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PROMOTING PRO-POOR GROWTH - OVERARCHING PAPER

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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, security). This policy statement focuses on one dimension of that bigger picture – the role of growth in reducing economic poverty. In doing so, it looks at the relationship between economic and other dimensions of poverty and how policies for economic growth and other policy areas (e.g. health, education, security) need to interact so that, collectively, they can make major and sustainable inroads into poverty reduction. Two key messages from this work are that:

- The pace and the pattern of economic growth are interlinked and critical for long term and sustained poverty reduction. Policies therefore need to promote both dimensions to make growth pro-poor, i.e. to make growth more effective in reducing poverty.
- Policies to tackle the economic, human, social, political and environmental dimensions of poverty go hand in hand and are mutually reinforcing.

2. When implementing the policy guidance on how aid donors can contribute to and facilitate pro-poor growth, they must bear in mind that the poor are not an 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.

3. **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.** Pattern and pace are interlinked and need to be addressed together. 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.
- ii) **Rapid and sustained economic growth is essential for reducing poverty.** Economic growth is an essential requirement and a major contributing factor in reducing economic poverty. The faster and longer sustained is growth, the greater its impact on economic poverty is likely to be. Policies for sustaining growth (e.g. macroeconomic stability, institutional quality, effective governance to reduce corruption, a favourable investment climate, etc.) should increase the incentives for entrepreneurship, investment and productivity growth.
- iii) **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 differences in initial conditions and whether growth occurs in areas and sectors where the poor 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 and infrastructure.
- iv) **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 pro-poor 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, religion).

- v) **Risk and vulnerability 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. The journey out of economic 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 traps. Policies that tackle risk and vulnerability through prevention, mitigation and coping strategies improve both the pattern and pace of growth and are a cost effective investment in pro-poor growth.
- vi) **Policies need to tackle the causes of market failure and improve market access.** Well functioning markets are important for pro-poor growth. Access to productive assets and for markets for goods and services need to be improved. Market failure hurts the poor disproportionately and is a serious obstacle to pro-poor growth. Policies need to tackle the causes of market failure, such as red tape, regulatory barriers and information asymmetries, particularly in markets that are important for the livelihoods of the poor, e.g. agricultural, financial and labour markets.

4. **Poverty is multidimensional and pro-poor growth will be facilitated by progress on the other dimensions (e.g. human, social, environmental, and political). To be more effective, policy makers need to better understand and tackle these interdependencies and thus promote a virtuous cycle of economic, human, social, environmental and political development in mutually reinforcing ways.**

- i) **Policies to tackle the economic, human, social, environmental and political dimensions of poverty go hand in hand.** Perceptions of dichotomies (e.g. as sometimes set out in terms of economic *versus* social policies) can be misplaced. The pace and pattern of growth have economic, human, social, environmental and political 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. Policies for poverty reduction thus need to build on and implement this consensus.
- ii) **Policy trade-offs still exist, but they need to and can be better managed, including through sequencing to tackle the binding constraints.** Decision makers should avoid policies which promote only one dimension of poverty reduction while undermining others. Policies need to be complementary rather than compensatory. Binding constraints can be identified from analysis of the growth, poverty and inequality experience, and investment decisions need to pay attention to transmission channels in order to increase their impact on poverty reduction. The quality of institutions is crucial to handling trade-offs in ways that foster pro-poor outcomes. Policy choices need to be informed by poverty impact assessments.

5. **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 for their interests.**

- i) **The poor need to be informed and empowered** to participate in and influence the policy reform process that goes with effective poverty reduction strategies (PRSs). Policies are needed to increase the voices and influence of poor women and men in order that evidence-based policies promoting pro-poor growth (rather than narrow vested interests) will prevail.
- ii) **A properly functioning state is essential 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 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 between the diverse interests of different segments of society.** This entails a better understanding of the political economy 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.
- iv) **PRSs need to be nationally owned, to better integrate the multiple dimensions of poverty and to include stronger stakeholder involvement.** The early phases of the PRS process have been weak in these respects. A better evidence based understanding of the social dynamics and political economy of growth together with greater stakeholder dialogue in their preparation and implementation, should contribute to strengthening the national PRS process.

6. **The pro-poor growth agenda has important implications for the targets and delivery modes of donor support. It is not a “business as usual” agenda, and just “more of the same” will not be sufficient.**

- i) **Donors should focus on supporting in-country processes,** identifying and promoting drivers of change, aligning themselves collectively behind credible partner country strategies for pro-poor growth in line with the Paris Declaration principles on aid effectiveness. Where credible strategies are not in place, donors should help partner countries and other stakeholders build the capacities to design and influence such strategies.
- ii) **Donor support needs to be flexible and responsive to country situations.** Policies need to be informed by better analysis of the constraints to growth and poverty reduction and the impacts of their policies through tools such as poverty impact assessments. POVNET has developed a simplified, cost effective approach that may be used widely. Policies must take account of country specificities and the political economy of the poverty reduction agenda, target the binding constraints to pro-poor growth, and be adaptive to what is possible. Effective scaling up requires sufficient absorptive capacity.
- iii) **Donors should stay engaged in states where the above approaches are not replicable because of weak or bad governance.** Donors need to adopt a different approach to fragile and failed states which focuses on investing in human capacity and to find opportunities to strengthen policy and dialogue frameworks. Sustained capacity building efforts are particularly important in such cases.

