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POLICY GUIDANCE ON PROMOTING PRO-POOR GROWTH

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## PRO-POOR GROWTH: POLICY STATEMENT

1. The 2001 DAC Guidelines on Poverty Reduction show that poverty has multiple and interlinked causes and dimensions: economic, human, political, socio-cultural, protective/security. This policy statement focuses on one dimension of that bigger picture – reducing economic poverty through pro-poor growth. In doing so, it looks at the relationship between the economic and other dimensions of poverty and how policies for pro-poor growth and other policy areas need to interact so that, collectively, they can make major and sustainable inroads into poverty reduction.

2. **Three key messages from this work are that:**

- Rapid and sustained poverty reduction requires pro-poor growth, i.e. a pace and pattern of growth that enhances the ability of poor women and men to participate in, contribute to and benefit from growth. Policies therefore need to promote both the pace of economic growth and its pattern, i.e. the extent to which the poor participate in growth as both agents and beneficiaries, as these are interlinked and both are critical for long term and sustained poverty reduction.
- Policies to tackle the multiple dimensions of poverty, including the cross-cutting dimensions of gender and environment, are mutually reinforcing and should go hand-in-hand. Progress in one dimension will be accelerated by progress in others. In tackling poverty, perceptions of policy dichotomies have been misplaced. Policy trade-offs do exist but can be better managed.
- Empowering the poor is essential for bringing about the policies and investments needed to promote pro-poor growth and address the multiple dimensions of poverty. To achieve this, the state and its policy-making processes need to be open, transparent and accountable to the interests of the poor. Policies and resources need to help expand the economic activities of the poor.

3. When implementing the policy guidance on how donors can support and facilitate pro-poor growth, they must bear in mind that the poor are not a homogenous group, that country contexts vary considerably, and that policy implementation must be based on a sound understanding of who the poor are and how they earn their livelihoods. Promoting pro-poor growth requires policy choices to be guided by assessments of their expected impact on the income and assets of the poor.

4. ***Rapid and sustained poverty reduction requires pro-poor growth, i.e. a pace and pattern of growth that enhances the ability of poor women and men to participate in, contribute to and benefit from growth.***

- i) **Both the pace and the pattern of growth are critical for long term and sustainable poverty reduction.** Economic growth is an essential requirement and, frequently, the major contributing factor in reducing economic poverty. For growth to be rapid and sustained, it should be broad-based across sectors and regions and inclusive of the large part of the work force that poor women and men make up. Pattern and pace are thus interlinked and need to be addressed together. Policies for sustaining growth such as those aiming at macroeconomic stability, institutional quality, democratic and effective governance and a favourable investment climate should promote the engagement of the poor in economic growth by increasing their incentives, opportunities and capabilities for employment and entrepreneurship.

- ii) **A pro-poor pattern of growth makes growth more effective in reducing poverty.** Developing countries with similar rates of economic growth have experienced quite different levels of economic poverty reduction, due to initial conditions and whether growth occurs in areas and sectors where the poor live and are economically active. Policies need to create the conditions and remove the obstacles to the participation of the poor in the growth process, e.g. by increasing access to land, labour and capital markets and by investing in basic social services, social protection and infrastructure. As the poor often depend heavily on natural resources for their livelihoods, policies to promote environmental sustainability should also be integral to promoting pro-poor growth.
  - iii) **Inequality matters.** Inequality of assets and opportunity hinders the ability of poor people to participate in and contribute to growth. High and rising levels of income inequality lower the poverty reduction impact of a given rate of growth and can reduce the political stability and social cohesion needed for sustainable growth. Gender is a particularly important dimension of inequality. Women face particular barriers concerning assets, access and participation in the growth process, with serious implications for the ability of growth to be pro-poor. The growth experience shows that rising inequality is not an inevitable consequence of the growth process, as long as there is a mix of policies that addresses both growth and distributional objectives, strengthens empowerment and deals with gender and other biases (e.g. race, caste, disability, religion).
  - iv) **The vulnerability of the poor to risk and the lack of social protection reduce the pace of growth and the extent to which it is pro-poor.** The poor often avoid higher risk opportunities with potentially higher payoffs because of their vulnerability. In addition, the journey out of poverty is not one way and many return to it because man-made and natural shocks erode the very assets that the poor need to escape poverty. Policies that tackle risk and vulnerability, through prevention, mitigation and coping strategies, improve both the pattern and pace of growth and can be a cost effective investment in pro-poor growth.
  - v) **Policies need to tackle the causes of market failure and improve market access.** Well functioning markets are important for pro-poor growth. Market failure hurts the poor disproportionately and the poor may be disadvantaged by the terms on which they participate in markets. Programmes are needed to ensure that markets that matter for their livelihoods work better for the poor. Such programmes need to be carefully designed to avoid replacing market failure with government failure. Policies to tackle market failure should be accompanied by measures aimed at increasing economic capabilities of the poor.
5. ***In tackling poverty, perceptions of policy dichotomies have been misplaced. Policy trade-offs do exist but can be better managed.***
- i) **Policies to tackle the multiple dimensions of poverty should go hand in hand.** Poverty is multidimensional. Pro-poor growth will be strengthened by progress on the non-economic dimensions of poverty. More effective policies require a better understanding of these interdependencies. Perceptions of dichotomies (e.g. economic versus social policies) can be misplaced. The pace and pattern of growth have multiple determinants and consequences and each dimension nourishes (or holds back) the other. Progress on the income poverty MDG facilitates progress on other MDGs and vice versa.
  - ii) **Policy trade-offs still exist, but can be better managed.** Policies which promote only one dimension of poverty reduction while undermining others should be avoided. Whenever possible, policies need to be complementary rather than compensatory. Sequencing of policies and investments can help manage trade-offs. Policy choices should be based on understanding the binding constraints through analysis of the growth, poverty and inequality experience and the

results of poverty impact assessments. The ability of institutions to handle trade-offs is important for achieving pro-poor outcomes.

6. ***For pro-poor growth policies to emerge, the poor need to be informed and empowered to participate in a policy making process that is accountable to their interests.***

- i) **The poor need to participate in and influence the policy reform process that goes with poverty reduction strategies (PRSs).** Approaches are needed to increase the voice and influence of poor women and men in order that policy making is evidence-based, rather than determined by narrow vested interests.
- ii) **A well-functioning state is important for responding to the interests of the poor.** Effective pro-poor growth strategies need policy and institutional change for which the state, in all its dimensions, is made more accountable to the interests of the poor. The state needs to provide the opportunity for structured public-private dialogue at various levels, including with civil society and private sector actors who are frequently marginalised. The state needs to provide the required incentives, enabling environments and policy and planning frameworks to be more accountable to the voices of the poor.
- iii) Pro-poor reform is likely to require changes to the current political settlement among the diverse interests of different segments of society. This entails a better understanding of the political economy, power relations and drivers of change, and supporting formal, transparent decision making, strengthening the demand for pro-poor change and building capacity of the state to respond to demand.

7. ***For donors, the pro-poor growth agenda is not business as usual and more of the same will not be sufficient.***

- i) **Donors should focus on supporting in-country policy processes.** Policies for pro-poor growth can only be achieved through country-level processes that are inclusive of the poor and based on country-level analyses. Donors should support the emergence and development of processes that are formal, transparent and take account of the interests of the poor, and conduct their policy dialogue through them. Donors should support measures to empower the poor in these policy processes and build the country-level capacity to undertake analyses, including poverty impact assessments.
- ii) **Donor support needs to be flexible and responsive to country situations.** The type of support provided needs to take account of the level of development, the policy environment and the extent to which there is a well-functioning state. Donors need to adapt their approach to fragile and failed states and more research is required to inform this process.
- iii) A pro-poor lens on areas important for pro-poor growth, such as private sector development, agriculture, infrastructure and risk and vulnerability, requires a rethinking of donor agendas. The importance of these areas for the pace and pattern of growth has been underestimated. New approaches to strengthen the contributions of private sector development, agriculture and infrastructure have been developed by the DAC. Work on risk and vulnerability/social protection/human security is ongoing.
- iv) **Donors need to enhance their organisational capacities to effectively support country-led, pro-poor growth.** Donors need to provide appropriate support and incentives to field staff, build multi-donor and multidisciplinary teams at the field level, and empower them to negotiate, co-ordinate and implement programmes. Recent progress to establish such teams in several partner countries should be replicated.

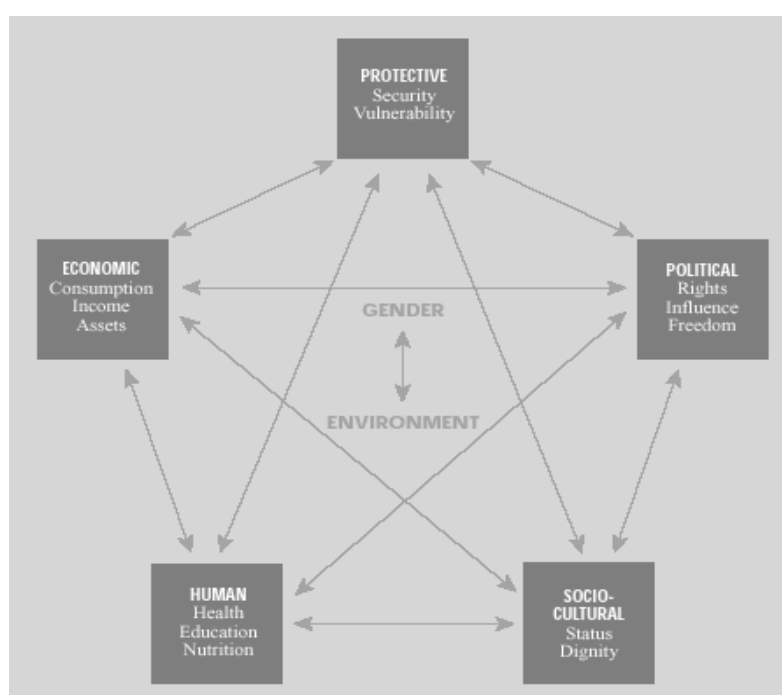
## CHAPTER 1

### INTRODUCTION

#### 1.1 The Multiple Dimensions of Poverty

8. The 2001 DAC Guidelines on Poverty Reduction show that the forms of deprivation that poverty takes, economic, human, political, socio-cultural and protective (security), are interlinked, and that gender equity and environmental sustainability cut across all the dimensions of poverty (See Figure 1).

**Figure 1. The Multi-dimensional Poverty Framework**



9. The focus of this report, is on one dimension of poverty - how to reduce economic poverty through pro-poor growth. As poverty is a set of interlinked forms of deprivation, it also addresses how progress on economic poverty may contribute to and be facilitated by progress on the other dimensions of poverty.

