. There is broad recognition that the public sector and development assistance cannot fill current development finance gaps, and therefore public or partnership innovations and private finance are essential. As private finance is not easily accessible in many low- and middle-income countries, creative efforts are needed. Innovative finance refers to new financial mechanisms and approaches that go beyond traditional grants and loans to attract private capital and increase funding for development, social impact and technology growth, often by creating new markets or linking finance to specific outcomes, as is the case with green bonds or impact investing. The aim of innovative finance is to be more sustainable, leveraging private sector skills and capital to tackle major challenges such as climate change or poverty. Innovation requires smart, scalable solutions that use capital more effectively for broader societal benefits.[19]

49. The present section comprises two subsections. The first provides a selective overview of innovative development finance options, grounded in the experience of Uganda. The second contains information on experiences with a variety of mechanisms that have been used to increase the volume of development finance available to subnational governments and to improve its use.

A. Overview of innovative development finance solutions

50. A range of instruments can be used to improve access to and the use of development finance. These include concessional and catalytic capital (including blended finance and risk-sharing); results-based or pay-for-performance financing; local-currency financing and currency risk management; digital financial inclusion and payment infrastructure; climate-risk and resilience-linked finance instruments; and equity and revenue-sharing models in infrastructure.

51. The experience of Uganda with innovative development finance has demonstrated some success and some relatively generalizable lessons: (a) de-risk and decouple private risk from public support via catalytic structures; (b) tie financing to verifiable outcomes to align incentives and improve accountability; (c) deepen domestic markets through local-currency instruments and appropriate capacity-building;

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[19] See the website of the Department of Economic and Social Affairs at https://financing.desa.un.org/; OECD, "Finance for sustainable development", available at www.oecd.org/en/topics/policy-issues/finance-for-sustainable-development.html; World Bank, "Innovative strategies to finance sustainable development, 13 April 2023; World Bank, "Transforming finance to meet today's development needs", 5 October 2025.

(d) connect digital finance ecosystems for credit and investment flows; and (e) embed climate resilience requirements as a standard design criterion.

Concessional and catalytic capital

52. These approaches are designed to use concessional capital to de-risk investments and to attract private capital to high-potential sectors (e.g. agriculture, infrastructure and energy).[20] Several catalytic facilities have been designed in Uganda, attracting private equity into agroprocessing hubs and upstream value chains. Uganda has also explored sovereign-backed guarantee pools, which has arguably partly reduced collateral requirements for small and medium enterprises. The Ministry of Finance, Planning and Economic Development and related institutions are trying to avoid crowding out the private sector; while governance complexity remains a challenge and leakage risks are real, there are scalable design features, including tiered blended facilities with explicit co-financing rules, clearly defined exit pathways for concessional risk buffers and the integration of local capacity-building into deal pipelines.

Results-based financing and pay-for-performance

53. In results-based financing, disbursements are tied to verifiable outcomes to align funders with measurable impact.[21] There has been strong alignment of funding to outcomes in cases where verification is feasible. There are, however, challenges with potential leakages and misaligned or poorly chosen metrics, but some scalable design features are evident. These include the existence of predefined realistic milestones; data integrity and local monitoring and evaluation capacity; and robust verification protocols with independent verifiers.

Local currency financing and currency risk management

54. The approach is intended to reduce currency mismatch by allowing borrowing and lending in local currency.[22] This has lowered repayment volatility for local borrowers and improved project viability in climate and rural initiatives in Uganda. There are some gaps and financial cautions related to domestic market depth limits, currency liquidity risk and macrostability prerequisites. There are several scalable design options, including the use of a tiered local-currency bond programme; the adoption of hedging strategies; and the adoption of supportive policies for market development.

Digital financial inclusion and payment infrastructure

55. This approach is intended to expand reach, reduce costs and enhance risk assessment by means of mobile money and digital identification.[23] This has increased the widespread adoption of mobile money, enabled scalable microcredit and promoted data-rich credit scoring. There are some potential concerns in areas such as data privacy and cyberrisk; consumer protection; and risk-based pricing. Important design

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[20] International Finance Corporation, "Creating opportunities in challenging markets, (Washington D.C., 2022); Manpreet Kaur Juneja, "How blended finance can attract cautious private investors to infrastructure", World Bank blogs, 7 August, 2024.

