

## Improving ODA allocation for a post-2015 world

Policy brief: targeting aid to benefit the poorest 20% of people in developing countries

**Official development assistance (ODA) accounts for just 7% of total international resource flows to developing countries. Yet, within an ambitious post-2015 development agenda, ODA will play as vital a role as ever. It is essential to improve allocation of ODA to where it can have most impact in driving poverty reduction and leaving no-one behind.**

- **ODA is the main international public resource that can be explicitly dedicated to poverty reduction.**
- **The purpose of ODA should be refined to explicitly focus on poverty reduction and leaving no-one behind.**
  - The study shows that **development agencies with a clear mandate for poverty reduction target poorer countries most effectively.**
  - Within a post-2015 framework, **ending poverty and leaving no-one behind requires investments across the three dimensions of sustainable development** (social, environmental and economic) that benefit the poorest people
- The most effective way to focus ODA allocation post-2015 is to refine the objective of ODA to **'benefit the poorest 20% of people in developing countries'**, from its current, broader objective, 'promotion of economic development and welfare'.
- **There is need to move beyond income-group-based ODA allocation** that only consider narrow economic averages and ignore wider aspects of sustainable development. ODA allocation should **move beyond country eligibility criteria to focus on people.**
- ODA to developing countries should target **appropriate assistance to the poorest 20% of people:**
  - Effective ODA should not draw resources away from the poorest countries.
  - The design of ODA instruments should be tailored according to wider resources present and prioritise investments where other resources are scarce.
  - ODA should address the vulnerabilities people face: ending poverty requires supporting states affected by conflict and fragility transition to stability and increasing the resilience of the most vulnerable against climate and other shocks.
  - The nature of assistance should vary in different contexts; effective ODA does not always require large financial transfers.
- The refined objective of ODA should be **formalized at the global level and institutionalised across international development cooperation** by the agencies and institutions that provide and implement ODA.
- **Decision making can only be as good as the information on which it is based:** there is a need for much better, sub-nationally disaggregated data on poverty and resources.

This policy brief presents recommendations from the study *Improving ODA allocation for a post-2015 world*, on how changes from the Millennium Development Goals (MDGs) to the emerging post-2015 development agenda should affect ODA allocation.

## Now is the time to ask what role ODA should play in a post-2015 world

The emerging post-2015 development agenda reflects a number of paradigm shifts that should reshape the role of ODA. The post-2015 development agenda is broader in the outcomes it seeks across the three dimensions of sustainable development – social, environmental and economic – as well as the contributions it seeks to mobilise from all actors, public and private, national and international.

Re-examining the role of ODA, and ensuring its use where it is needed most, is essential for an effective post-2015 development agenda. As discussions about the agenda and its implementation gather speed in the run-up to the Third International Conference on Financing for Development, now is the time to ask how to use ODA most effectively for the next 15 years and beyond.

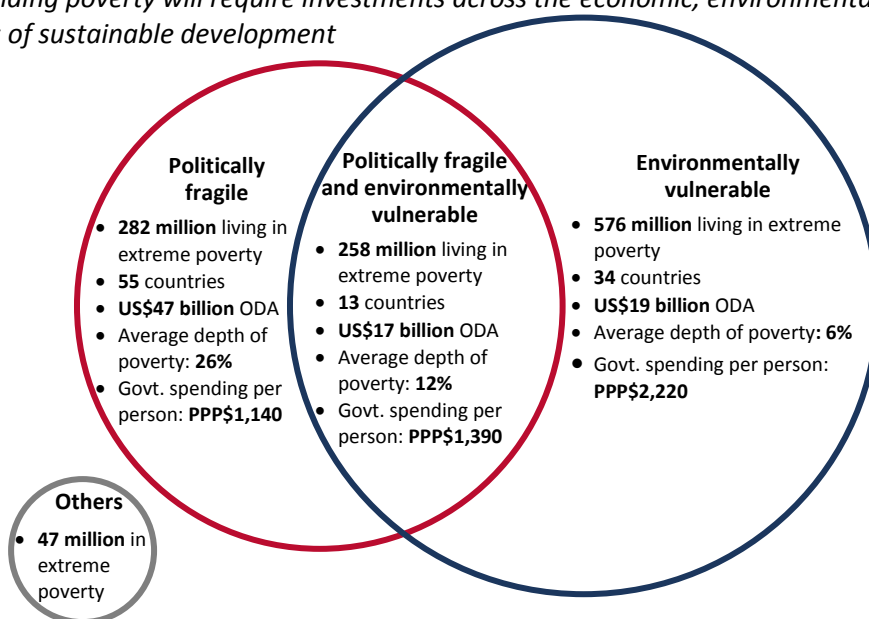
### ODA's comparative advantage is to focus on ending poverty and leaving no-one behind