- iv) **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 their agendas.** The importance of these areas for the pace and pattern of growth has been underestimated. New approaches to strengthen their contributions have been developed in POVNET's work on pro-poor growth.

- v) **Donors need to develop capacities in aid agencies, at both capital and field levels, to effectively promote pro-poor growth.** They need to work in ways that exploit cross-sector synergies and which strengthen donor co-ordination. They need to provide appropriate support and incentives to field staff and move from headquarter driven sector structures to build multidisciplinary teams empowered to influence and implement policies at the field level.

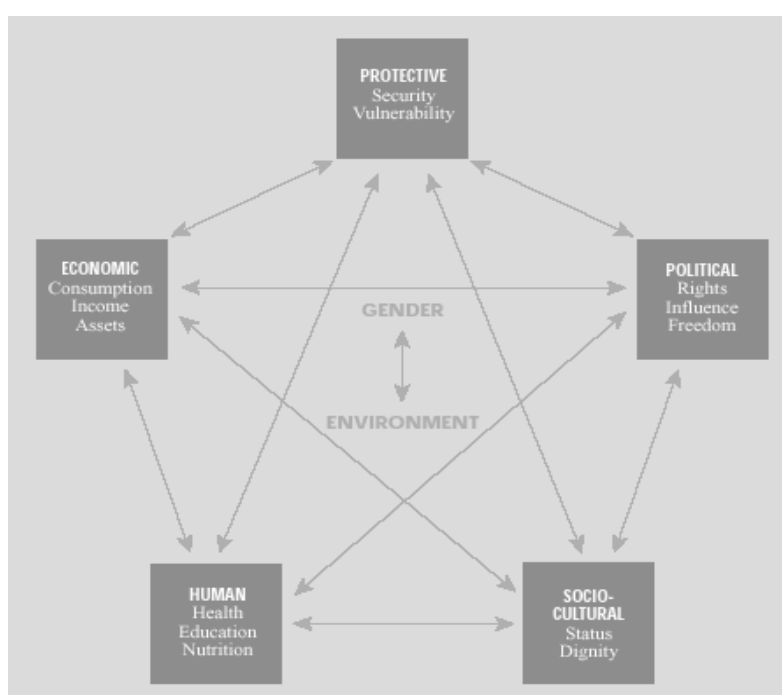
CHAPTER 1

INTRODUCTION

1.1 The Multiple Dimensions of Poverty

7. 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 (figure 1).

Figure 1. The Multi-dimensional Poverty Framework



8. The focus of the present report, on pro-poor growth, is on how to reduce economic poverty effectively. 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?

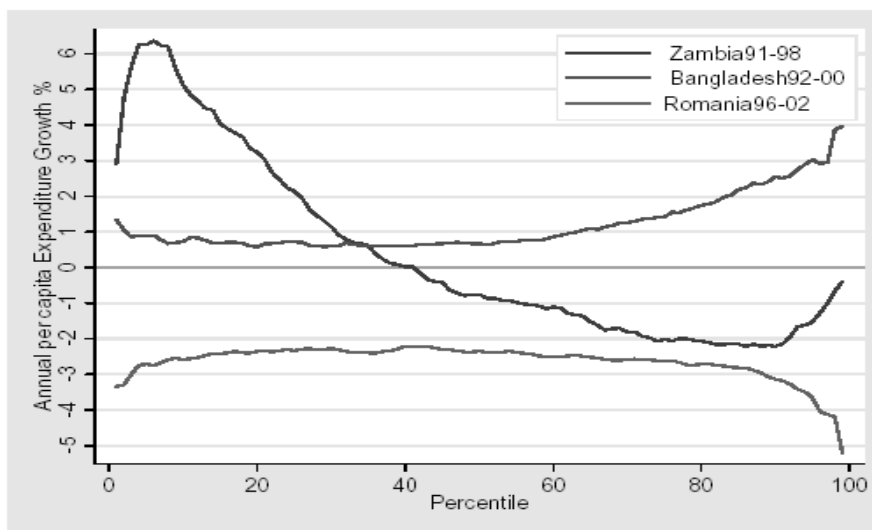
9. Reducing economic poverty is vital for over 3 billion people, roughly half the human race, with incomes less than \$2/day who are challenged to meet their basic needs – and even more crucial for the 1 billion people with incomes less than \$1/day, who struggle for survival. The experience of many 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 world 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. All countries need to accelerate pro-poor growth, focusing not just on pace but also the pattern of growth to ensure that the poor are able to participate in, contribute to and benefit from growth.

