FAST INSIGHT 4

Development finance and modern slavery and human trafficking

About FAST

Finance Against Slavery and Trafficking (FAST) is a global public-private partnership mobilizing the financial sector to fight modern slavery and human trafficking. The FAST Blueprint (September 2019) sets out five Goals and thirty Actions for financial sector actors to address modern slavery and human trafficking. This Insight focuses on the implications of the FAST Blueprint for development finance institutions, especially under FAST Goal 5.

Modern slavery is a drag on sustainable development

When one person enslaves another, they deny their economic agency and prevent them exercising outside labour options. Slavery also often involves control of consumption, savings and investment choices. This denial of agency ripples through the economy, leaving *everyone* worse off in 10 ways:

1. **Slavery reduces productivity**. It demotivates workers, and leads to inefficient labour allocation. This pushes capital towards rentier sectors, reducing overall economic productivity.

2. **Slavery creates inter-generational poverty.** The negative health, human capital formation (education) and income impacts of slavery spill over to victims' families and communities. They are transmitted through generations.

3. **Slavery institutionalizes inequality**. Rent-takers use their profits to entrench their power and institutionalize structural inequality. Addressing this can be very expensive: it cost the UK a payment of 5 per cent of GDP, paid over 180 years, to buy out British slavers in the 1830s.

4. **Slavery weakens multiplier effects**. Slaves lose control of their consumption, savings and investment choices, reducing economic multipliers. So emancipation leads to growth.

5. **Slavery discourages innovation in production**. It demotivates both workers and exploiters to innovate, making slavery-dependent industry inefficient, uncompetitive and unsustainable

6. **Slavery produces a capital market failure**. Capital markets tilt unfairly towards firms whose low costs rely on illegal labour practices. This is anti-competitive and inefficient.

7. **Slavery hits the public purse**. It reduces income and consumption tax receipts, and increases direct expenses to the public budget. UK Home Office researchers estimated domestic costs from modern slavery at GBP 3.3 to 4.3 billion per year.

8. **Slavery weakens governance**. It corrodes trust, increases social stratification, ethnic fractionalization, violence and conflict. It impedes state formation and investment in public good.

9. **Slavery fuels corruption and illicit financial flows**. Slavers bribe and corrupt officials to protect the slavery system, further weakening governance. Exploitation of migrant workers may in some cases be an illicit transnational financial flow.

10. **Slavery harms the environment**. Slavery rests on illegal management practices that often also disregard environmental protections. It coincides with deforestation, illegal and over-fishing, unsustainable agricultural practices, and negative impacts on biodiversity and carbon capture.

Development institutions have not yet focused on anti-slavery objectives at scale

- A recent survey of development institutions – multilateral development banks, development finance institutions, and export credit agencies – found that most treat modern slavery risks as an unintended outcome of poor project management. There has been limited effort to design interventions to reduce modern slavery risks.

- On average, less than USD 12 in Official Development Assistance (ODA) was committed per victim, per year, globally, between 2000 and 2017.

- The largest donor has been the US, followed by the EU, Norway, Germany, Canada, Australia, Spain, Sweden, UK and Switzerland.

- Only 1.3 per cent of the UN's country-level development strategies between 2000 and 2020 provided for joint (multi-agency) programming on modern slavery – an indication that it is not seen as a strategic priority.

- In a recent survey of development practitioners, 67 per cent of respondents said that their organization saw slavery as a social or criminal justice policy concern, not as an economic, trade or industrial policy concern.

Development finance can however help reduce modern slavery at scale

- From 1992 to 2017 around one fifth of the adult population of Uzbekistan experienced forced labour in the cotton harvest each year, as a result of government coercion and social pressure. Yet the number of people in forced labour fell from 448,000 in 2014 to 102,000 in 2019, according to the ILO. This was the result of coordinated efforts involving the Uzbek government, international donors, the ILO and, significantly, the World Bank.

- Brazil has rescued 55,000 people from slavery-like conditions since 1995. The policies and lending practices of development actors, including foreign donors and the national development bank, BNDES, have played a key role in promoting anti-slavery norms.