#### 1.2 What is pro-poor growth and why is it important?

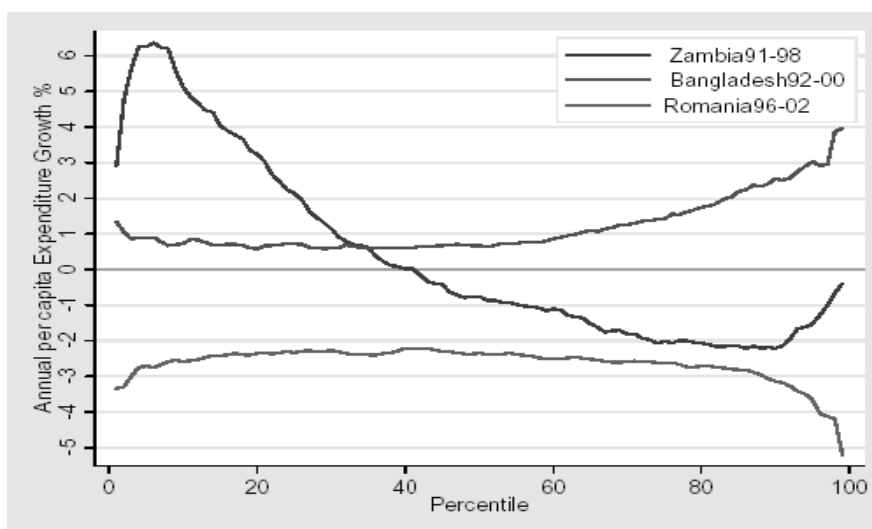
10. Reducing economic poverty is vital for over 3 billion people, roughly half the human race, with incomes less than \$2/day who are challenged to meet their basic needs – and even more crucial for the 1 billion people with incomes less than \$1/day, who struggle for survival. The experience of many developing countries in achieving economic growth and reducing poverty has been far from satisfactory. Large numbers of poor women and men have been able to escape economic poverty in countries such as China and India that have sustained high rates of growth. But in most developing countries, growth has been low and has not enabled the poor to lift themselves out of economic poverty. In terms of regions, Sub-Saharan Africa is in danger of not meeting the poverty reduction target of MDG 1 and Latin America has,

in recent years, experienced little reduction in income poverty. Even where, on the whole, growth and poverty reduction have been satisfactory, the evidence shows that a significant proportion of poor people have been marginalised in the growth process and have not been able to escape poverty.

11. Pro-poor growth focuses attention on the extent to which poor women and men are able to participate in, contribute to and benefit from growth, as measured by changes in the incomes of the households in which they live and the assets they and their children acquire to earn higher incomes in the future.<sup>1</sup> When may growth be termed pro-poor? There are different views on this issue. For some, what matters is whether the incomes of the poor are rising *relative* to the incomes of the non-poor and hence inequality is falling. The merit of this perspective is that it focuses attention on whether the poor are benefiting more or less proportionately from growth and whether inequality, a key determinant of the extent to which growth reduces poverty, is increasing or falling. For others, what matters most is the *absolute* rate at which the incomes of the poor are rising. For example, are the incomes of the poor rising fast enough to reduce the number of people living below the international poverty line in accordance with MDG 1:1?

12. The relative and absolute concepts of pro-poor growth are both relevant, and complement each other in the analysis of growth processes from a pro-poor perspective. In fact, the tools needed to analyse how the poor are participating in and benefiting from growth may be used with either definition. This may be illustrated by "growth incidence curves" (GICs), which plot how the incomes (or expenditure) of households at different levels of income have changed over a given time period (see Figure 2) revealing both absolute and relative changes in incomes.<sup>2</sup> Figure 2 shows that in Zambia the poor benefited from growth in absolute and relative terms (even though growth was weak), whereas in Bangladesh better-off households benefited more than the poor.

Figure 2. Selected growth incidence curves



Source: McKay, 2005



### 1.3 The Importance of Context

13. Developing effective strategies to reduce poverty requires an understanding of who the poor are and how they earn their livelihoods. The poor are not a homogenous group with poverty incidence varying with gender, membership of social groups, regions in which they live, urban as opposed to rural households and so on. And poor men and women pursue a diversity of strategies to earn their livelihoods. For example, though some two thirds of the world's poor live in rural areas, there are a wide range of "rural worlds" that offer different opportunities to earn livelihoods from agriculture and non-farm occupations. Strategies to increase pro-poor growth must take account of these differing opportunities to earn incomes. The country context is also crucial for developing effective strategies. The world's poor live in many different settings – in large, middle-income countries, having been marginalised by the growth process; in the low-income countries where growth has historically been low; and one-third of the world's poor live in 'fragile states' where the state does not function effectively. These variations require adapting the strategies described below to suit the particular context.

14. A thorough understanding of the growth/inequality/poverty experience is essential for adapting strategies to the context. A wide range of tools may be used to analyse the growth/inequality/poverty experience, as shown in Box 1.

#### **Box 1. Tools for analysing the linkages between growth, inequality and income poverty**

Tools which may be used for this kind of analysis include the following:

- i) Disaggregating growth to identify macro-micro linkages (GDP growth in relation to household income growth) and identify the sources of growth in terms of sectors, types of expenditure (consumption, investment etc), and increases in factor inputs (labour, capital) and their productivity and so on;
- ii) Examining the spatial distribution of growth (e.g., regions, urban-rural), changes in employment patterns (e.g. participation rates for women and men, sectors of employment, formal versus informal employment, unemployment) and wages/incomes derived from them;
- iii) Disaggregating changes in poverty and inequality using GICs to understand distributional impacts, adapting them to understand poverty and inequality experiences of different types of households (e.g. female and male headed, members of different social groups, urban versus rural households, region of residence), decomposing the contribution growth and changes in the distribution of income make to the incomes of the poor, calculating the average growth in the incomes of the poor and comparing it with the non-poor and similar countries.

Source: McKay, 2005.

### 1.4 The Structure of the Report

15. The report is structured as follows:

- **Chapter 2** sets out the policies required to promote pro-poor growth.
- **Chapter 3** examines the way pro-poor growth benefits from progress on the other dimensions of poverty.
- **Chapter 4** focuses on the policy-making process to promote pro-poor growth and on the need for the poor to be informed and empowered to participate in this process.
- **Chapter 5** considers the role of donors in the pro-poor growth agenda.

## CHAPTER 2

### REDUCING ECONOMIC POVERTY THROUGH PRO-POOR GROWTH

**Rapid and sustained reduction of economic poverty requires pro-poor growth: a pace and pattern of growth that enhances the ability of poor women and men to participate in, contribute to and benefit from growth.**

#### 2.1 Pace and Pattern

*The pace and pattern of growth are interlinked and need to be addressed together.*

16. The 2001 DAC Guidelines on Poverty Reduction state that both the pace and pattern of growth, in terms of its sustainability, composition and equity, are important for effective reduction of economic poverty. POVNET's recent work has shown pace and pattern to be interlinked. Growth that is broad based across sectors is likely to be longer sustained than growth dependent on market conditions in one or two sectors and provides greater opportunity for the poor to participate in the growth process, thus promoting equity. In developing countries, poor women and men make up a substantial proportion of the work force and if they are more able to participate in and contribute to the growth process, economic growth will be faster and more equitable. Moreover, unlike past approaches that sought to focus initially on the rate of growth with the hope of addressing its pattern and the distribution of its benefits later, it has become clear that the two need to be addressed together. Policies that impact on pace also address pattern and vice versa and so neither should be approached in isolation. An inclusive pattern of growth is crucial because the revenue systems of developing countries are often underdeveloped, thereby reducing the scope to use tax-based transfers to achieve equitable growth.

#### 2.2 Sustaining Growth

*Sustained growth is essential for reducing economic poverty.*

17. There is clear evidence to show that economic growth is an essential requirement and, frequently, the main contributing factor in reducing income poverty. Evidence across countries and time periods shows that long-term reduction in income poverty results first and foremost from growth. Studies of the experiences of 14 developing countries during the 1990s found that income poverty fell only when there was growth and, in general, the higher the growth the greater was the decline in income poverty.<sup>3</sup>

18. All countries experience short episodes of growth, either rapid or modest. These are not sufficient to provide the opportunities that poor people need to escape economic poverty. The key to reducing economic poverty lies in ensuring that a rapid rate of growth is sustained over the long term. This is what the countries of Asia such as China and India have accomplished recently and this has resulted in a substantial reduction in income poverty. Growth may start for a variety of reasons: discovery of natural resources, higher commodity prices, a better investment climate for the private sector and so on. In India, as little a change as government signalling a more positive sentiment toward business was sufficient to trigger growth.<sup>4</sup> Sustaining growth, however, requires deepening the incentive to invest and increasing the use and productivity of capital and labour across the economy as a whole, through appropriate policies and institutions. Recently, growth rates have increased in Africa. The challenge now is to ensure that growth accelerates to levels required to achieve MDG 1 and is sustained by appropriate policies and institutions.<sup>5</sup>

### Box 2. Private Sector Development (PSD)

The private sector is often referred to as the engine of growth and so, up to now, private sector development (PSD) has been mainly associated with increasing the pace of growth. The private sector also has a strong bearing on the pattern of growth, influencing whether growth is broad or narrowly based and more or less inclusive of the poor. Secure, safe and well paid jobs and productive self employment in agriculture and non-farm occupations in the private sector are important pathways out of income poverty.

The emerging pro-poor agenda for private sector development acknowledges that what matters is the degree to which growth provides opportunities for the poor, and the extent to which poor men and women benefit from them. At present, most developing countries are unable to create sufficient formal jobs to cope with the increase in the non-agricultural work force. This forces hundreds of millions of the poor to earn their livelihoods informally. It is estimated that 72% of the non-agricultural work force of Africa, 65% of Asia and 52% of Latin America earns its livelihood informally, representing one of the most important policy issues for PSD today.<sup>6</sup> While informal occupations may be their only means of survival, many of the poor may be forced to engage in low value-added occupations, find employment in insecure jobs where core labour standards are not enforced and there are no provisions for social insurance, thus contributing little to growth and failing to provide the opportunity and security to escape income poverty. In addition, as a result of the disadvantages faced by informal businesses, the substantial assets held in the informal economy – in Tanzania, their estimated value is USD 29 billion<sup>7</sup> – that could be used to help spur economic growth fail to fulfil their productive potential. In practice, there is a continuum between formality and informality with many informal businesses paying taxes and formally registered businesses employing labour and serving markets informally. PSD policies to address informality may help to increase job creation in the formal economy, reduce barriers to and increase the incentive for formality and help to improve productivity in the informal economy through better access to credit and business support services.