10. 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 the MDG 1:1?

11. 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. This may be illustrated by "growth incidence curves", which indicate how the average income growth in a country may be decomposed for different income groups (see Figure 2). Such curves may be used to analyse how different groups benefit from growth in absolute as well as in relative terms, and whether some groups (regions, urban-rural households, etc) are being excluded from these processes¹. Figure 2 shows that in Zambia, the poor benefited from growth (even though growth was weak), whereas in Bangladesh better-off households benefited more. In order to deepen the analysis of growth processes and assess their outcome with a pro-poor growth lens, a large variety of tools may be applied (see chapter 4).

Figure 2. Selected growth incidence curves



Source : OPPG, 2005

1.3 The Importance of Context

12. Developing effective strategies to reduce poverty requires an understanding of who the poor are and how they earn their livelihoods. Poor women and men are not an homogenous group and they 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 and the gender dimension are 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 has ceased to function effectively. These variations require adapting the strategies described below to suit the particular context.

1.4 The Structure of the Report

13. Pro-poor growth is growth that is *effective* in reducing economic poverty. What is meant by "effective" and the policies needed to achieve it are the themes of this report.

14. The report is structured as follows:

- **Chapter 2** sets out the policies required to promote pro-poor growth. It examines how growth may be made faster, longer, sustained and more effective in reducing economic poverty. It looks at ways to address inequality and risk and vulnerability and to make markets work better for the poor.
- **Chapter 3** examines the way pro-poor growth contributes to and benefits from progress on the other dimensions of poverty. It examines traditional dichotomies between pro-growth and pro-poor policies using a pro-poor growth lens. It addresses the inter-linkages between economic, human, social, environmental and political development and the trade-offs that exist between these different dimensions of poverty in promoting pro-poor growth.
- **Chapter 4** focuses on how to increase the likelihood that policies to promote pro-poor growth will be implemented. It sets out the way that political empowerment, the policy making processes of the state, the wider political settlement and nationally owned poverty reduction strategies may be supported to help bring about policy and institutional reform to promote pro-poor growth.
- **Chapter 5** considers the role of donors in the pro-poor growth agenda. It shows how donors need to align assistance to support in-country processes, how the targets and aims of donor support may need to be changed in response to country contexts and the implications of the pro-poor growth agenda for donor organisations. It illustrates the way donors will need to change how they approach important contributors to pro-poor growth such as private sector development, agriculture and infrastructure.

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.

15. 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 distribution or pattern later, it has become clear that the two need to be addressed together. Policies that impact pace also address pattern and vice versa and so neither should be approached in isolation.

2.2 Sustaining Growth

Rapid, sustained growth is essential for reducing economic poverty.

16. There is overwhelming 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.² The growth component was the main contributing factor in the rise of the incomes of the poor.

17. All countries experience short episodes of relatively modest growth. 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: in India, as little a change as government signalling a more positive sentiment toward business was sufficient to trigger growth.³ Sustaining and accelerating growth requires deepening the incentive to invest and improve productivity through appropriate policies and institutions. Recently, growth rates have increased in Africa. The challenge now is to ensure that growth accelerates and is sustained by appropriate policies and institutions.

Box 1. Private Sector Development (PSD)

Private sector development both helps sustain economic growth but also makes growth broader based and more inclusive. Jobs and self employment are important pathways out of poverty. As the private sector is the main source of jobs, private investment and entrepreneurship expands employment opportunities, including for the poor, but also helps generate the revenues that households and governments need to expand access to the health, education and infrastructure services that will increase productivity. This will lead to more rapid economic growth that involves and benefits the poor.

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 can take advantage of those. But 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.⁴ While informality provides a useful safety net, especially for many women and people from disadvantaged groups, it is not conducive to sustainable growth and poverty reduction – it distorts markets, excludes people from basic protections and reduces revenues for social and other public expenditures. In addition, there are substantial assets held in the informal economy – in Tanzania, their estimated value is USD 29 billion⁵ – that could be used more productively to help spur economic growth. Reducing regulatory and other barriers to the formalisation of firms, enhancing access to labour, financial, goods and services markets for women and men, helping poor people deal with their risks and vulnerability and encouraging innovation and competition will all contribute to promoting faster growth as well as growth patterns that are beneficial to the poor.

18. 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. Conflict and policy volatility, caused by frequent political change, undermine growth. Policies that contribute to faster and longer sustained growth include -- macro-economic stability; good institutional quality and 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 increased access to these resources. Harnessing the international economic linkages of trade and investment can help to sustain rapid growth but this needs to be accompanied by a more equitable international trading system and complementary policies to build domestic capacity and competitiveness. It also requires policies that enable productive assets to be redeployed, that reduce the cost and risk of trading and help the poor to adjust to the new situation. An effective regulatory framework to ensure environmental sustainability is vital, not least because a high proportion of developing countries are dependent on natural resources and as much of agriculture takes place on fragile lands.

