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Poverty in Middle-Income Countries

Andy Sumner
IDS, Brighton

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Poverty in Middle-Income Countries

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Abstract

This paper describes a shift in the global distribution of poverty from low-income countries (LICs) to middle-income countries (MICs) and how the role of external development actors (such as 'traditional donors' – meaning OECD DAC donors and philanthropic foundations and international NGOs) – might have to change to meet the challenges that this new distribution of poverty represents. The paper argues that, if we accept the proposition that most of the world's extreme poor already live in largely non-poor countries, in order to meet their own objectives of reducing poverty, external actors will need to find new configurations of relationships (or they could decide poverty in MICs is not their problem and focus on LICs). If they do remain concerned with extreme poverty, external actors will need to continue work in the new MICs, because most of the world's poor people live in such countries, but they will need a greater focus on issues of equity/inclusion/exclusion; working with advocacy groups and civil society on issues such as public spending priorities but with great sensitivity to the politics of doing so and recognising that development is very much 'beyond traditional aid' (meaning beyond international resource transfers). Global Public Goods (GPGs), innovative finance mechanisms and other 'beyond traditional aid' modalities will be areas where MIC governments, traditional donors and philanthropic foundations can work together, and the policy coherence, in areas such as trade, of traditional donors will be more important to MIC governments than aid flows. All of this will place far more importance on external actors understanding the political dimensions of development.

Introduction

This paper describes a shift in the global distribution of poverty and how the role of external development actors (such as 'traditional donors' – meaning donors from OECD countries and philanthropic foundations and international NGOs) might have to change to meet the challenges that this new distribution of global poverty represents.[1]

The basic thesis of the paper is three-fold. First, the paper builds upon data presented in Sumner (2010, 2011a, 2011b) and Kanbur and Sumner (2011) which demonstrate that there has been a change in the global distribution of poverty from low-income countries to middle-income countries.

Second, the paper argues this shift matters because the allocation and graduation frameworks of a number of bilateral and multilateral donors are based on low-income countries and, furthermore, there is a 'conventional wisdom' that poor people live in poor countries.

Third, the paper suggests the shift in the distribution of global poverty can be viewed in three possible ways. First, it could all be a sleight of hand – the world's poor people still live in 'poor' countries, albeit slightly less poor than before. Second, it is 'business as usual' because there are limits to domestic taxation on the rich and expanding middle classes in developing countries. Or third, this shift could mean that a fundamental reframing of global poverty is required, 'traditional

[1] Many thanks to two anonymous reviewers for comments and special thanks for RA support to Pui Yan Wong, Henrique Conca Bussacos, Nicki Goh and Rich Mallet.

aid' (resource transfer) is no longer relevant and global poverty is now about equity/inclusion/exclusion, advocacy coalitions and beyond 'traditional aid' (meaning resource transfers).

The paper is structured as follows. Section 2 provides a reprise of the data and the shift in the distribution of global poverty. Section 3 discusses the implications for external actors. Section 4 concludes.

Changes in the distribution of global poverty: A reprise

In 1990, 93 per cent of the world's poor people lived in LICs. Now, more than 70 per cent – up to a billion of the world's poorest people or a 'new bottom billion' – live in MICs (and most of them in stable, non-fragile middle-income countries) (see Table 1). Furthermore, and contrary to earlier estimates that a third of the world's poor live in fragile and conflict-affected states (FCAS), based on data from the early 2000s (Branchflower *et al.* 2004), a 'ball-park' estimate, taking the broad FCAS definition of 43 countries from combining the Fragile States lists, is that in 2007 about 23 per cent of poor people lived in FCAS and these were split fairly evenly between fragile LICs and fragile MICs. This is consistent with the new estimate of Chandy and Gertz (2011: 10) that 20 per cent of the world's poor live in FCAS.

In short, many of the world's poor people live in countries that have got richer in average per capita terms and have been subsequently been reclassified as MICs. After rising considerably in the 1990s, the total number of LICs has fallen significantly since FY2000. According to the Atlas GNI per capita data and country classifications (for World Bank FY2011), over the last decade the number of LICs fell from 63 to just 35 countries in FY2011. Most of the world's poor live in countries that have moved from low- to middle-income country status since 1999 when China graduated to MIC status – notably Pakistan (2008), India (2007), Nigeria (2008), and Indonesia (2003) (henceforth, with China, the PINCIs). China is now an Upper MIC as of July 2011. This concentration of the world's poor people in relatively few countries is a key part of the story. Although 28 countries have transitioned from LIC to MIC since 2000, about 60 per cent of the world's poor now live in just five populous new MIC countries – the PINCIs noted above. Indeed, of the top ten countries by contribution to global poverty only four are LICs – Bangladesh, DRC, Tanzania and Ethiopia.

In sum, most of the world's poor do not live in countries classified by the World Bank as LICs and most of the world's poor do not live in FCAS.