19. To sustain growth, policies and institutions need to increase the stability and predictability of doing business so that the risk-to-reward ratio for businesses and individuals improves, spurring entrepreneurship and investment. Social or political conflict, the lack of a functioning state and policy volatility, caused by frequent political change, undermine growth. Restoring peace and the legitimacy of the state are therefore essential pre-conditions for pro-poor growth in fragile states. Factors that contribute to sustaining growth include – macro-economic stability; institutions that provide clear rules that are enforced predictably, good governance that will reduce corruption and rent seeking; a favourable investment climate which includes secure property rights and efficient markets that allow the productive assets of land, labour and capital to flow to areas where the returns are highest and increases access to these resources, including for the poor.

20. Whilst macro-economic stability is essential for pro-poor growth, helping to sustain growth and ensuring that the incomes of the poor are not damaged by inflation or economic crises, it needs to be achieved through a flexible approach. Rigid adherence to targets that do not take account of the phase, in the economic cycle (expanding or contracting), or the potentially high returns to social investment, may undermine growth unnecessarily.<sup>8</sup> Moreover, they should take account of the effect on poor people so that, if public expenditure needs to be cut back to reduce fiscal deficits in pursuit of macro stability, the burden should not be borne by the poor. Governments have often found it politically expedient to placate powerful vested interests by maintaining spending on services and investments that matter to them whilst cutting back expenditures that matter for the poor because they lack a strong political voice.

21. Moreover, it is now recognised that, in themselves, policies associated with faster growth are not panaceas and may need complementary policies to bring about sustained, pro-poor growth. Harnessing the international economic linkages of trade and investment can help to sustain rapid growth but this is more likely to contribute to sustained pro-poor growth if the international trading system works is more equitable and trade policy is accompanied by complementary policies to build domestic capacity and

competitiveness, enable productive assets to be redeployed, reduce the cost and risk of trading and help the poor to adjust to or better cope with the new situation.

22. An effective regulatory framework with sound governance that ensures environmental sustainability is vital for sustaining growth, not least because a high proportion of developing countries are dependent on natural resources and because a high proportion of agriculture in Africa takes place on fragile lands. Policies that promote environmental sustainability underpin pro-poor growth by ensuring that natural resources are not exploited unsustainably (see chapter 3).

23. Exploitation of natural resources is frequently accompanied by a 'resource curse'.<sup>9</sup> Over reliance on exports of natural resources may undermine pro-poor growth in several ways: the exchange rate appreciates which damages (tradable) sectors of the economy, such as agriculture, and inequality increases as does the risk of corruption and conflict. This is why many of the resource cursed countries are also fragile states. As Botswana has proven, with effective policies to stabilise foreign exchange earnings, prudent public expenditure policies that target the poor and investments to promote broad-based growth, the discovery of natural resources can be the basis of pro-poor growth rather than the curse they have proved for many countries.

24. Given the diversity of types of economy, resource availability, levels of development and variations in policy and institutions, it is not possible to arrive at a formula of policies and institutions that can be applied universally.<sup>10</sup> Context is crucial. However, the fundamentals for sustaining growth remain the same across countries. What is required is a sound analysis of the country's growth/inequality/poverty experience and policy and institutional framework to identify the binding constraints that need to be addressed to sustain pro-poor growth.

### **2.3 Pro-Poor Growth Pattern**

*Economic growth is likely to be faster, longer sustained and more effective in reducing economic poverty when associated with a pro-poor pattern of growth.*

25. The effect growth has on poverty varies tremendously. Evidence shows that a 1% increase in per capita incomes may reduce income poverty by as much as 4% or by less than 1%, depending on the country and time period.<sup>11</sup> In part, this is due to initial conditions, particularly levels of inequality in incomes and assets. In addition, the effect growth has on reducing income poverty will depend upon the extent to which the pattern of growth enhances the ability of poor people to participate in, contribute to and benefit from growth. If the pattern of growth is broad based and inclusive with respect to the sectors from which poor women and men earn their livelihoods, the regions in which they live, creates jobs that they may fill, and increases access to productive assets and markets for goods and services they produce, it is likely that their incomes will rise more rapidly and they will be able to acquire the assets they need to continue to increase incomes in the future. If, on the other hand, the poor are stuck in regions and sectors that are marginalised from the growth process, then very rapid rates of per capita growth will do little to reduce poverty: in China, since 2000, income poverty has not declined despite double digit rates of growth nationally as the poor live in rural areas of marginalized regions in the west.

**Box 3. Infrastructure promotes pro-poor growth.**

The infrastructure gap is huge. Globally, more than 1 billion people have no access to roads, 1.2 billion do not have safe drinking water, 2.3 billion lack reliable energy, 2.4 billion have no sanitation facilities and 4 billion no modern communication services. In the absence of accessible transport, energy and water, the poor pay heavily in time, money and health. When road surfaces are severely corrugated, electricity blackouts frequent, water services dysfunctional and telecommunications absent, countries and regions have great difficulty to achieve pro-poor economic growth. There is strong evidence that good and equitable access to infrastructure services not only promotes **faster growth** but also **growth patterns** beneficial to poor people.

Reliable and affordable infrastructure reduces the production and transaction costs of doing business. It also helps to connect up poor people to the growth process by improving their access and mobility. One mechanism is by connecting remote areas to growth poles and, in this way, correcting regional imbalances and helping poor people break out of poverty traps. There is evidence that increased access to infrastructure contributes to lower inequality.<sup>12</sup> Furthermore, access to infrastructure services contributes to the achievement of several MDGs, e.g. by its positive impacts on primary education coverage and on reduction of malnutrition and child mortality (where clean water and safe sanitation are crucial factors). In many countries, infrastructure suffered from severe cuts in public spending during the 1990's. The hope that private investors could fill a major part of the financing gap did not materialise. Between 1997 and 2003, bilateral donor support to infrastructure decreased from roughly 35% to 15% of total bilateral ODA. Investment in new infrastructure and maintenance has been neglected. Governments and donors are now giving increased attention to infrastructure though much more needs to be done.<sup>13</sup>

26. Policies are needed to ensure that the poor are not marginalised from the growth process. Addressing lagging regions in which the poor are concentrated is not easy because faster developing regions tend to capture economies of scale and concentration. Nevertheless, context-specific solutions that include improved institutions and governance, a better investment climate with increased access to credit and services to increase productivity, improving transport links with growth poles and investing in the region's infrastructure may help kick start faster growth. Greater investment in health, education, infrastructure and agriculture targeted at the poor, combined with encouraging labour mobility to other regions, may pay dividends in ensuring that the poor benefit from growth.<sup>14</sup>

27. The performance of agriculture is critically important for a pro-poor pattern of growth. When agriculture lags other sectors, growth tends to be less pro-poor<sup>15</sup>. Where growth was initiated by increased agricultural productivity, growth has been pro-poor, as experienced in most countries of the Far East. Rising agricultural productivity contributed not only to growth and the incomes of the poor directly, it also helped with the transformation of the economy, enabling manufacturing and services to expand. The growth of agricultural (land) productivity should contribute to faster growth of the incomes of the poor, particularly if combined with the growth of productivity in non-farm activities to ensure that rural incomes rise rapidly.<sup>16</sup>

28. The world over, the proportion of the non-agricultural work force earning its living informally is increasing as employment in the formal sector has not kept pace with its growth. Where productivity in informal occupations is higher than agriculture and provides adequate incomes for the poor, as experienced in Vietnam,<sup>17</sup> growing informality may not detract from a pro-poor pattern of growth. In Africa, however, productivity and incomes from informal activities are low with the majority of the self-employed engaged in 'survival businesses' unable to escape poverty. To a large extent, this is also the case in Latin America. Addressing informality requires a combination of removing barriers to formalisation, increasing the positive incentives of becoming formal by reducing rent seeking by corrupt officials and improved access to markets and finance, and ensuring higher rates of investment and job creation in the formal sector.

#### Box 4. Agriculture

Agriculture plays an important role in ensuring pro-poor growth. The green revolution in Asia succeeded in lifting millions out of poverty. The average real income of small farmers in south India rose by 90% and that of landless labourers by 125% between 1973 and 1994 as a result of the Green Revolution<sup>18</sup>. Agricultural productivity plays a particularly important role in improving existing livelihoods, meeting consumption needs and providing the basis for new livelihoods. A 10% increase in crop yields may lead to a reduction of between 6% and 10% of people living on less than \$1/day.<sup>19</sup> For every 1% of growth in agricultural GDP, the positive impact on the poorest has been shown to be greater than that from similar growth in manufacturing or services.<sup>20</sup> Such impacts are usually best realised where there is an equitable distribution of assets, particularly land,<sup>21</sup> where there is access to markets for the poor and where there are good rural-urban links. Investment in agricultural research provides some of the highest returns to public spending yet funding by governments and donors has declined over the past decade.

Agriculture in Africa has not been able to contribute to pro-poor growth as effectively as in Asia. Since 1990, food availability has fallen 3% per capita in Africa whereas it has increased 30% in Asia. African agriculture faces particular challenges. These include the wide range of crops and livestock combinations across diverse ecological zones that increases the demands on research and extension; the lack of a suitable investment climate and domestic savings for investment; poor institutional quality; vulnerability in the absence of social protection that may undermine risk taking; low access to markets exacerbated by a weak road system; new and more demanding technical barriers to trade in accessing OECD markets; etc. These challenges are not insuperable, at least in the regions that are suitable for increasing agricultural productivity. They require a combination of concerted investment in improving access to markets and productivity enhancing technology, improving policies and institutional quality and a more favourable investment climate in agriculture addressing the needs of both commercial and small farmers. Like infrastructure, governments and donors need to re-examine and increase their commitment to the development of agriculture through more effective ways of providing support outlined in chapter 4.

## 2.4 Addressing Inequality

*High inequality undermines the pace and pattern of growth and its effectiveness in reducing economic poverty.*

29. In developing countries, the distribution of productive assets and the opportunity to participate in and benefit from growth are most unequal, resulting in a high level of inequality in the distribution of incomes. Inequality in the distribution of assets reduces the ability of poor people to increase their incomes and contribute to growth. Men and women work harder and invest more on land they own or over which they have secure use, as evidenced in China and Vietnam<sup>22</sup>. Investment in land and natural resources by poor people and market-based approaches to land redistribution will increase pro-poor growth. Greater equality of opportunity contributes to higher growth. When markets fail, a frequent situation in developing countries, the allocation of resources and opportunities for wealth creation are determined by wealth and power, disadvantaging poor men and women who may have made more productive use of them, thus undermining growth. Increasing inequality in opportunity, assets and incomes also runs the danger that mounting dissatisfaction and a sense of injustice combine to undermine the political and social stability that is vital for sustaining growth.