19. 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.⁶ 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 experience and policy and institutional framework to identify the binding constraints that need to be addressed to sustain rapid growth.

2.3 Pro-Poor Growth Patterns

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.

20. 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.⁷ 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 in terms of sectors from which poor women and men earn their livelihoods, 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 future.

Box 2. 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 difficulties to achieve pro-poor economic growth. There is strong evidence that good 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 help poor people break out of poverty traps. There is evidence that increased access to infrastructure contributes to lower inequality⁸. 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 materialize. Between 1997 and 2003, donor support to infrastructure decreased from roughly 25% to 15% of ODA. Infrastructure investment and maintenance has been neglected and governments and donors are today giving increased attention to infrastructure.⁹

21. In addition, policies are needed to ensure that the poor are not marginalised from the growth process. The regions and sectors in which the poor are concentrated may lag behind, reducing opportunity for the poor to escape poverty. 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, improving the investment climate, greater investment in health, education, infrastructure and agriculture and encouraging labour mobility to other regions, may pay dividends.¹⁰ When agriculture lags other sectors, growth tends to be less pro-poor¹¹. The growth of agricultural (land) productivity will contribute to a pro-poor pattern of growth, particularly if combined with the growth of opportunity in non-farm activities to ensure that rural incomes rise rapidly.

22. 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,¹² 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 3. Agriculture

Growth in 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 Revolution¹³. 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/day¹⁴. 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.¹⁵ Such impacts are usually best realised where there is an equitable distribution of assets, particularly land,¹⁶ 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 and yet, like infrastructure, both spending 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% 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; 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. 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. Governments need the support of donors.

2.4 Addressing Inequality

High inequality reduces the pace of growth and its effectiveness in reducing economic poverty.

23. High levels of income inequality reduce the effectiveness of growth in reducing economic poverty. Growth, inequality and poverty are interlinked. With a high level of income inequality, growth needs to be faster and longer sustained to achieve the same level of poverty reduction. Distributional changes during growth may undermine the effect of growth on the incomes of the poor. In Ethiopia, between 1981 and 1995, growth should have resulted in a 31% reduction of income poverty. Instead, a negative distributional change of 37% resulted in income poverty rising by 6%.¹⁷

24. Evidence suggests that rising inequality is not inevitable in the early stages of development as believed in the past. Growth reduces income inequality as frequently as it increases it.¹⁸ 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.

25. Inequality in the distribution of assets results in poor people having limited access to productive assets, and reduces their ability to increase their incomes and contribute to growth. Men and women have been shown to work harder and invest more on land they own or over which they have secure use, as evidenced in China and Vietnam¹⁹. Investment in land and natural resources by poor people and redistribution of land through market based mechanisms will increase pro-poor growth. Greater equality of opportunity contributes to higher growth. When markets fail, a frequent situation in the 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. Growing inequality in opportunity, assets and incomes runs the danger also that mounting dissatisfaction and a sense of injustice combine to undermine the political and social stability that is vital for sustaining growth.

26. 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 the key messages described below. 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 public spending is not efficient and benefits the non-poor disproportionately²⁰.

27. Gender biases, social stigma associated with caste, 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. Policies are needed to improve governance over laws that most countries have adopted to address discrimination on social grounds.

28. Policies that increase women's participation in the work force and the returns to that participation are major contributors to pro-poor growth. Women face particular difficulties in participating in the growth process because of their role as carers, discrimination in accessing assets such as land, and negative social attitudes. Greater access to infrastructure, reproductive health services and child care, declining fertility rates, higher female life expectancy and improved social attitudes all help to increase women's participation in the work force. Greater access for girls and women to education at all levels, access to land and finance and equitable employment policies, help to increase returns to women's participation in the work force²¹.

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 should be an essential element of pro-poor growth strategies.

29. 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 inherently risk averse. Prevention, mitigating or coping strategies that reduce vulnerability to risk, such as increasing the reliability of agricultural incomes and deepening insurance markets so that they reach the poor, 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.

30. 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 contingency plans to cope with natural disasters and man made shocks to avoid extreme deprivation for the poor so that they do not end up in poverty traps from which they cannot escape. If the poor are forced to sell or deplete the very assets that they need to earn better incomes, they will not be able to escape poverty.

Policies that prevent extreme deprivation such as labour schemes to build infrastructure are useful in this regard. Where poverty traps exist, 'smart' transfers that are contingent on the poor building assets by accessing health and education for their children should help, such as Mexico's Progresa/Oportunidades.²² Addressing barriers for the disabled to find productive employment is also valuable. Providing safety nets will help to prevent extreme deprivation amongst the elderly and chronically infirm.