While it is small in volume when compared to other resources, ODA has a comparative advantage in focusing on ending poverty; it can be targeted to benefit the poorest people in a way other resources cannot. ODA can reach people and countries neglected by other resources, and the wide variety of instruments that constitute ODA allow it to adapt to the context, whether leveraging new finance or delivering basic services.

Commercial resources, on the other hand, are bound by the need to seek profit, and flow mostly to more economically developed countries. And while domestic resources are primary for post-2015 implementation, governments need to serve all citizens and have many demands on their resources. The study demonstrates that the current and likely future scale of domestic resources in many developing countries is insufficient to achieve poverty eradication by 2030.

Ending poverty will require dedicated resources that can make and mobilise necessary investments across the economic, environmental and social dimensions of sustainable development that benefit the poorest people. Economic growth alone will not be sufficient. 17% of people in developing countries still live in extreme poverty, on less than \$1.25 a day. Some 96% of these people live in countries that are either politically fragile, environmentally vulnerable, or both (Figure 1).

Figure 1: Ending poverty will require investments across the economic, environmental and social dimensions of sustainable development



Source: *Improving ODA allocation for a post-2015 world, chapter 4. The size of each circle is scaled by the number of people living in extreme poverty.*

## ODA allocations could more effectively target the poorest people

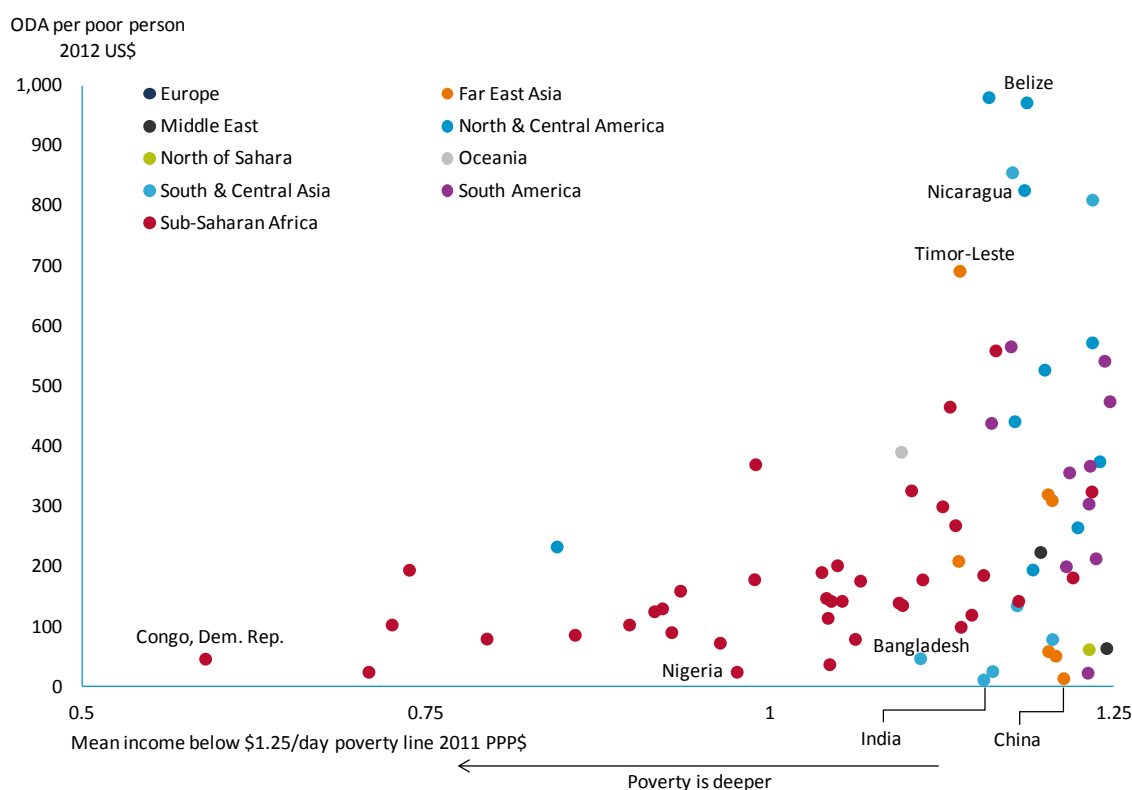
### Current ODA allocations do not respond effectively to the characteristics of poverty

While ODA allocations focus more on poorer countries than other resources, allocations do not always respond effectively to the characteristics of poverty.