30. Growth, inequality of incomes and poverty are interlinked and are sometimes described as three sides of a triangle.<sup>23</sup> With a high level of income inequality to begin with, growth needs to be faster and longer sustained to achieve the same level of poverty reduction. If income inequality increases, it will reduce the effect growth would have had on raising the incomes of the poor. In Ethiopia, between 1981 and 1995, growth should have resulted in a 31% reduction of income poverty, if the poor had benefited from growth equitably. Instead, increased inequality undermined the potential benefits from growth on the incomes of the poor and resulted in income poverty rising by 6%.<sup>24</sup>

31. Evidence shows that, contrary to earlier views, rising inequality is not inevitable in the early stages of development.<sup>25</sup> Growth reduces income inequality as frequently as it increases it.<sup>26</sup> Where inequality is high or rising, there will be a need to examine the pattern of growth and ensure that poor women and men are not being marginalised in the growth process. High levels of income inequality in Latin America and rising income inequality in Sub-Saharan Africa are thus a cause of major concern that require policy responses from governments and donors.

32. A very wide range of policies are required to address inequality starting with those required to bring about a pro-poor pattern of growth, and including measures to address risk and vulnerability. Evidence shows that investment in early childhood development will promote equality of opportunity and, hence, pro-poor growth. Efficient public spending on the basic social services of health, education and infrastructure that reach the poor is vital for pro-poor growth. The current situation is that, in many countries, public spending is not efficient and benefits the non-poor disproportionately.<sup>27</sup> Gender biases, social stigma associated with caste, disability, HIV/AIDS and membership of social or religious groups, result in individuals failing to achieve their latent potential. These inequities undermine growth and are all the more damaging for poor people's efforts to escape poverty because they are perpetrated over generations. Enforcement of laws that most countries have adopted to address discrimination on social grounds, needs to be improved.<sup>28</sup>

33. Gender is a particularly important dimension of inequality. This is illustrated by the difficulties that women face when participating in economic activities because of their role as carers, discrimination in accessing assets such as land, and negative social attitudes. Policies that increase women's participation in the work force and the returns to that participation are major contributors to pro-poor growth. Greater access to infrastructure, reproductive health services and child care, a decline in fertility rates caused by changes in attitudes or access to contraception, higher female life expectancy and improved social attitudes to women's involvement in economic activity all help to increase women's participation in the work force. Greater access for girls and women to education at all levels and equitable employment policies help to increase returns to women's participation in the work force.<sup>29</sup>

## 2.5 Addressing Risk and Vulnerability

*Risk and vulnerability limit poor people's participation in the growth process. The establishment of effective risk mitigation instruments and credible social protection should be an essential element of pro-poor growth strategies.*

34. Along with greater human security (chapter 3), increasing the economic security of the poor pays the double dividend of helping to sustain faster growth and bringing about a pro-poor pattern of growth. Taking advantage of opportunities requires taking risk – producing new crops, entrepreneurship, moving to new areas and jobs all involve risk. With their meagre incomes, the poor are especially vulnerable to the potential consequences of risk taking and are hence reluctant to take on additional risk. Prevention, mitigating or coping strategies that reduce vulnerability to risk, such as increasing the reliability of agricultural incomes, deepening insurance markets through public-private arrangements so that they reach the poor and ensuring credible social protection, are thus important for pro-poor growth. Policies that provide greater incentive to combine pro-poor growth with sustainable use of natural resources often contribute to addressing the vulnerability of the poor.

35. Escaping poverty is not a one way journey. Many poor women and men fall back into it. Shocks caused by natural disasters or man-made crises may cause economic contraction and huge numbers of people can fall back into poverty. Economic, political and social stability help to avoid man-made shocks and so contribute to growth and more effective reduction of economic poverty. Of course, it is not possible to eliminate risk either at the macro level or amongst households. It is important therefore to have in place

reliable social protection instruments that may be deployed rapidly to cope with natural disasters and man-made shocks, to avoid extreme deprivation for the poor and the loss of their human, financial and social capital in a desperate attempt to cope. If the poor are forced to sell or deplete the very assets that they need to earn better incomes, they will be less likely to escape poverty in future, resulting in 'poverty traps'. Policies that prevent extreme deprivation, such as labour schemes to build infrastructure can be useful in this regard. Where poverty traps exist, 'smart' cash transfers that are conditional on the poor building assets by accessing health and education for their children should help, such as Mexico's Progresa/Oportunidades.<sup>30</sup> Addressing barriers for the disabled to find productive employment may also pay high dividends as small changes in levels of accessibility may allow sizeable parts of the work force to live productive lives. Providing safety nets such as contributory or non-contributory pensions (South Africa) or cash transfers (Zambia) will help to prevent extreme deprivation amongst the elderly, chronically infirm or extreme poor.

## 2.6 Policies to tackle the causes of market failure and improve market access

*Markets connect poor men and women to the growth process. Market failures and disadvantages in the terms on which the poor participate in markets prevent pro-poor outcomes.*

36. Market failures are common in developing countries and when they occur, outcomes undermine pro-poor growth. The causes of market failure are manifold: inappropriate policies and institutions, unequal access to market information, concentration of market power, high cost of transactions and co-ordination failures or failing to take account of wider impacts such as on the environment. Even if markets do not fail, the poor may be disadvantaged when participating in them through discriminatory formal or informal institutions and higher costs of accessing markets.

37. When markets have failed or market outcomes have not been pro-poor, governments have often intervened directly, providing goods and services themselves. In many cases this has led to market failures being replaced by government failures with the poor still remaining disadvantaged. Deregulation has, in some cases, helped to improve market access and functioning for the poor. But in agricultural and rural markets where old market failures have resurfaced, the poor remain particularly disadvantaged by high transaction and co-ordination costs, poor access to information and lack of market power. New approaches, which combine tackling market failures with improving market access, are needed to make markets work better for the poor. These approaches need to include investment in the economic capabilities of the poor.

38. Participation in markets influences the ability of poor women and men to improve their livelihoods and contribute to growth. Well-functioning markets for productive assets that increase access for the poor have a vital role to play in generating pro-poor growth. This has numerous dimensions. Financial sector deepening is associated with higher rates of pro-poor growth,<sup>31</sup> especially when accompanied by increased access of the poor to financial services. Greater access to and security over land and other property for the poor and well-functioning labour markets that increase formal job creation, enable labour mobility and meet core labour standards are all needed.

### **Box 5. Financial markets**

Financial markets that are characterized by limited competition and/or adverse incentives for private lending often exclude poor people. For this reason, governments, development agencies and others have promoted microfinance schemes and these have been of great benefit to poor women and men. Nevertheless, it has become evident that isolated microfinance projects are not a long term solution. To bridge the gap between microfinance and traditional financial markets and to expand more generally the access of poor people to sustainable financial services, inclusive financial systems are needed which provide appropriate products and services for all types of clients. To achieve this, a supporting infrastructure (refinancing institutions, associations, credit bureaus, rating agencies, etc.) as well as a conducive macroeconomic and policy environment, are required.



39. On top of this, targeted assistance may be necessary in order to reach those who, even where the playing field for market access is levelled, still cannot make use of market opportunities because of lack of assets such as knowledge and skills, capital, land, or certain basic needs. But such assistance needs to be “smart”, to avoid distortions, to address the binding constraints and to reach the intended target group, and it should be temporary. Examples of such assistance include cash for work, voucher systems for research and business development services and output based payment systems for infrastructure services.

## **2.7 Key Implementation Issues**

- Is income poverty decreasing in line with MDG1:1? Is information available on the average rate of growth of the incomes of the poor? How does it compare to the overall rate of economic growth? Is there disaggregated data on income poverty and income growth with regard to gender, region, urban-rural, type of occupation and ethnicity?
- What is the level of income inequality and how has it been changing with economic growth? What can be done to reduce asset inequality and bring about greater equality of opportunity? What can be done to address unemployment, informality, poverty traps, lagging regions etc?
- Is growth broad-based and inclusive of the poor? Are poor women and men marginalised from economic processes? What barriers need to be removed for women, people with disability, ethnic or other minorities to participate in and benefit from the growth process? How efficient is public spending on basic social services and is it reaching the poor?
- What are the key policies and institutions that need to be improved to achieve sustained pro-poor growth (competitiveness, investment climate, legal system, property rights, public services, infrastructure etc)? Are direct and indirect impacts on poor women and men taken into account in the design of such policy reforms?
- How widespread is market failure and to what extent does it hurt the poor disproportionately? Are there special constraints for the poor in agricultural markets, land markets, rural credit markets, urban labour markets etc? What is the government response to market failure?
- Are there policies and instruments in place for poor people to manage their health risks, increase reliability of agricultural incomes, pool their livelihood risks, deepen insurance markets, reduce man-made shocks, cope with shocks and help poor men and women escape poverty traps? Are there safety nets for the elderly, infirm and extreme poor?

## CHAPTER 3

### ADDRESSING THE MULTIPLE DIMENSIONS OF POVERTY

**Poverty is multidimensional and pro-poor growth will be strengthened by progress on other dimensions of poverty. In tackling poverty, perceptions of policy dichotomies have been misplaced. Policy trade-offs do exist but can be better managed.**

#### 3.1 Inter-linkages between the different dimensions of poverty

*Pro-poor growth will be strengthened by progress on other dimensions of poverty. Policies to tackle the multiple dimensions of poverty should go hand in hand*

40. As set out in the DAC Guidelines on Poverty Reduction, the multiple deprivations that poverty takes are inter-linked. Understanding the inter-linkages should help to develop more effective pro-poor growth strategies and to integrate these better into national poverty reduction strategies, ensuring that policies to address the multiple dimensions of poverty go hand in hand. Pro-poor growth will be strengthened by progress on other dimensions of poverty than the economic one. Focusing on economic development alone, as some have attempted in past, is unlikely to prove as effective in addressing economic poverty as strategies that address the multiple dimensions of poverty. The paragraphs below provide the evidence for this, and show, for example, how failures to tackle social and cultural discrimination may keep millions in both economic and socio-cultural poverty even in middle-income countries. Moreover, they draw attention to the growing recognition that, without political empowerment of the poor, policies to address pro-poor growth are unlikely to be implemented in the first place.<sup>32</sup>

41. Reducing economic poverty through pro-poor growth should contribute to progress on the human dimension of poverty. For instance, higher incomes should enable the poor to spend more on health and education for their households so that they and their children may live healthier, more productive lives. And higher levels of economic prosperity should provide the resources the state needs to spend more on health and education. However, it cannot be assumed that higher levels of income will automatically produce better human development outcomes. Without effective policies to address them, the human capabilities of poor men and women may remain underdeveloped despite increased incomes, as shown by increasing infant mortality in recent years in Senegal and by the lack of progress on health indicators amongst the poor in Bolivia.<sup>33</sup> As noted earlier, public expenditure on health and education may not be pro-poor. The consequence is likely to be that the lack of development of human capabilities amongst poor men and women reduces the rate of growth and the extent to which growth is pro-poor. Not only will countries fail to achieve MDG 1 but they will fail also to deliver against the MDGs for health and education. Africa faces a particular challenge in combating the HIV/AIDS pandemic which is reversing gains in life expectancy made over decades. HIV/AIDS is undermining growth through reducing the productivity of the work force and is diverting scarce public resources away from making progress on other health issues and increasing access to education. The pandemic is now threatening countries such as India and China with huge populations. Effective policies, backed by adequate resources, are required to check the spread of the pandemic and to provide health care for the millions who are or will be affected.