[21] Global Partnership on Output-Based Aid, *A Guide for Effective Results-Based Financing* (Washington D.C., World Bank, 2018).

[22] Paul Horrocks and others, *Unlocking Local Currency Financing in Emerging Markets and Developing Economies* OECD (Paris, 2025).

[23] Purva Khera and others, "Digital financial inclusion in emerging and developing economies", IMF, 19 March 2021. See also www.worldbank.org/en/topic/digital.

features include interoperable digital rails with strong data governance, regulatory sandboxes for experimentation, and consumer education.

Climate-resilient finance and nature-based solutions

56. These initiatives are aimed at integrating climate risk considerations into financial products and at aligning incentives with adaptation and resilience.[24] There has been some success in that regard with, for example, weather-indexed insurance pilots reducing farmer default risk and resilience-linked lending for irrigation in Uganda. There are some issues with basis risk, data quality, affordability and policy coherence. For weather-indexed insurance to work, it is necessary to strengthen data networks, align insurance payouts with agronomic risk and integrate resilience criteria into loan covenants.

Equity and revenue-sharing models in infrastructure

57. This approach is designed to attract domestic investors to participate in revenue-generating infrastructure, with a shared upside.[25] There has been some success with domestic capital engagement and milestone-driven performance frameworks, but also some challenges with respect to governance, contract enforcement and price-regulation risks in monopolies. Successful efforts require standardized public-private partnership templates, clear regulatory oversight and the use of progress-tracking milestones.

B. Emerging innovative subnational development finance solutions

58. Pioneering development finance institutions, bilateral agencies and innovative municipal financing platforms have demonstrated that alternative approaches can successfully channel capital to subnational governments while building institutional capacity. These solutions differ from traditional sovereign-centred models by offering flexibility in legal contexts, emphasizing capacity-building alongside capital provision, accepting alternative securities beyond sovereign guarantees and integrating technical assistance with financial products. Below are some notable examples that are paving the way for broader reforms in various regions.

Direct lending without sovereign guarantees

59. The Development Bank of Latin America and the Caribbean has a comprehensive subnational lending platform, demonstrating that lending to subnational governments without mandatory sovereign guarantees is viable and scalable with suitable risk management. The Bank's model combines direct lending based on the creditworthiness of subnational governments using specialized assessment methods, comprehensive technical assistance for institutional strengthening and project preparation, and credit enhancement mechanisms such as partial guarantees and risk-sharing. The Bank deployed billions of dollars in direct lending to subnational governments across Latin America, with strong programmes in Argentina, Brazil, Colombia, Ecuador and Peru. Factors for success include strong in-house analytical credit assessment capacity, sustained multi-year engagement with borrowers, legal flexibility to lend without

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[24] See World Bank climate change webpage, at www.worldbank.org/en/topic/climatechange/overview. See also UNEP finance initiative webpage, at www.unepfi.org/.

[25] See World Bank Public-Private Partnership Resource Center webpage, at https://ppp.worldbank.org/; see also World Bank, "Understanding hybrid public-private partnerships", 14 October 2024.

sovereign guarantees and long-term institutional commitment to the subnational government sector.[26]

Integrated planning, finance and capacity-building

60. The European Bank for Reconstruction and Development has pioneered a comprehensive approach to urban infrastructure finance through its Green Cities programme,[27] which integrates strategic planning, financing and institutional capacity-building in a framework addressing demand- and supply-side constraints. There are three phases: Green City action plans that identify environmental and climate challenges through stakeholder consultation; direct loans for priority projects, utility lending, equity investments, guarantees or blended finance; and sustained technical assistance to prepare and implement projects and strengthen institutions. As of 2024, the programme had involved over 45 cities in more than 25 countries, mobilizing several billion euros in investments for energy efficiency, sustainable transport, water and sanitation, solid waste management and climate adaptation infrastructure. On the demand side, these action plans help cities to develop investment pipelines and capacity; on the supply side, blended finance mobilizes private capital with standardized approaches to reduce transaction costs.