Table 1 Global distribution of world poverty (% of world's poor, US$1.25), 1990 vs 2007

	Author's estimates based on PovCal (World Bank, 2011b, Adjusted base years)	
	1990	**2007**
East Asia and Pacific	49.0	16.6
of which China as % world poverty	38.9	9.6
Eastern Europe and Central Asia	1.3	1.7
Latin America and the Caribbean	2.4	2.3
Middle East and North Africa	0.5	0.9
South Asia	33.6	47.5
of which India as % world poverty	25.1	38.0
Sub-Saharan Africa	13.3	31.1
Total	100.1	100.1
Low-income Countries (LICs)	93.1	29.1
Middle-income Countries (MICs)	6.9	70.9
Total	100.0	100.0
Low-income, non-FCAS	-	16.5
Low-income, FCAS	-	12.6
Middle-income, non-FCAS	-	60.4
Middle-income, FCAS	-	10.5
Total	-	100.0
FCAS Total (43 in 2008)	-	23.1
China and India	64.1	47.6
MICs minus China	-	61.3
MICs minus India	-	32.9
MICs minus China and India	-	23.3
LICs minus China	54.1	-
LICs minus India	68.0	-
LICs minus China and India	29.0	-
PINCIs	76.4	60.2
LICs minus PINCIs	16.7	-
MICs minus PINCIs	-	10.7

Sources: Author's estimates presented in Sumner (2011a) and processed from PovCal Net (World Bank 2011a); totals may not add up to 100% due to rounding; FCAS (Fragile and Conflict-Affected States) definition = 43 countries of combined three lists as per OECD (2010); LIC/MIC status is based on World Bank country classifications; PINCIs = Pakistan; India; Nigeria; China and Indonesia.

Furthermore, this is not just a question of income poverty. One can find a similar story using other poverty measures (see Sumner 2010). Is the trend of concentration of world poverty in new MICs likely to continue? Chandy and Gertz (2011) estimate the proportion of the world's poor in MICs at slightly below 70 per cent (about 66 per cent) and project that this proportion of the world's poor in MICs will still be 55 per cent in 2015. This projected fall of the share of the world's income poor in the MICs is based on an assumption of static inequality and thus fast-falling poverty in the MICs especially so in India and China. However, Kanbur and Sumner (2011) have suggested this may be an overly optimistic view of poverty reduction in the MICs given inequality trends in fast-growing economies. Furthermore, the projections of Moss and Leo (2011) on GNI per capita suggest the number of LICs may well fall to around 20 in 2025, moving more of world poverty towards the MICs over time.

So, is this just about the LIC/MIC thresholds? The LIC/MIC thresholds matter not only because they play a role in determining the distribution of World Bank resources but because they are also used in the allocation and graduation frameworks of a number of bilateral and multilateral donors. For example, UNICEF graduates countries at the MIC/HIC threshold, and uses a weighted formula for allocations based on: (i) the Atlas GNI per capita data (but not the LIC/MIC threshold); and (ii) the under-five child population and child mortality rates for each country (for a detailed discussion of exactly how the thresholds are used by UNICEF, UNDP, UNFPA, WFP and the Global Fund to Fight AIDS, TB and Malaria, see UNICEF 2007: 76–80). The UN category of 'Least Developed Country', which has particular importance for trade preferences and other special treatment, is also based, in part, on the GNI per capita data and thresholds (for a detailed discussion see Guillaumont 2010). Further, for the decade prior to its 2010/11 Bilateral Aid Review, DFID allocated 90 per cent of its resources to LICs based on a '90/10 rule'. This was in turn based on the Collier and Dollar (2002) model of 'poverty-efficient' Official Development Assistance (ODA) allocation.

The LIC/MIC thresholds are based on GNI per capita average income (exchange rate conversion) and have been adjusted every year for 'international inflation' since their establishment based on research.[2] One could argue that thresholds set in the 1970s are worthy of a substantial review, particularly in light of the availability of some 40 years of new data. At a minimum one could ask: (i) whether the use of 'international inflation' ought now to include China and other emerging economies in its calculation; and (ii) whether the use of 'international inflation' rates for the world's richest countries is an appropriate way to assess the LIC/MIC thresholds over time for the world's poorer countries which may have had inflation rates above the 'international inflation' rate. More fundamentally, one could also ask, as previously noted, whether the original formulae developed in the 1970s are still relevant to assessing the differences between countries today and, if not, what formulae would make (more) sense in terms of other methods such as purchasing power parity (PPP)? Alternatively, should such thresholds be instead (i) applied at a different level – for example, sub-national level (so poorer states in India would qualify); or (ii) *simply discarded outright* in favour of a more sophisticated way of thinking about development assistance and cooperation (see later discussion)?

So, how sensitive are the findings to the thresholds? Of course, the LIC/MIC thresholds are arbitrary lines but how sensitive is the overall picture to those thresholds? Of the new MICs, several are close to the LIC/MIC threshold, notably Lesotho, Nicaragua, Pakistan, Senegal,

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[2] For more detail see Sumner (2010). According to the short history of the Bank's classifications available on their website (World Bank 2011a), the actual basis for the original thresholds was established by: finding a stable relationship between a summary measure of wellbeing such as poverty incidence and infant mortality on the one hand and economic variables including per capita GNI based on the Bank's Atlas method on the other. Based on such a relationship and the annual availability of the Bank's resources, the original per capita income thresholds were established.

Vietnam, and Yemen. These account for 64.7m of the world's poor. This would mean 4.8 per cent of the world's poor live in countries near the LIC/MIC threshold – not significant enough to change the overall picture though important to recognise nonetheless. Similarly, if the slightly higher threshold – the 'IDA allocation' threshold (used for IDA resource distribution) – was used instead of the LIC/MIC thresholds, it would not make much difference. This is because although there are nine new MICs that are 'blend' countries (under the IDA allocation but above the MIC thresholds), only two – Pakistan and Vietnam – make any significant contribution to global poverty (together home to 55m poor people, according to unadjusted data in PovCal). To assess how sensitive estimates of global poverty are to thresholds, one approach that can be taken is to produce cumulative poverty counts for US$1.25 poverty and plot against GDP PPP per capita (see Sumner 2011a).