42. The socio-cultural dimension of poverty focuses on status and dignity. A high proportion of the world's economic poor are members of social groups that are denied status and dignity in countries that have had success in economic development: indigenous people and those of Afro-American descent in Latin America, the so called scheduled castes of India, ethnic minorities of successful East Asian countries such as China and Vietnam. These countries prove how an absence of effective policies to address social or

cultural discrimination can leave millions in economic poverty despite higher per capita incomes. The inability of these men and women to fulfil their latent potential slows growth and makes it less pro-poor. In Sub-Saharan Africa, with its myriad of tribal and ethnic groups and a high incidence of poverty amongst female-headed households, discrimination on the basis of social groups and gender is rife, often spilling over into social conflict, undermining pro-poor growth and contributing to the failure of the state. From a wider perspective, people experiencing such loss of status and dignity are frequently denied their basic human rights. Many countries have appropriate legislation in place to address social discrimination and guarantee human freedoms. However, powerful elites, unaffected by its consequences and uninformed of its effects, have chosen not to enforce these laws effectively. Progress on addressing the social dimension should reduce both socio-cultural and economic poverty.

43. The wider concept of human security encompasses two dimensions of individual freedoms: the freedom from fear of conflict and natural disasters and the freedom from want in the form of hunger and lack of basic social services. It calls for policies to address the risk of war and conflict and of man-made and natural disasters, protect civil liberties and address hunger and want. Such policies are needed to create the conditions necessary for addressing economic security. The experiences of Rwanda and Sierra Leone show how increasing human security may start the process of laying the foundations for pro-poor growth. More research and thinking is required on how to bring about greater human security through reducing conflict.

44. Chapter 2 addresses the role women played in bringing about pro-poor growth. As recognised in the DAC Guidelines on Poverty Reduction, gender equity is a cross-cutting issue covering all dimensions of poverty. The first six MDGs are directly affected by the level of gender equity. Bringing about gender equity thus extends beyond bringing about the beneficial participation of women in the work force. It is based on securing 'all the human rights and fundamental freedoms in the political, economic, social, cultural, civil or any other field' for women, as set out under The Convention of the Elimination of All Forms of Discrimination Against Women (CEDAW). Progress on gender equity in developing countries remains slow and requires greater commitment from governments and donors.

45. Environmental sustainability also cuts across all dimensions of poverty. The state of the environment and the productivity of natural resources affect both the pace and pattern of growth. The poor are particularly dependent on natural resources for their livelihoods. Environmental sustainability is important for economic and human development as environmental 'costs' at the global, national and local levels, bear heaviest upon the poor. They are crucial for living conditions world wide with climate change and environmental pollution being major issues that require the concerted efforts of all governments to tackle. Environmental degradation is not the inevitable cost of economic development. Rather than trying to mitigate the environmental impact of policies and projects, developing countries and their donor partners should use tools such as Strategic Environmental Assessments to help make informed choices. Central to such an approach is effective governance and fiscal policies that change incentives in favour of environmental sustainability and growth. One way of dealing with land degradation is by increasing the availability and affordability of agricultural inputs, such as fertilisers, in combination with risk mitigation instruments (insurance), allowing farmers to make better use of them. Pro-poor growth would be greatly strengthened by investments in improving environmental quality backed up by effective regulatory frameworks and governance.

46. The political dimension of poverty may mean that the poor become marginalized in the political process and, hence, have little influence over the policy-making process. Where the inequality in political power between the poor and non-poor becomes marked, there is a danger that key institutions of the state may be captured by rich, powerful elites and used to bring about policies and institutions that promote their narrow vested interest, rather than promote widespread economic prosperity through pro-poor growth. Policy and institutional reforms required for pro-poor growth and wider poverty reduction are more likely

to be implemented if poor women and men are empowered to participate actively in the political process and, through their representatives, able to influence the policy-making process. Reducing the multiple dimensions of poverty is thus enabled by political empowerment, as further discussed in chapter 4.

### 3.2 Traditional Dichotomies

*Traditional dichotomies between pro-growth and pro-poor policies have been misplaced.*

47. Traditionally, pro-growth and pro-poor policies to empower poor people socially and politically have often been regarded as separate, unconnected and often competing strands of development. The former has been emphasised by economists who have pointed to the dramatic reduction in income poverty achieved by countries that have sustained high rates of growth as evidence that growth is the decisive influence in reducing economic poverty. The latter has been stressed by social and political scientists concerned with human freedoms and the rights of the poor. A pro-poor growth lens shows both these persuasive schools of thought to be complementary in reducing poverty and an effective poverty reduction strategy needs to encompass both these perspectives.

48. Countries like Brazil and Egypt that enjoyed high rates of growth in the 1970s, but did not invest in human capabilities, were unable to sustain growth because the productivity of the workforce failed to increase, thus reducing growth. Equally, without growth, it is unlikely that investing in the capabilities of the poor will be translated into reduced income poverty because the poor will not have the opportunity to use their new capabilities to earn higher incomes, as evidence by the experience of Jamaica.<sup>34</sup> Routes out of poverty vary. Countries such as India were able to increase growth with slow improvements in human development. Others, such as China, invested heavily in human development before bringing about rapid, sustained growth. What is clear, however, is that no country can maintain growth unless that growth is accompanied by major gains in human development. And, as noted above, policies to address social discrimination and increase human security are important for pro-poor growth.

### 3.3 Potential Trade-offs

*Policy trade-offs exist, but need to and can be better managed. Policies need to be sequenced to address the binding constraints. The ability of institutions to handle trade-offs is important for achieving pro-poor outcomes.*

49. One of the main reasons why traditional dichotomies have persisted for so long has been the perception that there are strong trade-offs between pro-growth and pro-poor policies. Some held the view that the public spending required to increase human development and security could only be afforded through high rates of taxation which would stifle growth. Others held the view that there was a choice between investment to promote growth and that needed to bring about a pro-poor pattern of growth. For example, investing in infrastructure to enhance growth in cities and towns that were expanding rapidly was seen as an alternative to investing in infrastructure to enhance the ability of poor people in rural areas to participate in the growth process.

50. Obviously, in the short run and at the extremes, there are trade-offs. In the short run, hard choices may need to be made on whether to focus initially on economic as opposed to social development and between pace and a pro-poor pattern of growth. But the pro-poor growth lens shows these trade-offs to be exaggerated. For example, in the short term, if the choice made is to invest in bringing about greater participation of women in the work force and developing human capabilities through improved access to health and education, it will lead to higher growth in the medium term, thus increasing the tax base to fund additional investment in the future. Equally, investment in infrastructure to promote trade, investment and

employment will generate income and tax revenues to support household expenditure and public investment in health and education in the medium term.

51. Priorities for the short term may be set by examining the growth/inequality/poverty experience and progress in achieving other MDGs to find the binding constraints to pro-poor growth and poverty reduction. POVNET has developed a simple, practical approach to carry out ex-ante poverty impact assessments (PIAs) that can help to inform policy choices and investment design (see box 6). It focuses on identifying transmission channels and the potential impacts of the intervention on different groups.

#### **Box 6. Analysing the Impact of Development Interventions**

Poverty and Social Impact Analysis (PSIA) has been developed by a number of donors to help understand the distributional consequences of policies on the welfare of people, particularly those who are poor and vulnerable. PSIA draws on a range of multi-disciplinary tools for this analysis and encourages an inclusive, transparent and accountable process. It can be used before, during or after an intervention. This is proving to be an effective approach, but tends to be costly and time consuming making it inappropriate for intensive use across a wide range of development interventions (projects, programs and policies). POVNET has developed a simple, more practical approach that can help to inform policy and investment choices and design. This draws on the PSIA framework, the MDGs and other important welfare measures. This framework for ex-ante poverty impact assessments (PIAs) focuses on:

- i) Existing information, assessing gaps, and whether there is need for more detailed data and analysis.
- ii) Aligning with national development /poverty reduction strategies.
- iii) Identifying the transmission channels through which interventions will impact on stakeholders.
- iv) Understanding impacts on the capabilities of different groups, in particular the most vulnerable.
- v) Examining the potential contribution to the MDGs and other high priority agendas, such as pro-poor growth.

52. In fact, there is a large policy space in which it is possible to pursue complementary policies that address both pro-growth and pro-poor objectives. Thus, the development of micro finance institutions that are part of the mainstream financial sector will help to increase credit to the private sector and to the poor, addressing both pro-growth and pro-poor objectives. Financial deepening of this type addresses not only economic poverty but is associated with gains in human development indicators such as reducing infant mortality<sup>35</sup>. Investment in providing and maintaining infrastructure which is accessible by the poor should help to increase pro-poor growth and reduce several other dimensions of poverty: provision of electricity for the productive use of the poor, for instance could improve labour productivity, increase household income by allowing women to spend more time on economic activities and household duties including care for children and health. As concerns environmental degradation, fiscal incentives for the sustainable use of natural resources and pricing policies that will lead to greater access to water and sanitation for the poor on a financially and fiscally sustainable basis<sup>36</sup> help to ensure that environmental gains are accompanied by increased, not reduced, pro-poor or pro-growth expenditures.

### **3.4 Key Implementation Issues**

- In what way do national poverty reduction strategies reflect understanding of poverty and the inter-linkages between the multiple dimensions of poverty? How can government (regional/local) planning take better account of the linkages between the economic and non-economic dimensions?
- Are policies for reducing the human, social and security dimensions of poverty helping to bring about pro-poor growth?