2.6 Pro-poor growth needs well functioning markets

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.

31. Poor women and men participate in markets which determine their ability 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 deepening that also increases access of the poor to financial services, greater access to and security over land and other property for the poor, well functioning labour markets that increase formal job creation and increase labour mobility whilst meeting core labour standards are all needed.

32. As noted above, market failures are common in the 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 in participating in them through discriminatory formal or informal institutions and higher costs of accessing markets.

33. 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, the poor are 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.

2.7 Key Issues to Address for Pro-Poor Growth

- Is the growth-inequality-poverty experience satisfactory? Are groups of poor women and men being marginalised in the growth process?
- Are the fundamental conditions for sustaining growth in place? What are the key policies and institutions that need to be improved to achieve sustained growth?
- Is growth broad based and inclusive of the poor? Are some regions lagging, is agricultural productivity improving, is informality increasing, are the poor increasing access to productive assets and how efficient is public spending on basic social services and is it reaching the poor? Do women have equal access to productive assets and are they benefiting equitably from public spending on basic social services?
- What is the level of inequality and is it increasing? What can be done to reduce asset inequality and bring about greater equality of opportunity? What aspects of the pattern of growth may be improved to reduce income inequality? What barriers need to be removed for women to participate in and benefit from the growth process?

- Are risk and vulnerability reducing growth and its effectiveness in reducing economic poverty? Are there policies and instruments in place for poor people to manage their health risks, increase reliability of agricultural incomes, pool their livelihood risks by deepening 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 and infirm?
- Are markets for productive assets and goods and services provided by poor men and women delivering pro-poor outcomes? What is required to bring about systemic change in these markets that will deliver pro-poor outcomes sustainably?

CHAPTER 3

ADDRESSING THE MULTIPLE DIMENSIONS OF POVERTY

Poverty is multidimensional and pro-poor growth will be facilitated by progress on other dimensions of poverty. To be more effective in reducing poverty, policy makers need to better understand the inter-linkages between economic, human, social, environmental and political development to establish a virtuous circle of poverty reduction.

3.1 Inter-linkages between the different dimensions of poverty

Reducing economic poverty will contribute to and be facilitated by progress on other dimensions of poverty.

34. 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. Reducing economic poverty through pro-poor growth will contribute to progress on other dimensions 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 address other forms of deprivation. In turn, the conditions needed for pro-poor growth will be facilitated by progress on other dimensions of poverty.

35. However, focusing on economic poverty alone, as some have done in the past, is not likely to prove as effective in reducing poverty as holistic strategies that combine progress on economic poverty with addressing the other forms of deprivation that poverty entails. Without effective policies to address them, the human capabilities of the poor 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 in Bolivia²³. In turn, the lack of human capabilities will tend to reduce 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 are required to check the spread of the pandemic and to provide health care for the millions who are or will be affected.

36. The social dimension of poverty focuses on status and dignity. A high proportion of the economic poor in middle income countries are members of social groups that are discriminated against socially: 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 discrimination can leave millions in economic poverty despite per capita incomes reaching middle income levels. 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. 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 will reduce both social and economic poverty.

37. Enhancing human security encompasses two dimensions of individual freedoms: the freedom from fear of conflict and natural disasters and freedom from want in the form of hunger and lack of basic social services. Chapter 2 showed why addressing risk and vulnerability should be an integral part of pro-poor growth strategies. The wider concept of human security, with its focus on civil liberties, should help to develop effective policies to address the risk of war and conflict, man made and natural disasters, hunger and want, creating the conditions for addressing economic risk and vulnerability. The experience of Rwanda and Sierra Leone shows how increasing human security may start the process of laying the foundations for pro-poor growth.

38. Environmental sustainability 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 level, bear heaviest upon the poor. Policies that promote environmental sustainability underpin growth by ensuring that natural resources are not exploited unsustainably. Such exploitation is frequently accompanied by a 'resource curse'.²⁴ 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. Policies to promote environmental sustainability are thus critically important for pro-poor growth. They are also crucial for living conditions world wide.

39. 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 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.

3.2 Traditional Dichotomies

Traditional dichotomies between pro-growth and pro-poor policies are misplaced. Policies to tackle economic, social, environmental and political development need to go hand in hand.

40. 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 emphasized 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 complements in reducing poverty. In fact, an effective poverty reduction strategy needs to encompass both these perspectives.

41. 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 the growth of output. Equally, without growth, it is unlikely that investing in the capabilities of the poor will be translated into reduced poverty because the poor will not have the opportunity to use their new capabilities to earn higher incomes, as evidenced by the experience of Jamaica.²⁵ 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 contribute to 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.

42. One of the main reasons why the 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 or different from investing in infrastructure to enhance the ability of poor people in rural areas to participate in the growth process.