Using this approach one can apply any threshold of GDP PPP per capita and observe the difference it makes to global poverty distributions. This overcomes the mismatch between the Atlas (exchange rate conversion) method to construct 'poor countries' (LIC/MIC thresholds) and 'poor people' (the PPP methodology of US$1.25 poverty data). Of course, any threshold ought to have a solid conceptual basis (see later discussion and Sumner, 2011b, forthcoming). One could, for example, set thresholds based on applying the poverty lines for individuals and multiples of them to a country's average income as follows:

- Extremely LICs – countries with an *average income* of less than $1.25 per capita/day
- LICs – countries with an *average income* of less than $2.50 pc/day
- LMICs – countries with an *average income* of less than $5 pc/day
- UMICs – countries with an *average income* of less than $13 pc/day (the poverty line in the USA)
- HICs – countries with an *average income* of more than $13 pc/day (the poverty line in the USA)

However, such an approach is open to the criticism that it simply replaces one set of arbitrary thresholds with another set, albeit a set that links to a measure of poverty.

So are MICs just poor countries by another name? Overall, it is evident that MICs (Lower and Upper MICs) have higher standards of living than LICs and are far less aid-dependent (see Table 2). The average, population-weighted, GNI per capita – by Atlas or PPP – in LMICs is quadruple that of LICs; the average human development score is significantly better in LMICs compared to LICs (including and excluding non-income components) and the average poverty headcount (percentage of population) in LMICs is half that of LICs. Further, the removal of China and India or the PINCIs group of five countries where world poverty is concentrated (Pakistan, India, Nigeria, China and Indonesia) from LMICs does not make much difference to human development indicators for the LMICs. The removal of the PINCIs substantially reduces the average poverty headcount in the LMICs however. Finally, LMICs have much lower ODA dependency data than LICs. The removal of China and India or the PINCIs raises the aid dependency indicators but to levels still far lower than that of the LICs group.

Table 2 Human development indicators in LICs, LMICs and UMICs (population-weighted)

Indicator	Data periods	LICs	LMICs	LMICs minus China and India	LMICS minus China, India, Pakistan, Nigeria and Indonesia	UMICs
GNI per capita (Atlas, current US$)	2009	494.5	2276.3	1851.4	2112.7	7480.3
GNI per capita (PPP, current international $)	2009	1156.5	4703.6	3769.0	4370.0	12494.9
Human Development Index	2010	0.39	0.58	0.55	0.58	0.71
Non-income HDI	2010	0.46	0.62	0.60	0.63	0.74
Poverty headcount (% population, US$1.25) (non-adjusted base years)	2000-2007	52.4	27.1	25.4	15.6	5.2
Net ODA received (% of GNI)	2008	12.3	0.6	1.5	2.2	0.2
Net ODA received (% of gross capital formation)	2008	51.3	2.0	5.8	7.8	0.9

Source: Data processed from World Bank (2010, 2011b); data refer to the most recent available data within that period and if there are no data between those periods, then that data point (for a particular country, for a particular indicator) is ignored; all table lines are population-weighted as follows: (sum of (indicator x country population))/total population of countries with data on that indicator); correlations use the most recent data in the periods stated (Atlas GNI pc, 2009; HDI 2010; Non-HDI 2010; Poverty headcount 2000–2007).

Implications for external actors working in middle-income countries

If we accept the proposition that most of the world's extreme poor already live in largely non-poor countries, in order to meet their own objectives of reducing poverty, external development actors such as 'traditional donors' (meaning OECD countries), philanthropic foundations, governments and civil society will need to find new configurations of relationships (or they could decide poverty in MICs is not their problem). If they remain focused on extreme poverty, external development actors will need to continue work in the new MICs because most of the world's poor live in MICs, but they will need a greater focus on issues of equity/inclusion/exclusion; working with advocacy groups and civil society on issues such as public spending priorities but with great sensitivity to the politics of doing so and recognising that development is very much 'beyond traditional aid' (meaning beyond international resource transfers). Global Public Goods (GPGs), innovative finance mechanisms and other 'beyond traditional aid' modalities will be areas where MIC governments, traditional donors and philanthropic foundations can work together and the policy coherence, in areas such as trade, of traditional donors will be more important to MIC governments than aid flows. All of this will place far more importance on external actors understanding the political dimensions of development.

Furthermore, in the discussion so far the emphasis has been on MICs as a grouping of similar countries. Within this grouping, however, there are clear differences, particularly in regards to the need for ODA. For example, there are ‘emerging’ powers, such as India and Indonesia that have little need for ODA but still have substantial poor populations. Large fragile MICs, such as Nigeria and Pakistan, also have large numbers of poor people and may have limited need for ODA, but state capacity for poverty reduction and public health programmes is a significant constraint. Stagnant, non-fragile MICs may need ODA to support productive capacities, including human capital investments in health and education, and there are also fast-growing LICs which will graduate to MIC status soon. This heterogeneity suggests that approaches to MICs countries will need to be tailored to types of MIC as well as differ from those adopted in LICs.

The need for attention to equity/inclusion/exclusion issues, politics and the rapid expansion of the middle classes in MICs

Inequality has moved up the policy agenda in some of the major international organisations (for example, UNICEF (2011) and UNDP (2011) leading the wider UN body but also the World Economic Forum (2011) and the International Monetary Fund (2011)). The basic case is that inequality matters because high inequality can inhibit growth, discourage institutional development towards accountable government and undermine civic and social life, leading to conflict, especially in multi-ethnic settings (Birdsall 2006).

The impact of inequalities on growth has received considerable attention. For example, Berg and Ostry (2011) in a recent IMF paper note that high inequality impedes the sustainability of growth spells. This resonates with the earlier work of Cornia *et al.* (2004) that identified critical threshold levels of inequality – showing that rising inequality above a gini value of 0.45 retards GDP growth significantly.