- What is the experience with complementary policies that are both pro-growth and pro-poor e.g. investment in health and education, micro finance, investment in infrastructure for the poor etc.?
- How effective are laws to prevent discrimination on the basis of gender, social and cultural differences and what could be done to improve the situation?
- In what way is the role of environmental sustainability in pro-poor growth and living conditions reflected in policies?
- Are policy choices and investment priorities informed by prior analysis of their potential impacts on the various dimensions of poverty?
- How are potential trade-offs dealt with between pro-growth and pro-poor policies? Are opportunities for sequencing policy reforms and coordinating investments in social and economic areas fully exploited?

## CHAPTER 4

### POLITICAL EMPOWERMENT AND THE POLICY MAKING PROCESS

**For pro-poor growth policies to emerge, the poor need to be informed and empowered to influence a policy making process that is accountable to their interests**

#### 4.1 Political Empowerment and Participation

*The poor need to participate in and influence the policy reform process that goes with poverty reduction strategies. Approaches are needed to increase the voice and influence of poor women and men in order that policy-making is accountable to the actual needs of the poor.*

53. To bring about pro-poor growth, it is important to make the policies described in chapters 2 and 3 the basis of national development or poverty reduction strategies which are supported widely within the state, the private sector and civil society. Addressing this issue represents a major challenge. In many developing countries, inequalities in political power and influence can be huge and if powerful elites so choose, they may pay lip service to or ignore the interests of the poor. At the extreme, in fragile or failed states, control of the state may be captured by a few, powerful interest groups who may impose policies and make investment choices that serve their interests rather than those of the poor. Even with a relatively well functioning state, the voice of the poor may be weak, policy-making processes opaque, informal or not amenable to being influenced by evidence-based dialogue and there may be little accountability of policy makers to the poor.

54. Actions are needed to bring about a stronger, better informed voice for poor people with whom they, and those who represent their interests, may influence policy makers. This may require the strengthening of the capacity of organisations who represent the interests of the poor (farmers', small business and women's organisations, trade unions, politicians, NGOs, media etc.) to analyse the growth/inequality/poverty experience and identify the key policy and institutional reforms required to promote pro-poor growth. The analysis may be used to convince other actors and organisations in the public and private sectors and civil society so that they may better align their demand for policy change more closely to the interests of the poor. Further, initiatives are required to make the various policy-making processes of the state more formal, transparent and evidence-based, so that they may be influenced by the representatives of the poor. In this way, the focus of policy-making may shift from the claims of competing vested interests, which frequently disadvantage the poor, to more evidence-based dialogue. A stronger voice and better policy-making processes should also help increase the accountability of the state to those representing the interests of poor women and men.

#### 4.2 The Role of the State and Public-Private Dialogue

*A well-functioning state is essential for responding to the interests of the poor. The state needs to provide the opportunity for the representatives of the poor to influence policy-making processes and make policy makers more accountable to the poor.*

55. The likelihood that the policy and institutional reforms required to promote pro-poor growth will be implemented will be increased if the state is functioning effectively. Where the checks and balances that the organs of the state (legislature, judiciary etc.) are meant to exercise on government break down, the

danger of capture of the state by vested interest increases. If the state is unable to make different parts of society (e.g. government, private sector, civil society) respect the rule of law and provide effective governance on behalf of all its citizens, it is likely that respect for the institutions of the state will be diminished. That would encourage vested interests within each group to flout the authority of the state in pursuit of their own goals. In these circumstances, the greater political power of these vested interest groups would make policies to promote pro-poor growth highly unlikely. At the extreme, the inevitable consequence of such developments is partial or complete failure of the state, frequently accompanied by political or social conflict, conditions which make pro-poor growth nearly impossible.

56. The state also plays a crucial role in determining whether policies for pro-poor growth are implemented through the structure and characteristics of the policy-making processes it adopts and the extent to which it makes policy makers accountable to the interests of the poor. Centralised, autocratic decision making by national government may reduce the influence that those who represent the interests of the poor have on the policy-making process and diminish accountability to the interests of poor people. Whilst macro policies should be made centrally, there are a wide range of economic policies that affect the investment climate (cost of doing business, infrastructure, etc) and social policies (health, education, social protection and inclusion etc.) that may be more suited to the context and pro-poor if policy-making is decentralised. However, decentralisation of policy-making, by itself, may not be sufficient. Without sufficient participation of the intended beneficiaries (including poor women and men), there is a danger that powerful vested interests locally may capture the policy-making process and decentralisation enable greater rent seeking and corruption. Decentralisation needs to be supported by human and financial resources and accompanied by building capacity to improve governance locally.

57. Moreover, the likelihood of policies being implemented that promote pro-poor growth should increase if they are developed and implemented through broad-based dialogue and participation involving the different parts of society and including the interests of the poor, rather than the autocratic decisions made by government alone. What is crucial in this kind of process is that not only the voices of a few large formal actors in the private sector are heard but also a much wider spectrum of people, including small farmers, micro-entrepreneurs in the formal and informal private sector and so on. Civil society has an important complementary role to play by articulating the interests of women, disadvantaged groups and society more generally in economic and social reform processes. Furthermore, if public - private dialogue only takes place at the national level, many opportunities at the local level may be lost.

58. It is important to note, though, that greater dialogue, by itself, is not a panacea.<sup>37</sup> Dialogue needs to serve a purpose and lead to policy outcomes. Interest groups in society, particularly those representing the interests of the poor, need to be better informed and organised in order to participate effectively in public-private dialogue and to articulate and defend their interest more widely. Where the boundary between the "public" and the "private" is fluid (as in much of Africa), the quality of the dialogue depends on the structure of the participating institutions. Merely assembling government representatives, high-level civil servants and the most powerful/influential private sector people around a table will not suffice to create an atmosphere of trust in which the broad direction of economic policy can be jointly expounded and may lead to consultation fatigue. The organisational and process dimensions of the dialogue can turn out to be key to its success. For example, it is important to assess which issues are likely to generate greatest interest, analyse in advance the political economy in order to determine whether such a dialogue is both feasible and timely and to communicate policy options. The dialogue should be linked to a specific policy reform process with declared objectives such as the formulation of a local or regional plan, green/white paper on an issue, national poverty reduction strategy etc. Local organisational capacity to conduct meaningful dialogue is key to ensuring policy outcomes in favour of pro-poor growth.



### Box 7. Dialogue as a means to Pro- Poor Policy Reform

An interesting example of successful interplay between market development and dialogue is the emergence during the last few years of a flourishing commercial radio market in Uganda. In 2004, 19 commercial radio stations were broadcasting to 7 million regular listeners. This has given many small local businesses, run by female as well as male entrepreneurs, an opportunity to participate in debates on how to improve and bring about reforms of the local business climate.

Source: Business Environment Website (<http://bdsknowledge.org>); MSE Radio Programmes in Uganda and Ghana, 2004.

59. Effective governance plays a crucial role in delivering policy outcomes. Experience from countries which have carried out successful governance reforms show that these are often linked to the processes of economic and social development, whereby virtuous circles are established between governance reforms and pro-poor growth. There can be different triggers to setting such circles in motion. Sometimes a crisis (political, financial, natural) or change in the political leadership can be the starting point for concrete steps to improve governance as well as sending positive signals to the private sector. Carrying out surveys of the business climate that show the importance of improved governance may help to trigger a process, during which public and private sector and civil society organisations are strengthened and they come to hold each other to account as partners in development.

#### 4.3 The Wider Political Settlement

*Pro-poor reform is likely to require changes to the current political settlement between the diverse interests of different segments of society.*

60. Policies and institutions represent the current political settlement between diverse interest groups that make up the state, the private sector and civil society. Hence, policy and institutional reforms needed to promote pro-poor growth are likely to involve changes to the current political settlement. As all change involves winners and losers, the likelihood of successfully promoting pro-poor change will be greatly enhanced by an understanding of the political economy of change: mapping stakeholder interests and understanding who is likely to win and lose from change. It may be necessary to arrive at technical solutions that minimise the adverse consequences of change or support other pro-poor reforms that may be in the interest of those who stand to lose from change. Otherwise, if those who are likely to lose from change are powerful enough, they will resist and hence block pro-poor change.

61. In such analysis, it is important to identify the potential constituencies in favour of and opposed to change. In so doing, it is important to recognise that those in favour of and opposed to pro-poor policy reform may vary from issue to issue. For example, farmers and large exporters may be on opposite sides in terms of priorities for public expenditure but on the same side in ensuring a competitive exchange rate. Further, it is useful to identify change agents, those who are able to influence policy makers and public opinion and support them in delivering pro-poor policy change. An understanding of the historical context, decision making structures (formal and informal) and the types of evidence and arguments that are most likely to influence decision makers, will also help in promoting policy reform in favour of pro-poor growth.<sup>38</sup>

62. Successful policy and institutional change in favour of pro-poor growth depends upon effective demand for change. Frequently, those who represent the interests of the poor do not have the capability to undertake evidence-based research or articulate policy change in ways that will minimise resistance to change. In these instances, building capacity amongst those who are advocating such change (e.g. rural NGOs, farmer's organisations etc) should prove helpful. There are instances where the state is unable to

respond effectively to the demand for change because of technical or resource limitations. In such instances, assistance in building the capacity of the state to respond effectively to change should prove helpful.<sup>39</sup> To meet the demand for change and the capacity of the state to respond, this kind of capacity building should be directed not only to central but also to regional and local levels. Where policy and investment choices exist and conflicting views threaten to block progress, ex-ante poverty impact assessments may help to understand better the relative merits of the choices and to provide solutions that mitigate the impact on those who stand to lose from change.

63. Instead of the view taken in the past that increasing growth that would benefit the poor depended upon the wholesale adoption of a set of policies that were universally applicable, evidence has shown that introducing policy and institutional change is a continuous process that involves innovation and lesson learning.<sup>40</sup> This process requires the progressive forging of a ‘social contract’ in favour of pro-poor growth between the different parts of society (i.e. the state, the private sector and civil society). The contract will be strengthened by political empowerment of the poor, a state open to influence and accountable to the private sector and civil society, including those who represent the interests of the poor, and by processes that will help to bring about a pro-poor political settlement in the wider polity.

#### 4.4 Poverty Reduction Strategies

*Poverty reduction strategies need to be nationally owned, better integrate the pro-poor growth component and to contribute to greater accountability of the state to the interests of the poor.*

64. Effective poverty reduction strategies, be they national development strategies or formal Poverty Reduction Strategy Papers (PRSPs), provide an important opportunity to strengthen the voice of the poor, influence the state’s policy and the wider political settlement. As policy reform involves winners and losers, the need to overcome possible resistance to change means that strategies should be nationally owned and have broad-based support. In the early phases, PRSPs were regarded mainly as a means to obtain HIPC debt relief and hence there was limited national ownership.<sup>41</sup> Further, these PRSPs focused on social development with a cursory glance at the need to accelerate pro-poor growth. The policies required to increase growth to the unprecedented levels projected were not set out, nor were the mechanisms for enhancing the extent to which the poor would be able to participate in, contribute to and benefit from growth.