Utilities-focused approach: bypassing municipal fiscal constraints

61. Agence française de développement has an innovative approach that involves channelling resources through subnational government utilities and service providers rather than through subnational governments themselves, effectively bypassing subnational government fiscal and institutional constraints while supporting local infrastructure. In many countries, the utilities possess stronger financial profiles than their parent subnational governments through dedicated revenue streams from user fees, commercial management structures, clear performance metrics and regulatory oversight that enforces financial discipline. Agence française de développement provides financing directly to utilities based on their own creditworthiness and project viability rather than requiring subnational or sovereign guarantees. Implementation mechanisms include direct utility loans secured by specific revenue streams, performance-based financing tying disbursement to operational improvements, blended concessional windows combining market-rate lending with grants, and regulatory support for tariff reform. Agence française de développement has applied this model extensively in North Africa (Egypt, Morocco and Tunisia) and sub-Saharan Africa (Burkina Faso, Côte d'Ivoire and Senegal), financing water supply networks, wastewater treatment, solid waste systems and urban transport. The approach works best for revenue-generating infrastructure but requires utilities to have sufficient autonomy, adequate tariff levels, competent management and appropriate sector regulation.

Guarantees for subnational governments: reducing sovereign dependency through risk-sharing

62. Guarantee and credit enhancement mechanisms deploy limited public resources to mobilize larger flows of commercial capital to subnational government infrastructure without full sovereign guarantees. Key structures include partial credit guarantees (50–80% of debt service), partial risk guarantees (targeting specific risks), insurance on bonds issued by subnational governments (elevating credit ratings to investment grade) and first-loss facilities in blended finance structures. Institutional

[26] Development Bank of Latin America and the Caribbean, "CAF approves USD 200 million to improve urban mobility in Bogotá", 29 June 2025.

[27] See www.ebrdgreencities.com/.

providers operate at multiple scales, from global facilities such as the World Bank and GuarantCo to national mechanisms such as credit contingency funds in Colombia and local government loan guarantees in the United Republic of Tanzania. GuarantCo has supported over 1 billion dollars in local currency infrastructure financing, while municipal bond guarantees in India have enabled successful pooled financing in Tamil Nadu and Karnataka. Despite implementation challenges, including contingent liability concerns, pricing requirements and limited default experience, guarantee instruments are a promising avenue for scaling subnational government climate finance while managing fiscal risk.

Green Cities Guarantee Fund: a mechanism for urban climate infrastructure

63. Building on proven guarantee mechanisms, the Green Cities Guarantee Fund[28] represents an innovation to address barriers facing subnational governments in accessing affordable capital for climate infrastructure. Proposed by the Global Commission for Urban Sustainable Development Goals Finance of the Sustainable Development Solutions Network with a planned pilot phase in Latin America, the Fund aims to de-risk lending to subnational governments and affiliated entities by transferring repayment risk to a highly rated guarantor. Guarantees can mobilize 6 to 25 times more financing than traditional loans, and analysis by the European Investment Bank indicates that subnational government borrowers have lower default rates (2.2%) than private sector borrowers (3.6%). The Fund would provide partial and full credit guarantees for local and hard currency debt for transport, water and sanitation, renewable energy, waste systems and climate disaster risk management. The planned Latin American pilot, with Argentina, Brazil, Colombia and Mexico as initial markets, presents opportunities for subnational governments to leverage this tool for transformative climate investments. The Fund would operate under independent governance that balances stakeholder perspectives, with capitalization from multilateral development banks, bilateral agencies, national Governments, philanthropic organizations and, eventually, private investors. It would promote self-sustainability through guarantee premiums and investment returns.

Local government funding agencies and pooled finance

64. Local government funding agencies are specialized financial institutions that are jointly owned by member municipalities, enabling collective capital market access and achieving economies of scale and credit quality that individual jurisdictions cannot attain independently. The model features joint and several liability, whereby all members back funding obligations, promoting AAA ratings through portfolio diversification, statutory protections providing municipalities with assured revenue access, professional management by specialized staff and non-profit orientation focused solely on minimizing member borrowing costs.