Inequality has also been linked to fragility and conflict (Cramer 2003; Stewart *et al.* 2011). In terms of poverty, as shown by the extensive review by Dercon and Shapiro (2007) of long-run data sets, the key explanations for escaping from poverty are largely equity-related: changes in economic and social assets (e.g. changes in employment, land ownership and education) and/or social exclusion and discrimination and/or location in remote or otherwise disadvantaged areas.

The decline of inequality in a number of Latin American countries in particular over the last decade has led to a range of papers seeking to understand what development actors can do to reduce inequality.[3] What policies are behind these changes in inequality? Birdsall *et al.* (2011: 14) have argued empirically that ‘social democratic’ regimes (e.g. Brazil, Chile and Uruguay) are more likely to reduce inequality than ‘left populist’ ones (e.g. Argentina, Bolivia, Ecuador, Nicaragua and Venezuela) and both are more likely to reduce inequality than non-left regimes (e.g. Colombia, Costa Rica, Mexico, and perhaps Peru). They argue that this is due not only to more social spending but also to more progressive public spending and policies overall. It is also due to macroeconomic policies, especially so in the social democratic regimes. On the social spending side, this includes spending on cash transfers targeted at the poor in the bottom expenditure groups and greater increases in spending on health and education that reach the

[3] Lopez-Calva and Lustig (2009) have observed inequality that has declined in 13 of the 17 countries with comparable trend data. Whilst Palma has argued that the countries in Latin America with the worst income distribution in 1985 (Brazil, Chile, Guatemala, Nicaragua and Panama) have reduced inequality but only by a relatively minor amount and those countries with lower inequality in 1985 (Uruguay, Costa Rica, Argentina and Mexico) have actually increased inequality over the last 25 years.

lower and middle quintiles, as well as increases in basic services. But it also includes spending on education, with greater increases in spending on primary and secondary schooling than on public universities.

Cornia (2010: 86) also links observed declines in income inequality in some Latin American countries to the election of new political regimes and ‘the changes in economic and social policies part of the “new Left-of-Centre Latin American model” that has been gradually taking shape during the past decade’.

López-Calva and Lustig (2009) concur that improved provision of education has been a key factor in recent declines in inequality. More broadly, government spending on transfers became more progressive in the 2000s in all of these countries, which has led to improvements in health, nutrition and basic infrastructure as well as education: these programmes have had a significant impact on poverty.

Changes in labour earnings and labour policies can play a central role in reducing inequality. In Brazil, Barros *et al.* (2009: 1) find that,

> half of the decline in labour earnings inequality was caused by an acceleration of educational progress, which took place in Brazil over the last decade. The other half of the decline in labour earnings inequality came from labour market integration. Given that the minimum wage sets the floor for unskilled workers’ earnings, and for social security benefits, one might imagine that the recent increase in the real value of the minimum wage is one of the forces behind the overall income inequality decline in Brazil.

Indeed, the reproduction of inequality is narrowed down to five variables using the case of Brazil: father’s education; mother’s education; father’s occupation; race; and region of birth. Parental education is the most important circumstance affecting earnings, but the occupation of the father and race also play a role (Bourguignon *et al.* 2007).

Cornia (2011) argues that changes in inequality have been driven by changes in the remuneration of production factors and changes in transfers received and taxes paid by each household on different income types, noting (pp2–3), ‘Generally, the bottom percentiles of households receive most of their incomes from unskilled labour and transfers and the top ones from skilled labour and capital income’. Cornia (2011) argues that income inequality rose between 1980 and 2000 as a result of trade, foreign direct investment and financial liberalisation and a rise in migration. In contrast, the fall in inequality between 2000 and 2008 in Latin America, for example, was due to policy interventions such as: the equalisation of the distribution of human capital targeted social spending; changes in tax/GDP ratios; labour markets (rising real minimum wages, after two decades of declines + growing number of people covered by formal contracts and stable average wages); macroeconomic stability and exchange rates (no financial crisis and low inflation and public debt); and other factors. Cornia (2010: 86) notes factors explaining the decline in inequality in Latin American countries (LACs), 2002–7 as follows,

> the favourable external environment of 2002–2007, the rapid regional growth of GDP during this period, the longer-term improvements in human capital formation and in its distribution, and the changes in economic and social policies part of the ‘new LOC Latin American model’ that has been gradually taking shape during the past decade… Other important changes that are less frequently emphasized in the literature were recorded starting from the mid-1990s. The first concerns the steady gains in educational achievements realized since the beginning of the 1990s by both center-right and left-of-center (LOC) regimes – both social-democratic and populist – and the parallel decline in many aspects of educational inequality... The second change is the slowdown in the growth of the labor force… Together with a faster growth of labor demand for unskilled workers and in the supply of skilled workers, the slower

> increase in unskilled labor supply possibly contributed to reducing unemployment and halting the long-term rise in the wage premium. The third, and possibly most important, change concerns the shift towards democratization and the election of LOC governments. Indeed, during the past decade the political center of gravity of the region's shifted with surprising regularity towards political regimes that place greater emphasis on distributive and social issues while, at the same time, avoiding the populist excesses of the 1980s.

It is worth remembering that the amount of redistribution required to end poverty is often small in middle-income countries (typically less than 1 per cent of GDP – see Sumner, 2011b). Ravallion (2010) has argued that most countries with an average per capita income over $4,000 would require very small additional taxation to end poverty (as an example, Palma (2011) cites Brazil's *Bolsa Familia* which he notes distributes US$50/month to 11 million families at a cost of about 0.5 per cent of GDP in 2005) and Soares *et al.* (2011) find that due to 'outstanding' targeting, Conditional Cash Transfers in Brazil, Mexico and Chile have cost less than 1 per cent of GDP and have accounted for 15–21 per cent of the reduction in inequality.