65. Poverty reduction strategies need to be based on realistic views of growth prospects based on domestic and external environments as well as a thorough analysis of the inter-dependencies between growth, inequality and poverty in the country (see box 1 above). Binding constraints to accelerating pro-poor growth need to be identified, attention given to both its economic and social determinants and the linkages between the multiple dimensions of poverty addressed to ensure a holistic approach to reducing poverty. Poverty reduction strategies should become the instruments of strengthening the social contract between the different segments of society. This can be fostered by encouraging greater participation and dialogue in their preparation and ensuring that representatives of the interest of the poor are involved in monitoring implementation, thereby helping to increase the accountability of the state to the interests of the poor.

#### 4.5 Key Implementation Issues

- In which areas important for pro-poor growth is the state not functioning effectively? Does it, ensure respect for the rule of law and effective governance over the activities of government, the private sector and civil society?
- Are economic reform programmes accepted and owned by the country's political stake-holders? What are the drivers of economic change and what is the role of private sector actors, civil society and media in relation to economic reform?
- Are mechanisms in place for poor women and men to influence the policy making process? How can the voice of the poor be strengthened so that they are better able to influence the policy making process?
- Is there a sound understanding of stakeholder interests and of who is likely to win and lose from specific policy changes? Is it possible to identify and support change agents who can champion pro-poor change?
- To what extent is analysis of constraints and opportunities conducted at the local level and decision making on reform and investment decentralised? Is institutional capacity for this at the local level sufficiently developed or supported?
- Do poverty reduction strategies reflect a sound understanding of the linkages between growth, inequality and poverty reduction? How can the process of preparing PRSs strengthen the social contract in favour of pro-poor growth?

## CHAPTER 5

### THE ROLE OF DONORS

**The pro-poor growth agenda has important implications for the way donors support partner countries. It is not a 'business as usual' agenda, and 'more of the same' will not be sufficient.**

#### 5.1 Donors in the Pro-Poor Growth Agenda

66. The pro-poor growth agenda, focusing on policy and institutional change, recognises the importance of country contexts in identifying the binding constraints to pro-poor growth. This shows the practice of some donors of pushing agendas based on their experience elsewhere, or priorities developed by their governments and head offices, to be inappropriate as neither may be suited to the country context. And, the perennial debate within donor organisations, of whether to support growth or to develop the capabilities of the poor, is shown to be misplaced as the pro-poor growth agenda highlights the importance of breaking down traditional dichotomies between economic and social development.

67. Moreover, the pro-poor growth agenda recognises that helping to bring about pro-poor policy and institutional change is predicated upon strengthening the voice of poor women and men and supporting champions of pro-poor change to increase their influence over the policy-making process. Pro-poor change cannot be imposed from the outside. The practice of providing 'our solutions to their problems' is unproductive. Implementing policies to promote pro-poor growth involves a continuous process of strengthening the engagement between policy makers and the representatives of the private sector and civil society, especially those who represent the interests of the poor and promoting evidence-based, transparent decision-making, as well as innovation and lesson learning to arrive at policies suited to the local context.

68. The implications of the above are that donors need to reappraise the way they relate to partner countries and the modalities they use to provide assistance. Carrying on business as usual and scaling up aid to do more of the same will not suffice.

#### 5.2 Supporting In-country Policy Making Processes

*Donors should focus on supporting in-country processes that are inclusive of the poor. Donors should support the emergence and development of policy-making processes that are formal, transparent and accountable to the interests of the poor, and conduct their policy dialogue through them.*

69. As set out in the Paris Declaration on Aid Effectiveness,<sup>42</sup> effective aid requires the mutual commitment that partner countries exercise leadership in developing and implementing national development strategies through broad-based consultative processes and that donors respect country leadership and help strengthen their capacity to exercise it. In promoting the pro-poor growth agenda, donors should focus on assisting partner countries to develop and implement nationally owned poverty reduction strategies suited to the local context through processes that strengthen the social contract in favour of pro-poor growth.

70. Donors may help support the policy-making process at various levels and by build capacity to: i) identify the binding constraints to pro-poor growth; ii) undertake broad-based dialogue ; iii) innovate to find context-specific solutions, iv) make informed and evidence-based policy choices such as by carrying out ex-ante poverty impact assessments; and v) manage for development results and ensure accountability.

Donors may help to ensure that poverty reduction strategies better integrate pro-poor growth with progress on other dimensions of poverty.

71. Support for these policy processes should form the basis of policy dialogue between donors and partner country governments. The outcomes of the policy-making process and the policy dialogue should, in turn, be reflected in donors' country assistance strategies and the design of programmes, helping to make them better aligned and more relevant to country-led processes.

### **5.3 The Basis of Engagement**

*Donor support needs to be long term, flexible and responsive to country situations.*

72. The pro-poor growth agenda is, by its nature, long term. Helping partner countries implement policies and institutions needed to promote pro-poor growth is a continuous process, informed by the growth/inequality/poverty experience. To promote pro-poor growth, donors must therefore be prepared to engage with partner countries on a long-term basis and to provide aid predictably. Short-term assistance is unlikely to be productive, unless it complements and is well coordinated with more long-term development interventions.

73. As recognised in the Paris Declaration, donor harmonization is essential for improving the quality as well as quantity of aid. A well thought through, co-ordinated response by donors to poverty reduction strategies and other policy reform processes should help to ensure effective donor support. Each donor is likely to have core competency in particular areas addressed by the strategy or reform process and may therefore focus on supporting parts that they have the greatest value added to contribute, consistent with co-ordination and local ownership principles.

74. The aims of the assistance provided and the modality for delivering aid will need to reflect country situations. In addition to the level of development of the country and hence its access to resources, donor assistance will need to take account of the extent to which there is a functioning state and a social contract that is pro-poor. Clearly, middle-income countries do not need large, budgetary assistance. For these countries, addressing pro-poor growth is likely to focus on the pattern of growth: job creation, lagging regions, informality, discrimination on ethnic and gender grounds, etc., to better connect the poor to the growth process. In low-income countries with functioning states, budgetary support, with appropriate engagement over the implementation of poverty reduction strategies and pro-poor policy reform and support to capacity building where needed, may be appropriate.

75. In recognition of the need to innovate, the unpredictable nature of policy change and changing priorities, donors will need to be flexible in providing assistance. Earmarking aid for specific purposes without reference to the context well in advance of its use may not be helpful. It may well fail to address the binding constraint or prove inappropriate by the unpredictable nature of policy change. It is better to provide programmatic aid that will allow flexibility in supporting specific initiatives, as and when they become appropriate. The programmes should be informed by engagement in the policy reform process, address the broad, strategic direction of policy and institutional change and identify the types of investment and assistance that may be needed and enable individual projects to be undertaken flexibly whilst ensuring that they contribute coherently to desired programme outcomes. In promoting pro-poor growth, donors need to work with partners within the state, the private sector and civil society. Some areas of assistance may be suitable for sector-wide approaches (SWAPs) of the type now common in health and education. In others (private sector development, agriculture) there will also be a need to work directly with representatives of the private sector and civil society.

76. Given the aim of reducing poverty, what priority should donors give to different types of interventions? Should donors - on one hand – provide support at a general level of institutional change, capacity building or infrastructure or – on the other hand – go for interventions that are directly focused on poor people, e.g. targeted support to community-based organisations representing the poor?

77. A pro-poor growth lens shows that these different options should not be looked upon as mutually exclusive, but rather as complementary. Without the necessary policy and institutional reform, targeted support, no matter how well designed and implemented and irrespective of whether its subject is economic or social development, is unlikely to bring about sustained gains for the poor. On the other hand, focusing on the enabling environment alone ignores, for example, that small enterprises often don't have the capacities needed to exploit new market opportunities, or that women and particular social groups and the poor generally may start with disadvantages in economic capabilities, suffer discrimination and lack political voice to influence policy outcomes. Selecting combinations of interventions that are most efficient must be judged on a case-by-case basis depending upon the specific situation. To improve aid effectiveness it is also important to find optimal combinations which take account of comparative advantages within donor agencies in terms of staff capacity and financial resources.

#### **5.4 Fragile and Failed States**

*Donors need to stay engaged in states where respect for the rule of law and governance are weak*

78. With the aim of helping those who have helped themselves and to make aid more effective, there has been a move among some donors to shift resources to countries that have well-functioning states and a basic commitment to promoting pro-poor growth. Whilst this is understandable, with the objective of achieving the MDGs, it is not advisable to abandon millions of poor women and men that live in fragile or failed states and leave them with little hope for the future. Some 30% of the world's poor people live in such states. It is in these states that the incidence of poverty is likely to be highest and where aid may play a vital role as a catalyst for change. In Sierra Leone, during the civil war, poverty incidence exceeded 80%. The restoration of peace and the building of a functioning state, with the support of donors, have led to a substantial reduction in poverty.

79. However, the approach to these states will need to be adapted to their special circumstances. Many of these countries experience social or political conflict and, for them, the restoration of peace must be the first priority. Even if there is no outright conflict, national strategies are unlikely to be based on broad consultation and, even if they are, the state is unlikely to be able to effectively implement policies needed for pro-poor growth. Under these circumstances, donor assistance should focus on finding opportunities to strengthen policy dialogue, improving policy-making processes, developing capacities of those proposing policies that will promote pro-poor growth, building capabilities of organs of the state to exercise oversight over government and strengthening institutions. Resources can be directed to the development of human capabilities and the construction of basic infrastructure.<sup>43</sup>

80. The programme of assistance will need to be accompanied by engagement with the state to strengthen in-country processes that will restore its legitimacy and help the state improve its administrative and regulatory functions. Peer review mechanisms, such as those available under NEPAD or other country groupings, can be helpful in this regard. The incentive of greater international acceptance that would enable countries to participate in international institutions and draw on greater international assistance can help to serve as a catalyst for change, as proved recently by the ending of the north-south civil war in Sudan.