43. 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 against 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 develop 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 revenue to support household and public investment in health and education.

44. 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, it is possible to pursue pro-growth and pro-poor policies such as increasing the efficiency of public spending on social services and infrastructure and ensuring that they reach the poor. There is room for greater innovation in meeting the cost of investment from the private sector provided there are incentives to invest in health, education and infrastructure that will provide acceptable commercial returns. In such situations, governments, aided by donors, can focus on investing in ensuring access for the poor. The development of micro finance institutions that are part of the mainstream financial sector is another example of policies that are able to combine pro-growth and pro-poor objectives.

45. Priorities for the short term may be set by examining the growth/inequality/poverty experience to find the binding constraints to economic 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 and investment design and choices (see box 4). It focuses on identifying transmission channels and the potential impacts of the intervention on different groups.

Box 4. 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 restricted approach that can help to inform policy and investment choices and design. This draws on the PSIA framework, the MDGs and other important measures. This framework for ex-ante poverty impact assessments (PIAs) focuses on:

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

46. Currently, in many countries, a vicious circle exists whereby poor women and men are marginalised from the growth process and this, in turn, limits the extent to which they are able to contribute to growth, thus reducing the pace of growth. This needs to be replaced by a virtuous circle whereby growth is stimulated by improved incentives to invest and increase productivity across the economy. This enables greater investment in social development that in turn enhances the contribution of poor people, leading to pro-poor growth.

3.4 Key Issues in Addressing the Multiple Dimensions of Poverty

- Do national development and poverty reduction strategies reflect a holistic view of the various dimensions of poverty?
- How close are the linkages between economic and non-economic dimensions of development in the country? Is the reduction of economic poverty being accompanied by progress on other dimensions of poverty?
- Is proper attention given to existing linkages between the economic and non-economic dimensions of poverty in regional/local government planning, e.g. by promoting access to well maintained infrastructure, which helps to reduce several dimensions of poverty?
- Are policies for reducing the human, social and security dimensions of poverty helping to bring about necessary conditions for pro-poor growth?
- Has the importance of environmental sustainability to pro-poor growth and living conditions been reflected in effective policies and institutions?
- Are existing institutions able to handle potential trade-offs between pro-growth and pro-poor policies in a constructive way? Are opportunities for sequencing policy reforms and coordinating investments in social and economic areas fully exploited?

CHAPTER 4

POLITICAL EMPOWERMENT AND CHANGE PROCESSES

Policies to promote pro-poor growth are more likely to be designed and implemented if the poor are empowered to participate in the policy making process and if policy makers are made more accountable to the interests of the poor

4.1 Political Empowerment

The poor need to be informed and empowered to participate in and influence the policy reform process that goes with effective poverty reduction strategies.

47. As noted in chapter 3, the political dimension of poverty may result in policies that reflect the interests of the rich and powerful, rather than those required to promote pro-poor growth and address the multiple dimensions of poverty. Policies are needed to bring about a stronger, better informed voice for poor people with which they, and those who represent their interests, may influence policy makers. This may require the strengthening of the capacity of organisations (farmers' and women's organisations, trade unions, politicians, media etc.) to analyse the growth/inequality/poverty experience and identify the key policy and institutional reforms required to promote pro-poor growth. Such analysis should take account of both the pace and pattern of growth, whether inequality is increasing and how different groups of the poor are benefiting from growth. 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 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

A properly functioning state is essential for responding to the interests of the poor.

48. 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 the 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, often leading to social and political conflict. The inevitable consequence of such developments is partial or complete failure of the state and conditions in which pro-poor growth is highly unlikely.

49. The structure and characteristics of the policy making process affect the extent to which the state is accountable to the interests of the poor. Centralized, autocratic policy making by central government will reduce 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 are likely to be more suited to the context and pro-poor if policy making is decentralized. Representatives of intended beneficiaries (including poor women and men) need to be included in the oversight of their implementation

locally. 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.

50. 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. The impact on the business climate of improved governance may help to trigger a process, during which public and private sector institutions are strengthened and they come to look upon each other as partners in development. This makes both more inclined to participate constructively in the public debate, contribute to continued improvements in public policy and governance and undertake the investments needed to promote pro-poor growth.

51. 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 micro-entrepreneurs in the formal and informal private sector. Civil society has an important complementary role to play by articulating the interests of 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 are lost. Reforms at local government level have a strong impact on improving the local business climate. 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 with 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.²⁶

52. It is important to note, though, that dialogue, by itself, is not a panacea²⁷. Interest groups in society, particularly those representing the interests of the poor, need to be better informed and organized in order to participate effectively in public-private dialogues and to articulate and defend their interest more widely. In Africa, where the boundary between the "public" and the "private" is fluid, the quality of the dialogue depends on the structure of the participating institutions. Merely assembling government representatives, high level civil servants and 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 organizational and process dimensions of the dialogue can turn out to be key to its success. For example, it is important to analyze in advance the political economy in order to determine whether such a dialogue is both feasible and timely, and linked to a specific policy reform process with declared objectives such as the formulation of a poverty reduction strategy or green/white paper etc. Donors can assist in making such dialogue more effective by providing the evidence required, sharing knowledge about best practice and supporting an effective policy making process.