The study finds that more ODA is allocated per poor person to countries where there are fewer people living in poverty. In 20 countries, which collectively account for over three-quarters of people in extreme poverty, ODA is less than US\$100 per poor person each year (27 US cents per day). Yet, ODA exceeds US\$1,000 per poor person in 33 countries that account for less than 1% of the world's poor.

ODA allocations are also greater to countries where the depth of poverty is lower (where people live further below the poverty line; Figure 2). ODA exceeds US\$500 per poor person in 44 countries – in all of these countries, the depth of poverty is less than 10%.<sup>i</sup> Yet ODA is just US\$64 per poor person (18 US cents per day) in 16 countries where the depth of poverty is more than 20%. In addition, ODA allocations do not respond effectively to all aspects of poverty (non-income dimensions). For example, the study finds that ODA allocations do not prioritise health investments in countries where health deprivation is a greater contributing factor to overall multidimensional poverty.

Figure 2: ODA per poor person is higher where the depth of poverty is lower



Source: *Improving ODA allocation for a post-2015 world, chapter 2.*

### ODA allocations do not respond effectively to wider resources

Domestic public finance is rightly at the centre of financing for development and this will continue post-2015. ODA should work within a framework of domestically led implementation. Yet, ODA per poor person is lower in countries with fewer domestic resources. In these countries, ODA is one of the main international resources and the depth of poverty is high, presenting an opportunity for ODA to be more poverty focused. Currently, ODA that supports domestic resource mobilisation accounts for only a small proportion of allocations, at less than 0.1% of total ODA.

The private sector is an important actor in holistic development, though the role of ODA in working with private sector resources is controversial. Current core private sector ODA allocations do not

focus on the poorest countries or the sectors most relevant to poverty reduction. Current core ODA support for the private sector is small, at around 2.7% of ODA, and, in just one example, small- and medium-sized enterprise development accounts for just 3% of that total.

### **ODA allocations do not respond effectively to the vulnerabilities of the poorest people**

Many of the world's poorest people are disproportionately affected by fragility or vulnerability to climate or other shocks. States affected by conflict or fragility account for an increasing proportion of people living in extreme poverty – from 20% in 1990 to around 50% now. Yet, while such states are some of the largest ODA recipients, other such states are not prioritised in ODA allocation. Fluctuating ODA allocations do not meet the need for sustained long-term financing that can address the numerous, overlapping and complex challenges facing states affected by conflict and fragility.

### **Ineffective targeting reflects the lack of incentives within current ODA architecture**

The current objective of ODA<sup>ii</sup> – promoting economic development and welfare – is broad. It does not distinguish investments that increase headline economic growth with little demonstrable impact on the poorest, on the one hand, from investments that actually reduce extreme poverty, on the other. The study shows the result: while ODA allocations are, overall, more poverty-focused than other resources, they do not respond effectively to the characteristics of poverty, the wider resources available to developing countries or the vulnerabilities that the poorest people face.

### **ODA allocation based on income-groups will not support sustainable development**

The World Bank's income-group system has been a key determinant of many donors' ODA allocation decisions, and it is often used in practice as a way to evaluate countries' developmental progress as a whole. Yet income groups present an extremely narrow view of progress and one that is in increasingly sharp contrast with the modern definition of sustainable development in its three dimensions (social, environmental and economic) and with the emphasis on leaving no-one behind. Income groups are defined entirely by average GNI per person in each country, ignoring both the environmental and social dimensions of development and the extent to which economic progress is shared evenly within a country. Effective decision making on ODA investments within the post-2015 framework cannot be achieved by using income groups alone as a basis for guiding allocation.