In short, the capacity to redistribute may become an important issue for poverty alleviation in middle-income countries. Thus a better understanding of the redistributive preferences of the expanding middle classes in MICs will be important for all development actors.

Despite differences in defining the middle classes, general trends suggest that the middle class (or at least those who are not extremely poor and not wealthy) has been expanding, especially so in MICs, and will continue to do so in the coming decades assuming growth continues. AfDB (2011) and ADB (2010) with the definition of $2–$20/day per capita income, respectively estimate the African middle class to be 313m or 1 in 3 (34 per cent) of Africans and the developing Asian middle classes to be at least 1.9bn or 56 per cent of the population of developing Asia. The growth in the size of the middle class is largely driven by a number of Asian countries whose populations are graduating out of poverty and into the middle classes. However, it is much wider than just India and China.

OECD (2011) discusses in some considerable detail this issue of middle-class preferences for the amount and type of income redistribution and redistributive fiscal policy. It notes that if public services are of low quality, the middle classes are more likely to consider themselves a loser in the fiscal bargain and less willing to contribute to financing the public sector. Other factors that determine preferences in redistribution are noted from the literature, including: personal experiences of social mobility; national and regional cultural and social values; the extent of impacts of (higher) taxation on leisure consumption; levels of university education; and attitudes to prevailing levels of meritocracy. Support for redistribution is undermined by low institutional capacity in tax administration and the quality of state services and pessimistic views about social mobility.

All of the above would suggest that the policy levers for tackling poverty and inequality are clear enough and include addressing more structural and institutional factors such as setting minimum wages, and increasing the level and progressive weighting of social spending, notably through cash transfers. However, building and understanding middle-class political support (or lack of it) for such measures (and taxation) will be of importance to governments, civil society, donors and philanthropic foundations.

Table 3 Comparable estimates of the size of the middle classes ($2–$20/day, household survey data)

	Millions			% of population		
	1990	**2000**	**2005–9**	**1990**	**2000**	**2005–9**
Africa	151.4	196.3	313.3	27.0	27.2	34.3
Sub-Saharan Africa	66.0		129.9	24		33
Developing Asia						
East Asia and Pacific	565.3		1894.9	21.0		56.0
China				40.4	71.3	89.1
India			274.1			24.6
Latin America and Caribbean	250.2		349.7	71.0		77.0

Sources: AfDB (2011: 21), ADB (2010: 6).

Working with advocacy groups and civil society on issues of equity/ inclusion/exclusion in MICs

Given the above, working with advocacy groups and civil society actors to influence policy on matters such as public spending priorities is one avenue through which external development actors can pursue their aims of poverty reduction. Within most if not all countries, there are various actors and organisations pushing for progressive change (however defined). We can note, for example, civil society organisations (CSOs), women's organisations, social movements, workers' unions, rights-based organisations and independent media as all playing important roles in the mission to promote progressive agendas. But what role can external development actors play in supporting these elements of civil society? There is little point in pretending that this does not cross over into the political domain – indeed, this constitutes an explicitly political approach infused with liberal values. For example, Hearn (1999) finds that CSOs committed to the promotion of liberal democracy and economic liberalism are the most popular with donors. Yet donors also link into global citizenship movements, underpinned by universal human rights. As Eyben *et al*. (2004: 24–25) point out, tensions within aid relationships appear to be particularly striking in middle-income countries: 'many of the larger MICs have more complex and diverse institutions both within and outside government and donors can find themselves involved in internal political conflicts through the choice of whom they decide to associate with'.

On this approach, there is a considerable body of literature on civil society in developing countries to draw upon (see, for example, Frantz 1987; Hadenius and Uggla 1996; Howell and Pearce 2000; Robinson 1995), as well as the 'drivers of change' approach and numerous case studies (see for discussion DFID 2005; OECD-DAC 2005; Moore 2001; Warrener 2004).

And, of course, efforts to support Southern-based CSOs are not new. For example, Howell and Pearce (2000: 75) remarked more than a decade ago that there was considerable funding for projects to strengthen CSOs in developing countries. In addition, strengthening and increasing the visibility of civil society in policymaking processes was a core element of PRSPs (Molenaers and Renard 2002).

Given the new context of high MIC poverty levels, how can external development actors use and adapt existing frameworks for engagement with civil society? Howell (2000: 7) outlines three broad approaches that donors have traditionally adopted in order to support and develop civil society: institution and capacity building; partnerships and coalitions; and financial sustainability. In practice, she explains, these approaches are not clear-cut and tend to overlap. The third donor approach outlined above by Howell – (ensuring) financial sustainability – highlights the importance of the material bases of CSOs and other organisations. The performance and impact of many, if not most, CSOs tend to be constrained by insufficient resources (e.g. money, time). And as Howell (2000: 8) points out, the opportunities for Southern-based NGOs and CSOs to fundraise domestically are limited due to their countries' high poverty levels and low levels of economic development.