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.

53. 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 reform needed to promote pro-poor growth will 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.

54. 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: those against pro-poor change in one instance may support other pro-poor policy changes. 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 whether the form of contestation and negotiation involved in policy change is based on a 'corporatist' (based on national interest) approach to national development or a 'confrontational' approach, whereby one viewpoint attempts to dominate the others, will also help in promoting policy reform in favour of pro-poor growth.²⁸

55. 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 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 organs of the state to respond effectively to change should prove helpful.²⁹ This kind of capacity building, to strengthen the demand for change and the capacity of the state to respond, should be supported at various levels, central, regional and local. 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.

56. 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.³⁰ This process requires the progressive forging of a ‘social contract’ in favour of pro-poor growth between the different parts of society. The contract will be strengthened by political empowerment of the poor, the strengthening of decentralized, pluralistic, formal decision making, contestation and negotiation of policy change on the basis of evidence rather than political power and increased accountability of the state to the interests of the poor by involving them in monitoring outcomes.

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.

57. Effective poverty reduction strategies, be they national or development strategies or formal Poverty Reduction Strategy Papers (PRSPs), cannot be imposed from the outside. The need to overcome possible resistance to change means that they must 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.³¹ 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 were able to participate in, contribute to and benefit from growth.

58. 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 5). 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.

Box 5. Tools for analysing the linkages between growth, inequality and income poverty

Tools which may be used for this kind of analysis include the following³² :

- i) Disaggregating growth to identify macro-micro linkages (GDP growth in relation to household income growth) and to identify the relationship to the sources of growth in terms of sectors, regions and other spatial dimensions (e.g. urban-rural), increases in factor inputs (labour, capital) and their productivity.
- ii) Decomposing changes in poverty and inequality amongst different groups, identifying the contribution of growth in average incomes as opposed to the distribution of income and charting the growth of income across the income percentiles to better understand distributional impacts (i.e. “growth incidence curves” as illustrated in chapter 1) and calculating the average growth rate in the incomes of the poor.
- iii) Analysing outcomes in labour markets and modelling the economy to understand the growth and distributional effect of policy change

4.5 Key Issues for Political Empowerment

- Is the state functioning effectively, ensuring respect for the rule of law and effective governance over the activities of government, the private sector and civil society?
- Are poor women and men able, through those who represent their interests, to influence the policy making process? Is the process of policy making based on evidence, decentralized where appropriate and participatory so that it may be influenced by those who represent the interest of the poor? How can the voice of the poor be increased 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? Have the structures and processes through which policies are made and ways to influence them been recognised? Is it possible to identify and support change agents who can champion pro-poor change?
- Are poverty reduction strategies nationally owned? Do they have a sound understanding of the linkages between growth, inequality and poverty reduction? How can their preparation be used to strengthen the social contract in favour of pro-poor growth and the state held more accountable for delivering pro-poor outcomes?

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

59. 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.

60. 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, promoting evidence based, transparent decision making and innovation and lesson learning to arrive at policies suited to the local context.

61. 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 National Leadership

Donors should focus on supporting in-country processes for developing nationally-owned poverty reduction strategies and the reform of policy making processes

62. As set out in the Paris Declaration on Aid Effectiveness,³³ effective aid requires the mutual commitment that partner countries exercise leadership in developing and implementing national development strategies through broad based consultative processes and 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 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.

63. Donors may help in the preparation of nationally owned poverty reduction strategies by: i) building analytical capacity to help partner countries identify the binding constraints to pro-poor growth; ii) providing resources to undertake broad based dialogue and build capacity amongst those who represent the poor to engage in policy dialogue; iii) helping countries innovate to find context-specific solutions, informing policy choices by carrying out ex-ante poverty impact assessments; and iv) assisting the process

of ensuring accountability by building capacity to manage for development results amongst the state and those who represent the interests of the poor. They may help to ensure that poverty reduction strategies better integrate pro-poor growth with progress on other dimensions of poverty.

64. Donors may help to improve policy making processes generally by supporting formal, transparent processes of policy making (draft legislation, “white” and “green” papers) helping to ensure that consultation is broader and decisions more evidence based. They may also support specific, pro-poor policy reforms through: i) supporting the demand for pro-poor change from credible champions by helping them to provide evidence for change and articulate policy solutions that will minimise resistance to change; ii) supporting change agents to establish broad constituencies in support of pro-poor change; and iii) building capacity to provide an adequate supply response from the state.