## 5.5 Rethinking Agendas and Approaches

*A pro-poor growth lens reveals the need to rethink agendas and approaches in areas important to pro-poor growth, such as private sector development (PSD), infrastructure, agriculture and risk and vulnerability.*

81. There is clear evidence that during the last decade some donors have tended to neglect the needs of sectors important to the strengthening of productive capabilities important for pro-poor growth. Over the past two years, POVNET's task teams working on PSD, infrastructure and agriculture have found that the pro-poor growth lens requires donors to rethink agendas and approaches to these areas that have a major impact on pro-poor growth (see box 8 for examples). Instead of stand-alone areas for donor assistance, they need to form an integral part of poverty reduction strategies that focus on pro-poor growth. There are substantial synergies between these areas and, together, they impact on both the pace and pattern of growth. A fuller description of the contribution of these areas to pro-poor growth and implications for donors' strategies is presented in separate reports on these areas.<sup>44</sup>

82. *Private sector development* contributes to pro-poor growth by helping to bring about sustained and inclusive growth that provides opportunity for the poor. Rather than attempting to assist types of firms (e.g. certain size groups, activities, sectors) alone, the PSD agenda needs to focus on how policies combine to provide incentives that shape private sector activity that brings about pro-poor outcomes in markets that matter for the livelihoods of the poor. To help donors increase the leverage of private sector development on reducing poverty, POVNET prepared guidance on six important topics:

- Removing barriers to formalisation. Donors can support efforts by developing countries to reduce such obstacles as regulatory and administrative barriers, fees and financial requirements, corruption in public administration, socio cultural attitudes and lack of key business services.
- Implementing competition policy. Donors should provide technical assistance and capacity building targeted at supporting the formulation of competition policy and strengthening institutions responsible for enforcing competition law.
- Promoting the supply side response: Business development services and financial assistance. Donors should adopt more market based and sustainable approaches to providing support to firms and focus on the causes of problems, promote a level playing field, avoid or minimise subsidies and have a clear exit strategy.
- The financial sector's contribution to pro poor growth. Donors should encourage developing countries to improve the capabilities of supervisory and regulatory authorities, strengthen financial intermediaries, support prudent mobilisation of savings and remittances and help bridge the gap between banks and microfinance institutions so that greater access to financial services is mainstreamed in the development of the financial sector .
- Enhancing women's market access. Donors should support policies that address structural and social barriers to women's participation in labour, financial, goods and services markets.
- Constructing inclusive public private dialogue. Donors should support, in a time-bound and strategic way, the establishment and operation of dialogue processes at national, sub-national and local levels. Helping poor entrepreneurs to participate and promote their interests is key.

83. *Infrastructure* contributes to both growth rates and growth patterns and to both income and non-income dimensions of poverty. The agenda for infrastructure needs to change from promoting growth to promoting pro-poor growth, meeting the needs of different groups and from projects in isolation to projects/programmes as part of networks that harness synergies between types of infrastructure. POVNET has developed four guiding principles for developing infrastructure to promote pro-poor growth:

- Promoting country-led frameworks as a basis for co-ordinated donor support.
- Enhancing infrastructure's impact on pro-poor growth by focusing on bottlenecks, meeting the needs of different groups with appropriate services and tariff levels and benefiting from synergies between types of infrastructure.
- Improving management of infrastructure by prioritising maintenance and rehabilitation, building management capacity, reducing corruption and better management of environmental impacts.
- Increased and better use of financial resources by greater efficiency and cost recovery, improving private participation and more predictable public funding and donor assistance.

84. *Agriculture* is crucially important for ensuring a pro-poor pattern of growth. Sound investments in agriculture and policy reform are cost-effective investments in pro-poor growth. The agenda for agriculture to contribute to pro-poor growth is much broader than increasing sector output. It focuses on agriculture's role in helping to improve existing livelihoods, to serve as the catalyst for transforming livelihoods by providing new opportunities, on and off-farm, and to reduce risk and vulnerability. Priorities for action within a pro-poor growth agenda for agriculture include:

- Increasing access to markets and assets, improving access to productivity enhancing technology, especially for small producers and agribusinesses, and increasing investment in infrastructure (power, irrigation, roads).
- Increasing opportunity to earn non-farm incomes through policies that increase access to capital, facilitate the movement of labour, investment in transport and communications services and access to health and education.
- Addressing risk and vulnerability by focusing on prevention strategies (e.g. drought resistant crops, irrigation), mitigation strategies (e.g. secure savings and crop and price insurance instruments), as well as coping strategies (e.g. smart transfers and safety nets).
- Supporting the development of country-led national development strategies that include agriculture (including forestry and fisheries) and rural development as part of the pro-poor growth agenda and fostering partnerships on the ground between the state, the private sector, civil society and donors to bring about policies that will increase the contribution of agriculture to pro-poor growth.

85. Work is underway within POVNET to develop approaches to addressing risk and vulnerability, including instruments that increase social protection that are adapted to conditions in the developing countries.



**Box 8. Promoting pro-poor growth: Examples of evolving agendas and policy responses****Private Sector Development**

<b>Evolving agendas</b>		<b>Policy responses</b>
<i>From ...</i>	<i>To ...</i>	
Target firms and sectors directly.	Promote enabling environments for pro-poor growth, focusing on market outcomes.	Strengthen the enabling environment, ensuring an improved risk to reward ratio. Any direct firm level support should be non-market distorting.
Informal sector is marginal and temporary.	Informal sector is large, the way from informality to formality is a continuum.	Reduce disincentives to formalisation, facilitate risk taking.
Institutions and processes of institutional change were neglected.	Policy and institutional reforms	Promote dialogue between the state, the private sector and civil society.
The private sector is one of many stand-alone sectors.	PSD is a central part of a national poverty reduction strategy (PRSs).	Link/merge PSD in wider PRSs focusing on both pace and pattern of growth.

**Agriculture**

<b>Evolving agendas</b>		<b>Policy responses</b>
<i>From ...</i>	<i>To ...</i>	
Focus on commodity production and increasing farm productivity.	Focus on household productivity through diversified production and off farm work.	Build household assets, reduce market-related barriers and expand access to local, national and international markets.
One work location	Multiple work locations	Support diversified livelihoods
Smallholders are marginal.	Reduce risk and vulnerability to increase market participation.	Secure assets (land, water, finance) and mitigate shocks (new forms of insurance).
One size fits all technologies.	Technologies that respond to the very diverse needs of a wide range of small producers.	Target research and development investments to smallholders.
Agriculture is synonymous with the farm.	Agriculture contributes to growth and poverty reduction beginning at the field level all the way to the table.	Promote a holistic approach to rural poverty reduction in country PRSs.

**Infrastructure**

<b>Evolving agendas</b>		<b>Policy responses</b>
<i>From ...</i>	<i>To ...</i>	
Donor driven/project based	Country led/programmes	Coordinate and align donor support to country led frameworks.
Infrastructure for growth	Infrastructure for inclusive growth, involving and benefiting the poor.	Target the poor to improve their access, encourage their involvement and promote their employment, ensure affordability, e.g. by use of "smart subsidies".
Finance capital costs	Greater focus on governance structures and the sustainability of infrastructure facilities; stronger focus on maintenance.	Emphasize cost recovery, improved public operator management and enhanced transparency to address corruption and environmental sustainability.
Private sector fills the gap	Greater public sector role with support from donors with public private partnerships.	Make aid predictable, apply mix of financial instruments to leverage private sector investment and build capacity in capital and financial markets.

## **5.6 Building Capacity in Donor Organisations.**

*Donors need to enhance their organisational capacities to effectively support country-led, pro-poor growth.*

88. The pro-poor growth agenda requires donors to change the way they are organised to provide assistance. Effective donor co-ordination is essential in addressing the broad agenda for pro-poor growth. In some countries, such as Tanzania, donors are already sharing the analysis required to develop country strategies with each other and are co-ordinating their responses to nationally-owned poverty reduction strategies. Such practice will need to be replicated in all countries.

89. Success in promoting pro-poor growth will also depend upon the capabilities of field office staff to engage with partner countries long-term, informed by the political economy of change, structures for policy-making and a sound understanding of how to influence the policy-making process. This may require donors to increase their understanding by undertaking assessments of power relations, governance and change processes.<sup>45</sup> Field staff may require greater delegation of authority to engage effectively, be empowered to take the risks involved in supporting policy change, and not penalised for taking on difficult, time consuming and risky initiatives in the short term. Staff will need to be in the field for an extended period of time if they are to build the knowledge and network of contacts across the state, the private sector and civil society. This may require changing the incentives that staff are currently provided with in terms of career development.

90. Home office staff need to support field staff by helping to undertake analysis to identify the binding constraints to pro-poor growth and providing guidance on the engagement process. Donor staff need to improve their understanding of the transmission mechanisms through which development interventions contribute to pro-poor growth patterns and be able to analyse how interventions affect different stakeholders in relation to different capabilities (economic, human, political, socio-cultural, protective). Analytic tools such as poverty impact assessments can help in these respects. Skills such as understanding power relations and influencing change processes and expertise in developing infrastructure may need to be strengthened through training and recruitment. Additional training may need to be given to re-orient approaches to PSD, agriculture and infrastructure, and to enable staff to better integrate economic, social and political development perspectives, needs and opportunities.

91. The pro-poor growth agenda shows that the ways in which field and home offices work together need to be reconsidered. Traditional specialist skills-based departments need to break out of their “professional silos” to forge multi-disciplinary teams. The monitoring and evaluation of aid effectiveness in promoting pro-poor growth needs to move away from inputs (aid volumes) and outputs to processes, outcomes and impacts. Inputs and outputs may not reflect the progress achieved in bringing about pro-poor policy and institutional change. Home office staff have an important role to play in influencing other departments of their government to promote policy coherence so that policies in areas such as foreign investment, trade and immigration complement the efforts of the donor agency.

## **5.7 Key Issues for Donors**

- How can donors support the development of nationally owned poverty reduction strategies and reform processes that address pro-poor growth and poverty reduction effectively?
- To what extent is donor assistance long term and adapted to the country situation? To what extent is aid sufficiently predictable and flexible in responding to changing partner country needs?

- Is engagement confined to the state or broad-based across the different segments of society? How can donors better apply market-based approaches in their support to private sector development in order to avoid distorting markets?
- Do donors and partner countries share the same views regarding the most appropriate mix of interventions (such as support for institutional change or support that is more directly targeted at poor peoples' needs) and on the comparative advantages of different donor organisations?
- What approaches are used to engage with fragile or failed states?
- In what ways have the agendas for important areas that impact pro-poor growth (e.g. PSD, agriculture, infrastructure and risk and vulnerability) been reassessed in the light of the pro-poor growth agenda?
- What is needed to support field and home office staff in promoting pro-poor growth? Are field staff sufficiently empowered to engage with partner countries and take the risks inherent in promoting pro-poor policy change? Are there incentives to promote staff to work in multi-disciplinary teams?

## ENDNOTES

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