There are, of course, numerous, potential problems associated with externally funded CSOs. For example, to what degree will external assistance influence or manipulate an organisation's political agenda? Do CSOs risk having their views and actions delegitimised by accepting foreign assistance? Robinson and Friedman (2007) investigate how far external donor funding influences the policy engagement and outcomes of a selection of CSOs in Uganda and South Africa. Regarding the South African CSOs, they find that the source of funding, whether internally generated or externally supplied, does not seem to be a significant factor in explaining their differential policy impact (Robinson and Friedman, 2007: 659). Further, they find that one CSO in particular receives 90 per cent of its funding from foreign sources, but manages to maintain a high degree of independence in framing agendas whilst significantly contributing to public policy (Robinson and Friedman 2007: 660). Meanwhile, in Uganda they report a more mixed set of results. For example, one organisation has experienced internal ideological and factional divisions and had its viability and independence undermined by its reliance on foreign aid. Additionally, it is argued that one CSO's limited contribution to national policy debate cannot be explained by its dependence on donor funds (Robinson and Friedman 2007: 661). In conclusion, they claim that,

> Foreign aid is not the most critical determination of successful policy engagement; the character of a particular organization and its specific relationship to the state are decisive. But resources do matter, since the least effective organizations in terms of policy engagement… are also the least well-endowed financially.
>
> (Robinson and Friedman 2007: 663)

In terms of funding CSOs, Robinson and Friedman (2007: 665) suggest four measures donors can take to strengthen the organisational capacity of CSOs: replace short-term project support with long-term program grants and technical assistance; provide specialised assistance aimed at strengthening capacity for policy analysis and advocacy; encourage the adoption of strategies designed to identify and institutionalise local sources of funding; and encourage governments to remove restrictive controls and simplify NGO registration procedures, thus promoting a more supportive policy environment for CSOs. Their third proposed measure is consistent with Aldaba *et al*.'s (2000: 678) argument that one of the ways NGOs can become self-sustainable in a 'beyond aid scenario' is by taking better advantage of domestic resource options.

Donors can also engage in 'partnership work' in middle-income countries. Eyben *et al*. (2004: 14) describe how a very small financial investment in strengthening the relationships between a country's state government, its civil society, and donors can bring about significant shifts in social policy. Larbi-Jones (2004), for example, points to DFID's work on partnerships in Brazil. This also brings to the fore questions of positioning. As Fowler (2000a, 2000b: 595) argues, NGOs/CSOs in developing countries need to carve out a space for themselves. In addition, external development actors should think carefully about the *local* political economy of aid. In a study of aid interfaces and the role of local elites in Nicaraguan rural villages, D'Exelle (2009: 1468) finds that 'village brokerage structures, as part of the interface with aid providers, are strongly correlated with recurrent exclusions from aid flows', and that the poorest are disproportionately affected. Pushing for political change – decentralising the brokerage structures – can thus be justified by its potential to reduce poverty.

Aid to MICs might entail supporting processes that have the potential to reduce rather than reinforce patterns of exclusion. This involves building *long-term* and *consistent* relationships with selected recipient organisations with social change agendas (e.g. local NGOs, community-based organisations, cooperatives etc.) (Eyben *et al.* 2004: 14), and gaining a deeper understanding of context. This means that working in MICs becomes a fundamentally more political undertaking for external development actors and, as such, external development actors will be required to involve themselves more intimately with domestic political processes, something they have tended to be unsure about doing in the past (Eyben *et al*. 2004: 15). Further, such activities may not be well received by MIC governments who may perceive it as interference in domestic political affairs.

The rapidly declining importance of aid as resource transfer to MICs and the prospects for global public goods, innovative finance mechanisms and other 'beyond aid' modalities as focal points where MIC governments, traditional donors and philanthropic foundations could work together

Aid has traditionally been seen as resource transfers of grants or concessional lending (e.g. OECD 2010: 2). However, the range of available aid instruments is constantly expanding and diversifying with the emergence of both 'upstream' aid products/instruments (e.g. policy coherence in trade, climate, migration/remittances; advocacy for and support to independent media and CSOs; and global public goods), as well as 'downstream' aid products/instruments (e.g. project aid or programme aid for service delivery) and completely new financing mechanisms that include private and public contributions in the form of various innovative finance mechanisms. All of this might suggest 'aid' is no longer the right word to describe what might accurately be termed 'international cooperation'.

Severino and Ray (2009) have argued that our conventional understanding of ODA is looking more and more outdated, becoming increasingly irrelevant as a tool for action. Severino and Ray (2009) discuss a 'triple revolution' in ODA in terms of goals, players and instruments (all mushrooming), and question the validity of the current definition of ODA (i.e. in terms of loans and grants from governments). Key issues of the moment, and possible future 'game changers', include: the emergence and rise of new non-DAC donors (accounting for at least 10 per cent of global ODA according to UN ECOSOC 2008) and other actors such as private foundations; new financing and delivery modalities, such as innovative finance mechanisms, and climate financing; and the creation of new institutions such as cash-on-delivery and output-based aid (see Birdsall and Savedoff 2010). In short, the very definition of what aid is and what it hopes to achieve are on the table for discussion, and the path is potentially set for the design of a new kind of development assistance which is tasked with three conceptually distinct subsets of objectives: first, accelerating the economic convergence of developing and industrialised countries; second, providing for basic human welfare (guided predominantly by the MDGs); and third, finding solutions for the provision and preservation of global public goods (Severino and Ray 2009: 5).

Yet, since the 1990s, there has been an end to the state's monopoly over development assistance. Not only have the size and number of major international NGOs (e.g. Oxfam) expanded but we have also begun to witness the emergence of a range of new actors, from private foundations (e.g. the Gates Foundation) and businesses (e.g. Project (RED)), to transnational thematic funds (e.g. GAVI). Additionally, there is now an array of different sources of funding and aid channels. For example, recently, at the 2010 MDGs Summit, the Leading Group on Innovative Financing for Development proposed a 'Global Solidarity Levy' which would be used to finance global public goods (Giovannetti 2010: 50).