5.3 The Basis of Engagement

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

65. 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, providing aid predictably. Short term assistance is unlikely to be productive, unless it complements and is well coordinated with more long term development interventions.

66. 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 the group of donors to the poverty reduction strategy should help to ensure effective donor support.. Each donor is likely to have core competency in particular areas addressed by the strategy and may therefore focus on supporting parts of the strategy that they have the greatest value added to contribute. But, by co-ordinating their responses, they will ensure that the broad agenda for pro-poor growth and poverty reduction may be addressed adequately.

67. 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. The main type of assistance required is likely to be technical, with financial assistance limited to piloting new approaches that can demonstrate the effectiveness of pro-poor policy change, including improved access to social services and infrastructure.. In low income countries with functioning states, budgetary support, with appropriate engagement over the implementation of poverty reduction strategies and pro-poor policy reform, may be appropriate.

68. 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, may well fail to address the binding constraint. Because of the unpredictable nature of policy change, earmarking aid well in advance of its use may not be helpful. It is better to provide programmatic aid that will allow flexibility in supporting specific initiatives, as and when they become appropriate. The programme should address the broad, strategic direction of policy and institutional change and identify the types of investment and assistance that may be needed, enabling 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 the private sector and civil society. When interacting with the private sector, assistance should preferably be provided through local change agents and facilitators, not directly to businesses, thereby avoiding the distortion of markets by attempting to pick winners.

5.4 Fragile and Failed States

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

69. 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.

70. However, the approach to these states will need to be different to that set out above. 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, improve policy making processes, develop capacities of those proposing policies that will promote pro-poor growth, build capabilities of organs of the state to exercise oversight over government and strengthen institutions. Resources can be directed to the development of human capabilities and the construction of basic infrastructure.³⁴

71. The programme of assistance will need to be accompanied by engagement with the state to strengthen in-country processes that will restore the legitimacy of the state and help it 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 and agriculture.

72. 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 6 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 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 the separate reports on these areas.³⁵

73. *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), the PSD agenda needs to focus on how policies combine to provide incentives that shape private sector activity to bring about pro-poor market outcomes. To help donors increase the leverage of private sector development on reducing poverty, POVNET prepared guidance on six important topics and prepared some guidance:

- 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.
- 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.

74. *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.

75. *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:

- Releasing its potential for pro-poor growth by 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 instruments), as well as coping strategies (e.g. food based safety nets);
- Supporting the development of country led national development strategies that include agriculture 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.

Box 6. Promoting pro-poor growth: Examples of evolving agendas and policy responses**Private Sector Development**

Evolving agendas		Policy responses
From ...	To ...	
Target firms and sectors directly	Promote enabling environments for pro-poor growth, focusing on market outcomes instead of firms	Strengthen the enabling environment, ensuring an improved risk to reward ratio.
Informal sector is marginal and temporary	Informal sector is large, informality is a continuum	Reduce disincentives to formality, facilitate risk taking. Direct firm level support to be the exception
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 more holistic and integrated agenda for pro-poor growth	Link/merge PSD in wider pro-poor growth strategy focusing on both pace and pattern of growth

Agriculture

Evolving agendas		Policy responses
From ...	To ...	
Sectoral approach/production units	Rural livelihoods approach	Holistic approaches - build assets and foster diversified livelihoods
One work location	Multiple work locations	Promote diversified livelihoods and rural-urban migration
Focus on food crops	Diverse income streams	Expand/diversify markets Strengthen competitiveness of small-scale producers
Government support and social safety nets	Reduce risk and vulnerability	Assess trade-offs between growth promoting and risk and vulnerability reducing measures; develop new forms of insurance

Infrastructure

Evolving agendas		Policy responses
From ...	To ...	
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 develop capacities in field and home offices to promote pro-poor growth effectively.

76. 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 adopted in all countries.

77. 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.³⁶ Field staff may require greater delegation of authority to engage effectively, be empowered to take the risks involved in supporting policy change, and not penalized 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.

78. 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 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 enable staff to better integrate economic, social and political development perspectives, needs and opportunities.

79. 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

- Is donor assistance aligned to nationally owned poverty reduction strategies? How can donors support the development of nationally owned strategies that address pro-poor growth and poverty reduction effectively and ensure that the process of their preparation and implementation helps to strengthen the social contract in favour of pro-poor growth?
- Is donor assistance long term and suited to the country situation? Is aid 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?

- Does donor policy include staying engaged in fragile or failed states? Has a different approach been developed to engage with such states?
- Have the agendas for important areas that impact pro-poor growth been reassessed in the light of the pro-poor growth agenda?
- Do field and home office staff have the capabilities required to promote pro-poor growth? Are field staff empowered to engage with partner countries and take the risks inherent in promoting pro-poor policy change? Are staff working in multi-disciplinary teams?

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