## **A specific focus on poverty will drive effective allocations**

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### **A clear and focused objective will improve targeting**

The evidence is clear: development cooperation agencies with a clearer and more formal mandate to reduce poverty are more effective at targeting ODA allocations to the poorest. Agencies with a legal mandate to reduce poverty allocate over 80% of ODA to countries with above-average poverty rates; agencies that do not make poverty reduction an explicit objective allocate 31% (Figure 3).<sup>iii</sup>

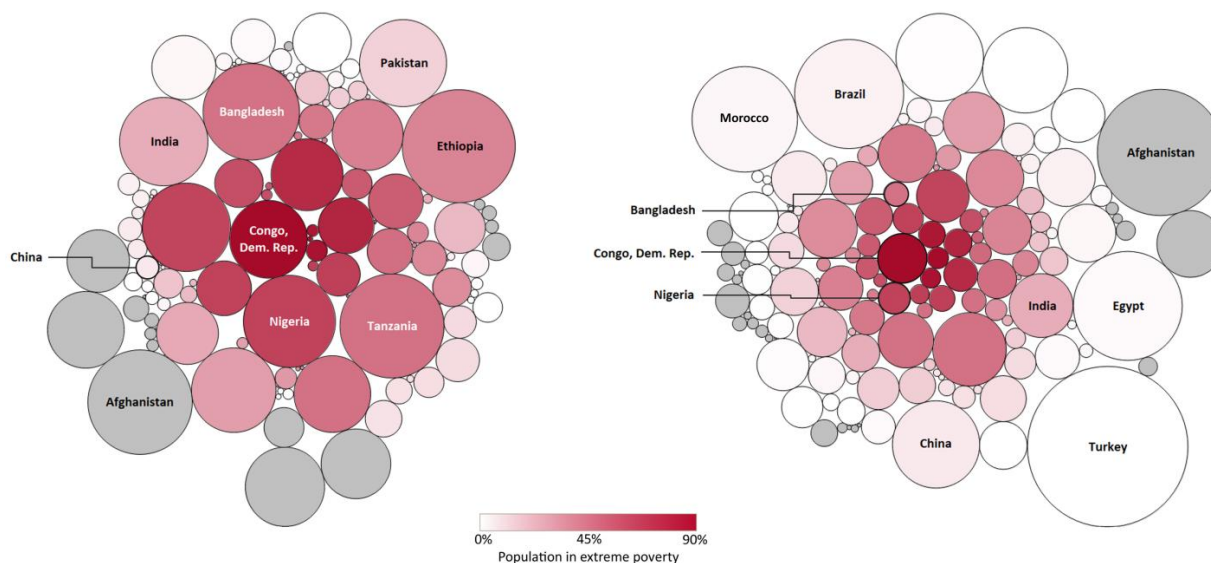
This shows the importance of establishing a clear purpose for providing ODA within the post-2015 development agenda. It shows the transformative impact that formalising a 'poverty focus' that addresses economic, social and environmental vulnerabilities of people living in extreme poverty could have on ODA allocations overall.

Figure 3. A clear objective is the foundation for effective targeting of ODA

(i) Agencies with a legal mandate for poverty reduction

(ii) Agencies that do not specify poverty reduction as an objective

Source: *Improving ODA allocation for a post-2015 world, chapter 2.*



## To drive poverty reduction and leaving no-one behind, ODA should explicitly target the poorest 20% of people in developing countries

### Targeting benefit for the poorest people, not economic development and welfare

The study proposes refining the objective of ODA to ‘**benefit the poorest 20% of people in developing countries**’. This would establish a clear purpose for ODA over the post-2015 timeframe and beyond, ensuring that allocations underpin the goal of ending \$1.25-a-day poverty by 2030 and the transition to sustainable development, as well as longer term objectives to end poverty in all its forms and leave no-one behind.

The refined objective would replace the current objective of ODA for the ‘promotion of economic development and welfare’. It would mean explicitly targeting benefit for the poorest people in developing countries, rather than targeting eligible countries: current country-eligibility criteria do little to incentivise allocations that benefit the poorest people within eligible countries.

Refining the objective would form the basis of a targeting discipline that incentivises the provision of appropriate support across the dimensions of sustainable development. This targeting discipline will incentivise the allocation of ODA in a way that considers: the scale, nature and causes of poverty and the inextricable link of poverty eradication to sustainable development; the vulnerabilities and risks that the poorest face; the access that the poorest have to public services and economic opportunities; and the resources and capacity of domestic institutions in developing countries.