65. Kommuninvest (Sweden), Kommunalbanken (Norway), Municipality Finance (Finland) and BNG Bank (Kingdom of the Netherlands) each provide financing representing substantial shares of total municipal debt, offering lending rates only marginally above government bond yields. Successful adaptation requires phased implementation, partial liability in the initial phase, development partner credit enhancement, technical assistance and regulatory oversight.[29]

[28] Eugenie L. Birch and others, The Green Cities Guarantee Fund: Unlocking Access to Urban Climate Finance, Penn Institute for Urban Research and Sustainable Development Solutions Network Global Commission for Urban Sustainable Development Goals Finance (Philadelphia, 2024).

[29] OECD, "Subnational investment promotion and decentralisation in the OECD" (Paris, 2023).

Green bonds, blue bonds, impact bonds and green banks

66. Market-based financing instruments offer municipalities diversified mechanisms to mobilize private capital while signalling commitment to environmental, social and governance objectives. Green and blue bonds have experienced explosive growth, with annual issuance exceeding 500 billion dollars globally and notable municipal issuances from Paris, Johannesburg and Mexico City.[30] While offering reputational benefits and access to investors focused on environmental, social and governance considerations, challenges include verification costs, reporting obligations, risks related to greenwashing and limited applicability.

67. Impact bonds tie private investor returns to the achievement of predetermined outcomes, with nascent municipal applications in disaster risk reduction and social infrastructure. Green banks (i.e. specialized public institutions such as Connecticut Green Bank and New York Green Bank) deploy innovative financing through low-cost debt, credit enhancements and technical assistance, and have mobilized billions in private capital for energy efficiency and renewable energy infrastructure.[31] These instruments demonstrate that subnational governments can access capital markets when appropriate conditions exist, although they supplement rather than replace traditional mechanisms and require sophisticated institutional capacity.

V. Concluding observations

68. **The present paper covers selected topics on improving public resource mobilization through fiscal and financial management reform, fiscal decentralization and innovative development finance. This material must be considered and interpreted in the light of country-specific contexts, but a few summary points can be made.**

69. **First, building resilient national fiscal frameworks can begin with a reorientation of public financial management towards outcomes, priorities and value for money while also balancing short-term stabilization goals with long-term sustainable development and climate commitments. Priorities include reducing spending rigidity, enabling timely reallocations and institutionalizing ongoing reprioritization across policy objectives. Such efforts are central to progress on the Sustainable Development Goals, which depends on managing trade-offs and exploiting synergies. Institutional and procedural changes must embed resilience, foresight and risk management into fiscal policymaking and the broader policy cycle.**

70. **Second, supreme audit institutions can play their vital preventive and monitoring roles within the public financial management ecosystem only if they have legal independence to ensure objective oversight and credible reporting, which are essential for the achievement of the Goals. It is important to alleviate restrictions caused by mandates, insufficient resources or capacity deficits. Supreme audit institutions must be able to offer objective opinions on budget execution effectiveness and outcomes and emerging risks and issues such as climate change adaptation. An inability to meet these responsibilities will affect supreme audit institutions' performance and stakeholders' confidence in their outputs.**

71. **Third, more attention to the role of subnational governments in supporting the Goals could yield major benefits. Subnational governments require powers,**

[30] Climate Bonds Initiative, "Sustainable debt: global state of the market summary 2024" (2025).
[31] "What Is a Green Bank?" Available at https://cgc.org/what-is-a-green-bank/.

resources and capacity to act more autonomously and as key players in a multilevel government team. Funding sources must be integrated to ensure effective results. In addition, the roles of subnational governments must be grounded in an intergovernmental system tailored to country context and designed to create conditions and incentives that properly balance upward and downward accountability and promote transparency. Reforms should be strategically sequenced and accompanied by capacity-building, and the system can evolve as the capacity and results of subnational governments mature.

72. **Lastly, increasing the volume of development finance and improving its allocation are essential. National public resources and development assistance, however, cannot cover the enormous and growing global infrastructure investment gaps. Reforms must attract private capital and deploy innovative mechanisms that ease and share risk and create stronger incentives for borrowers and lenders. Special attention is also required in order to increase development finance that is targeted to climate change action and other global priorities, as well as to allow subnational governments to secure the finance required to support essential investments in the Goals.**