Innovative financing mechanisms (IFMs) and climate financing are two particular areas receiving increasing interest both in policy and academic arenas (see, for example, de Ferranti 2006; Jones 2010; Ketkar and Ratha 2009; Lob-Levyt and Affolder 2006; McCoy 2009). Such initiatives represent a marked departure from existent and past means of development financing (e.g. ODA) and 'traditional' donor-recipient arrangements, and, in many cases, are successful at engaging new stakeholders and different kinds of donor networks.[4]

Furthermore, GPGs are likely to be increasingly important in a world of global collective problems such as climate change. Traditionally, donor assistance has typically done less to supply GPGs (Barrett 2002). However, te Velde *et al.* (2002) find that donors with large aid budgets tend to be those that also have a larger share of GPGs in their aid portfolios. New interest in international or global public goods is fuelled, in part, by an understanding of globalisation and its impacts (Ferroni and Mody 2002). The main rationale behind providing GPGs is to regulate or compensate for the negative effects of global public 'bads', or 'products' which generate negative externalities across borders and reduce utility (Coyne and Ryan 2008: 5), such as air pollution, civil war and violent conflict, disease, HIV/AIDS, international terrorism, and financial shocks.

According to Kaul *et al*. (1999: 2–3), GPGs must meet two key criteria. First, their benefits must have strong 'publicness' (i.e. they are characterised by non-rivalry in consumption and non-excludability). And second, their benefits must be at least quasi-universal in terms of countries, people, and generations. Meanwhile, Ferroni and Mody (2002: 1) argue that international public goods are primarily about three things: the rules that apply across borders; the institutions that supervise and enforce these rules; and the benefits that accrue without distinctions between countries (i.e. the (quasi) universality criterion noted above).

The provision of GPGs is particularly important not only because of the globalised nature of the contemporary world but also because markets do not generally have sufficient incentives or the ability to allocate the necessary resources to public goods (Ferroni and Mody 2002: 2). Governments too, when acting in isolation, are unable to provide them. GPGs can originate in both rich and developing countries – for example, while developing countries can contribute significantly towards climate change mitigation efforts, much funding for medical research, which feeds into health GPGs, is targeted in rich countries with the appropriate infrastructure (te Velde *et al*., 2002: 120). However, the penetration, sustainability and impact of GPGs hinge on negotiations and agreements at the global level. As Barrett (2002: 73) points out, GPGs cannot usually be supplied by governments acting unilaterally; cooperation is typically needed. International organisations can play a key role in helping to build these relationships through their ability to convene, their ability to generate and transfer knowledge, and their ability to assist global and regional negotiations (Ferroni 2001: 13).

Yet Kaul *et al.* (1999: 450–1) argue that GPGs tend to be underprovided due to three 'gaps' within public policymaking processes: a jurisdictional gap (i.e. the discrepancy between the global boundaries of major policy concerns and the national boundaries of policymaking); a participation gap (i.e. we live in a 'multi-actor' world but international cooperation remains primarily intergovernmental); and an incentive gap (i.e. there is not a strong enough case for countries to

[4] IFMs are incredibly diverse, ranging from airline and tobacco taxes and advance market/purchase commitments, to global public-private partnerships and health funds. Many adopt explicitly market-based approaches, and many attempt to integrate consumers and the private sector more directly in the development financing process. While expectations of IFMs are high (Jones 2010), robust assessments and evaluations are to date somewhat limited.

address their international spillovers or to cooperate on a GPG agenda). The (potential) supply of GPGs also takes place within an 'anarchic legal setting', making agreements at the international level difficult to thrash out (Barrett 2002: 48). Further, the successful supply of GPGs may rest on the resolution of conflicting interests at the national level. Combating climate change is arguably one of the most widely discussed examples of a GPG, but past summits and conferences (e.g. Kyoto) have only seen limited success.

GPGs are particularly important with respect to the engagement of donor and philanthropic foundations with middle-income countries. Indeed, MICs themselves constitute key players in the supply of GPGs and forging and developing partnerships with MICs is increasingly important for global collective action. Engaging developmentally with MICs is thus seen as an end in itself (i.e. achieving poverty reduction in those countries), as well as a means to providing GPGs. We can therefore conceptualise GPGs in two ways: as a policy framework for engagement with MICs; and as fundamentally contingent on the actions and cooperation of MICs. Of particular relevance to the earlier discussion on aiding FCAS, Coyne and Ryan (2008) examine the possibility of foreign intervention in order to minimise global public 'bads' such as civil war (and the arguments could extend to global poverty). One could also note the parallel with the 'responsibility to protect' (R2P) in humanitarian assistance.

MICs are also central to the supply of regional public goods (Ferroni 2001) and, indeed, to the supply of regional public bads. For example, Fallon *et al.* (2001) describe how the spillover effects of the East Asian crisis affected the whole global economy and Rostoski (2006: 541) discusses the role of regional 'anchor countries' and 'locomotives', such as China, Indonesia and Thailand, claiming that cooperation with such countries produces positive effects for their neighbours.[5]

A range of IFMs have been designed and implemented already, many of which relate to GPGs or at least regional, cross-border instruments and international or regional collaborations. Aside from some of the more well-known new institutional approaches to global health, such as the GAVI Alliance Fund, UNITAID is an initiative financed almost solely through airline ticket solidarity contributions. Other examples of innovative financing include: drug donation programmes (Liese *et al*., 2010); the Millennium Vaccine Initiative, which has channelled US$1 billion in tax credits to corporations in order to promote delivery of existing vaccines and accelerate development of new vaccines for developing countries (Stansfield *et al*. 2002); Debt2Health (IFM Working Group 2, 2009); and the auction of greenhouse gas emissions permits, most notably taken up by Germany (IFM Working Group 2, 2009). On top of these there are also initiatives such as the International Health Partnership Plus (IHP+), which aims to strengthen national health systems, and Global Health Partnerships, for instance in Rwanda, which bring together reforms in financing with reforms in service delivery (Sandor 2008).