- Coordinated action by development actors has also helped reduce modern slavery risks in the Thai fishing sector, global garments sector, palm oil industry and large-scale infrastructure and construction development.

- These experiences point to the importance of development actors knowing and showing the connections between their lending, projects and programming, and modern slavery risks (FAST Goal 2); and using their individual and collective leverage to mitigate these risks (FAST Goal 3) and to provide and enable remedy (FAST Goal 4).

Development finance increasingly aims to foster 'responsible business conduct'

- It is increasingly common for development actors to assess the risk that a loan or investment will increase modern slavery before committing, and then putting project safeguards in place.

- This is not just the case for OECD lenders. Chinese lending is also increasingly subject to legislative and industry-backed norms prohibiting links to forced and child labour. These have the potential, if enforced, to help ensure Chinese overseas lending contributes to slavery reductions.

- Development actors' project safeguards arrangements increasingly align around international expectations of responsible business conduct and business respect for human rights. These are reflected in the UN Guiding Principles and Business Human Rights, and relevant OECD Guidance.

- There is a growing cohort of development actors actively learning on their own, and from each other, what effective safeguards, due diligence and business engagement looks like.

- Their operational practices vary significantly. Some conduct their own risk assessments, while others rely on borrowers, beneficiaries and clients to do so. Some hold their partners to international labour standards; others defer to national arrangements. That creates a real risk that where states do not already respect international standards, development efforts will not only do nothing to generate behavioural change, but could in fact amplify labour violations and reinforce institutional environments conducive to such violations.

- Most safeguards are however limited to project lending. They do not extend to so-called 'policy lending', or advisory work.

- Development actors may need to consider not just how slavery risk may arise within their business relationships, but also how contextual risk can heighten project risk, and vice versa. In Ghana, for example, World Bank funding for a dam in the 1960s led to the disruption of traditional agricultural livelihoods, which then led to families trafficking children into slavery on Lake Volta. And presently, in Eritrea, EU financed road construction, managed by the UN, may contribute to demand for forced labour supplied through a controversial government conscription scheme.

The turn to 'blended finance' also provides both risks and opportunities

- Growing emphasis on blended finance and public-private partnerships (PPPs) raises questions about how to balance financialized treatment of development projects as future income streams with their broader social purpose. Some commentators raise concerns about the use of the Sustainable Development Goals for 'rainbow-washing' of investments. Others note weaknesses in private assessment of social risk.

- Historical episodes, such as the financialized development of the Mississippi Valley in the 1830s, point to the risks of such an approach. The absence of a central risk monitor for capital markets and the inability of private actors to reliably assess risks can lead to financial panics and broader economic harm, as in 1837 – the steepest economic downturn until the Great Depression.

- Without central monitoring, risk can build up to toxic levels, endangering the system. De-risking can become risk reallocation – to society as a whole.

- The episode also points, though, to the possibility of innovation to address a lack of reliable risk information: it led to the invention of the commercial credit ratings system. Given their growing reliance on private capital to finance development, public and multilateral development actors, have a growing stake in ensuring global capital markets accurately price ESG risks, including modern slavery risks.

Development actors have important opportunities for innovation for prevention

- COVID-19 has increased modern slavery risks – but also offers an innovation opportunity.

- The increased role of governments in the private economy, as owners and investors, following pandemic bailouts, gives governments greater leverage to promote responsible business conduct.

- At the same time, the pandemic has seen a surge of capital into ESG markets, looking for ways to invest in business that promotes achievement of the Sustainable Development Goals.

- Development actors could innovate to promote prevention of modern slavery by:

  » Rethinking development pathways to focus on protecting and promoting economic agency;

  » Embedding responsible business conduct expectations in all investment and lending decisions, and in their policy lending;

  » Supporting the development of harmonized anti-slavery metrics in ESG and social impact measurement and disclosure frameworks;

  » Investing in the development of anti-slavery bonds and embedding anti-slavery objectives in sustainable finance and sustainability-linked finance;

  » Collaborating to learn what works.

More Information

This Insight draws extensively on Developing Freedom: The Sustainable Development Case for Ending Modern Slavery (UN University, January 2021).

If you prefer to learn by listening, check out *Finance Against Slavery and Trafficking: The Podcast*.