The study calls for the refined objective of ending poverty and the explicit focus on benefiting the poorest 20% of people in developing countries to be formalised at the international level, as part of the post-2015 discussions, and institutionalised by the agencies and institutions that provide ODA.

### Who are the poorest 20%?

The poorest 20% are the people living in or most vulnerable to extreme poverty; latest estimates are that 17% of the population of developing countries live in extreme poverty, on less than \$1.25 a day. The poorest 20% of people are those who have least access to wider resources, public services or the benefits of economic development – whether in least developed countries or rapidly growing emerging economies. They are often those most marginalised in society and those who benefit least from national growth and development. They are, too often, left behind.

## **Benefiting the poorest 20%: Investing across the dimensions of sustainable development**

Explicitly targeting ODA in developing countries to benefit the poorest 20% of people can incentivise allocations that make and mobilise the investments across the social, environmental and economic dimensions needed to end poverty. Focusing on benefit for the poorest 20% of people will help overcome the false dichotomy between poverty eradication and sustainable development. It does not mean reducing ODA allocation outside core social sectors – for instance, in economic sectors, governance, environmental sustainability or global public goods. Rather, it should enhance the effectiveness of ODA in these areas by incentivising demonstrable impact on the poorest people.

## **Benefiting the poorest 20%: Assistance tailored to the context**

ODA is a mix of varying instruments – and effective ODA allocation should not mean drawing resources away from the poorest countries. ODA should provide appropriate assistance to the poorest 20% of people, whether in a Least Developed Country with low domestic resources or a rapidly growing emerging economy. However, the type of ODA should vary by context. Effective ODA does not always require large financial transfers.

While focusing on the poorest 20% of people in developing countries, ODA must support country led implementation and national development goals and strategies. Support for domestic resource mobilisation will become increasingly important where domestic resources are growing slowly. Where resources are growing more rapidly, ODA can still play an important role, for example, in supporting the development of human and technical capacity to expand basic services, connecting small business to economic growth, or strengthening systems to spend resources effectively.

## **Benefiting the poorest 20%: Addressing the vulnerabilities people face**

Explicitly targeting the poorest 20% of people in developing countries will focus ODA towards investments that reduce vulnerability and safeguard progress towards ending poverty. For example, it is the strength of resilience mechanisms and coping strategies that determine the lasting severity of climate shocks: focusing on the poorest 20% of people will incentivise assistance that builds coping mechanisms for the most vulnerable people that are essential for realizing and safeguarding poverty reduction. In countries affected by conflict and fragility, such a focus can incentivise the long-term, systematic approach and sustained financing that helps countries move out of instability.

## **Better disaggregated data will inform better decision making**

Effective decisions about how to allocate resources require accurate, timely, disaggregated data on the scale of needs and the resources available in different contexts. Yet, current data on both poverty and resources are often patchy, inaccessible, out of date, or of insufficient quality to answer even basic questions about the needs or scale and characteristics of resources. There is need to improve the timeliness, consistency and accuracy of existing data, and to invest in disaggregated data systems, so that we better understand needs and resources below the national level.

*This policy brief is based on a study (Improving ODA allocation for a post-2015 world). This independent study was commissioned by UNDESA for the 2016 Development Cooperation Forum, as part of a UNDESA research project funded by UKAID on development cooperation in a post-2015 setting. The views presented do not necessarily represent those of the United Nations or the Government of the United Kingdom. The study aims to generate ideas for the post-2015 discussions, particularly in advance of the Third International Conference on Financing for Development (FFD3) and the 2016 Development Cooperation Forum. Earlier versions were presented at the 30 October 2014 Joint Meeting of the General Assembly 2nd Committee and ECOSOC on “A renewed global partnership for development and successor arrangements to MDG-8” and the FFD3 First Round of Substantive Informal Sessions (New York, 10 – 13 November 2014).*

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<sup>i</sup> I.e. people living in extreme poverty are on average less than 10% below the \$1.25-a-day poverty line.

<sup>ii</sup> “Is it ODA?” Factsheet, OECD-DAC 2008 <http://www.oecd.org/investment/stats/34086975.pdf>

<sup>iii</sup> Based on analysis of ODA allocations against a review of the mandates and mission statements of 63 agencies that accounted for 90% of ODA disbursements in 2012. See chapter 2 of the study.