Analysts point to the potentially huge revenues – for instance, US$6–11bn from a tobacco tax in high-income countries (IFM Working Group 2, 2009) – as well as long-term sustainability of revenue flows and awareness raising. They also describe other benefits, from harmonisation of health systems flows (through a Health Systems Funding Platform) and increases in efficiency of private health sectors (through Seed Mechanisms), to double or even triple dividends associated

5 Regional public goods are similar to GPGs; the main difference is spatial and scalar (although of course this also entails working within different legal and strategic frameworks). Kanbur (2001) distinguishes three kinds of activities to pursue regional public goods. First, non-country-specific investments in knowledge, dialogue, research into technologies, and negotiation of agreements on shared standards and policy regimes. Second, inter-country mechanisms for managing negative cross-border externalities and/or for creating beneficial ones. And third, country-specific action to take advantage of the benefits created under the two modalities above. The groundwork for pursuing regional public goods has arguably already been laid down in the shape of regional trade blocs and regional integration schemes; working through and building on these could facilitate the creation of greater spillover communities.

with tobacco taxes and global environmental taxes (reduced number of smoking-related diseases and reduced carbon emissions respectively).

Relative to the range of IFMs already in place, the number of proposed options or options in the pipeline is substantial. Other proposed initiatives include: procurement mechanisms whereby purchases of health products are pooled; mobile phone voluntary solidarity contributions; a global lottery endowment; and taxes on arms sales (Atkinson 2005; de Ferranti *et al*. 2008; Jha 2004; Ratha *et al*. 2008).[6]

In sum, if most of the world's poor live in MICs, external development actors could refocus on equity/inclusion/exclusion issues, working with advocacy groups and civil society to influence policy such as public spending priorities and with MIC governments on GPGs, innovative finance and other 'beyond aid' questions.

Conclusions

To reiterate from the introduction, the shift in the distribution of global poverty can be viewed in three possible ways. First, it could all be a sleight of hand – the world's poor still live in 'poor' countries, albeit slightly less poor than before. Second, it is business as usual because there are limits to domestic taxation on the rich and expanding middle classes in developing countries. Or third, this shift could mean that a fundamental reframing of global poverty is required, 'traditional aid' (resource transfer) is no longer relevant and global poverty is now about equity/inclusion/exclusion, advocacy coalitions and 'beyond traditional aid' questions such as global public goods.

If we accept that the third view will increasingly be the case in the years ahead and if external development actors want to reduce global poverty, they will need to work in MICs but with new objectives and policies and partnerships (or alternatively, focus on LICs alone and the quarter of the world's poor who live in LICs). Working in MICs will inevitably lead to more political tension – on spending priorities, political voice, policy coherence; this will mean that external development actors will need more political analysis.

The analysis of the data that world poverty is turning from an international to a national distribution problem, means that governance and domestic taxation and redistribution policies are becoming more important than ODA (and new MICs may not want development assistance of the traditional bilateral sort). Aid to low-income countries will still be about resource transfers and increasingly about fragility, conflict, and post-conflict, but this will be for a minority of countries. Middle-income countries are less and less likely to need or want resource transfers over time; instead, they will probably be more concerned with 'policy coherence' from traditional donors. MICs may be more concerned with designing favourable and coherent development policies on remittances and migration, trade preferences, and climate negotiations and financing, as well as tax havens. Further, it is unlikely that taxpayers in donor countries will be comfortable with resource transfers to countries that have substantial domestic resources.

6 Climate financing is likely to also lead to a new generation of financing mechanisms. Brown (2009) outlines five categories of proposals, including the auctioning of assigned amount or emission allowances (rather than distribution for free to 'Annex I' domestic firms that have to comply with emissions reduction) and the creation of carbon market-based levies, such as the 2 per cent CDM levy mechanism which is used to raise funds for the Kyoto Protocol's Adaption Fund. Other proposals include imposing levies on international maritime transport and on air travel, developing a uniform global tax on CO_2 emissions (with a per capita exemption for least-developed countries) and the issuance of bonds on international markets. These proposals are all means of creating new mechanisms to generate new and additional resources for addressing adaptation (and some mitigation activities) that are separate from and additional to existing ODA (Brown *et al*. 2010).

At the same time, external development actors are likely to be increasingly concerned about equity and governance issues – and drivers of progressive change. It is true that many middle-income countries may be able to support their own poor people to a certain extent, but inequality remains an important issue. Poor people often lack a voice in governance structures, and their governments may lack political will, even when domestic resources are on the rise. In such cases, traditional donors might seek to direct their activities towards supporting inclusive policy processes and the media, social movements, advocacy groups and civil society organisations, and other drivers of change. Doing so may not be well received by MIC governments; many of them will be donors themselves and perhaps less interested in ‘progressive (domestic) change’ and more in their foreign and economic policy interests as noted above. The main area of agreement might be in global public goods, where interest in collective action on security, climate change, and other global issues is shared. The other issues could include defining global poverty as a global public ‘bad’ that requires collective action, although specific political and economic interests over who contributes and who benefits differ among countries.

In the meantime continued donor relationships with MICs are justified on the grounds of: high levels of exclusion and inequality; domestic constraints (e.g. inadequate tax systems); need for technical expertise; and international and regional public goods. However, external development actors may lack financial leverage in MICs, so will need to find alternative means of supporting poverty reduction. This might involve engaging with civil society and NGOs. Such engagement is likely to be highly politically sensitive and donors will need to tread carefully, employing detailed understanding of political and economic conditions. External development actors will increasingly need to recognise that MICs have moved from being passive recipients of aid to being active participants in the international architecture. Indeed, many of the MICs may well be foreign aid donors themselves. The changing dynamic entails a need to rethink development assistance from a focus on poor countries to poor people and tailored to different types of context.

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