Financing Poverty Eradication

Anis Chowdhury
Australian National University
University of New South Wales Australia

Outline

- Conceptual issues
- External financing
- Domestic resource mobilisation
- Counter cyclical policies – debt, inflation, growth & poverty

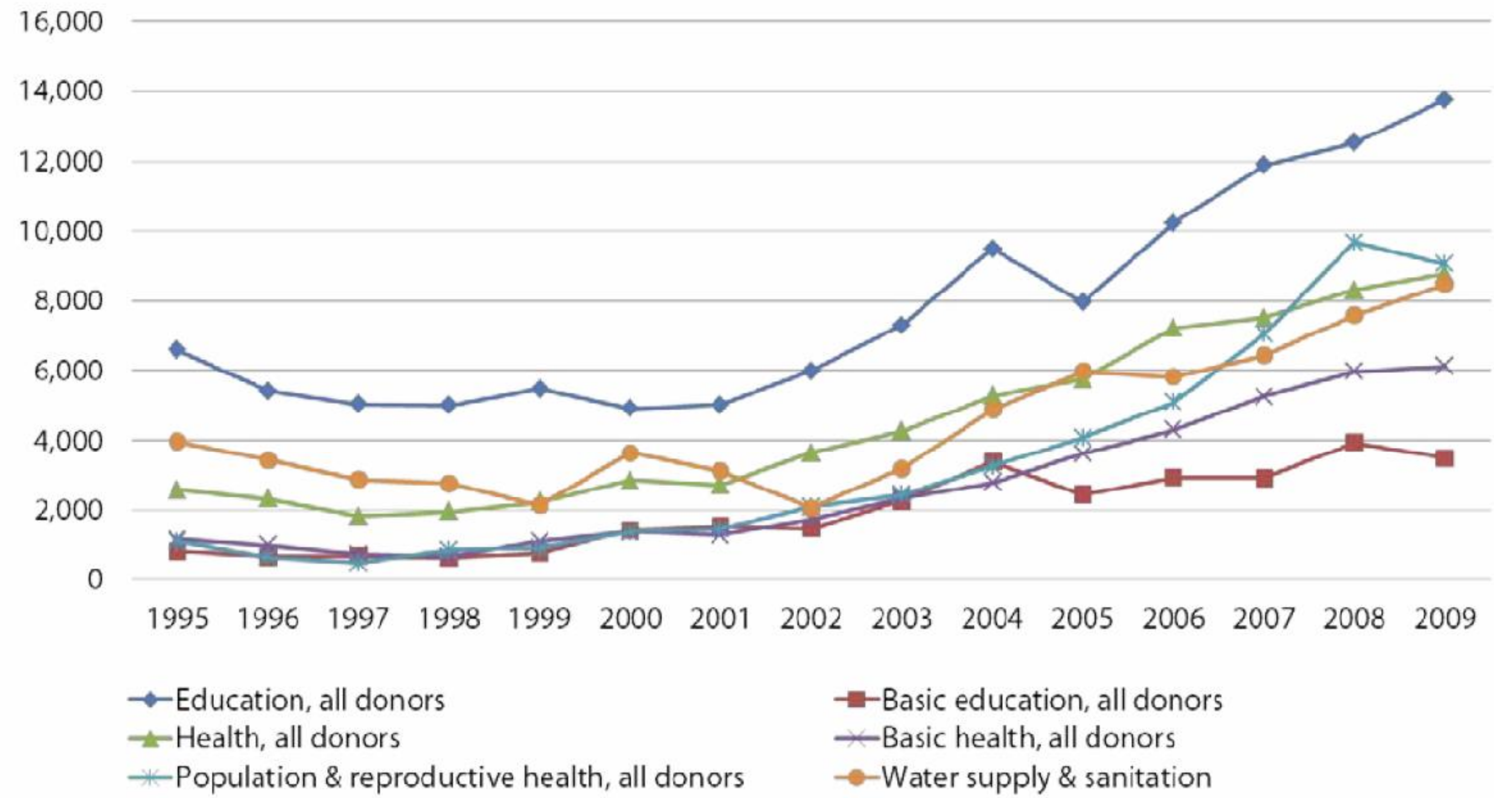
Conceptual issues

- Growth
- Poverty reduction
- Poverty eradication
- Vulnerability
- Multi-dimensional poverty

From decades of development to decades of poverty eradication

- 1960s-1970s: UN's 1st & 2nd Decades of Development
  - growth focused; largely achieved, but disappointing poverty results
  - ILO's basic needs approach, quality of life
- 1980s-1990s: UN's 3rd & 4th Decades of Development
  - Structural change; but derailed by debt crisis
  - SAP– back to growth focus; but disappointing
  - UNICEF's adjustment with human face
  - UNDP's Human Development Report
  - Social Summit (1995)
- 2000s: MDGs & Agenda 2030
  - Poverty reduction
  - Multi-dimensional poverty
  - Poverty eradication

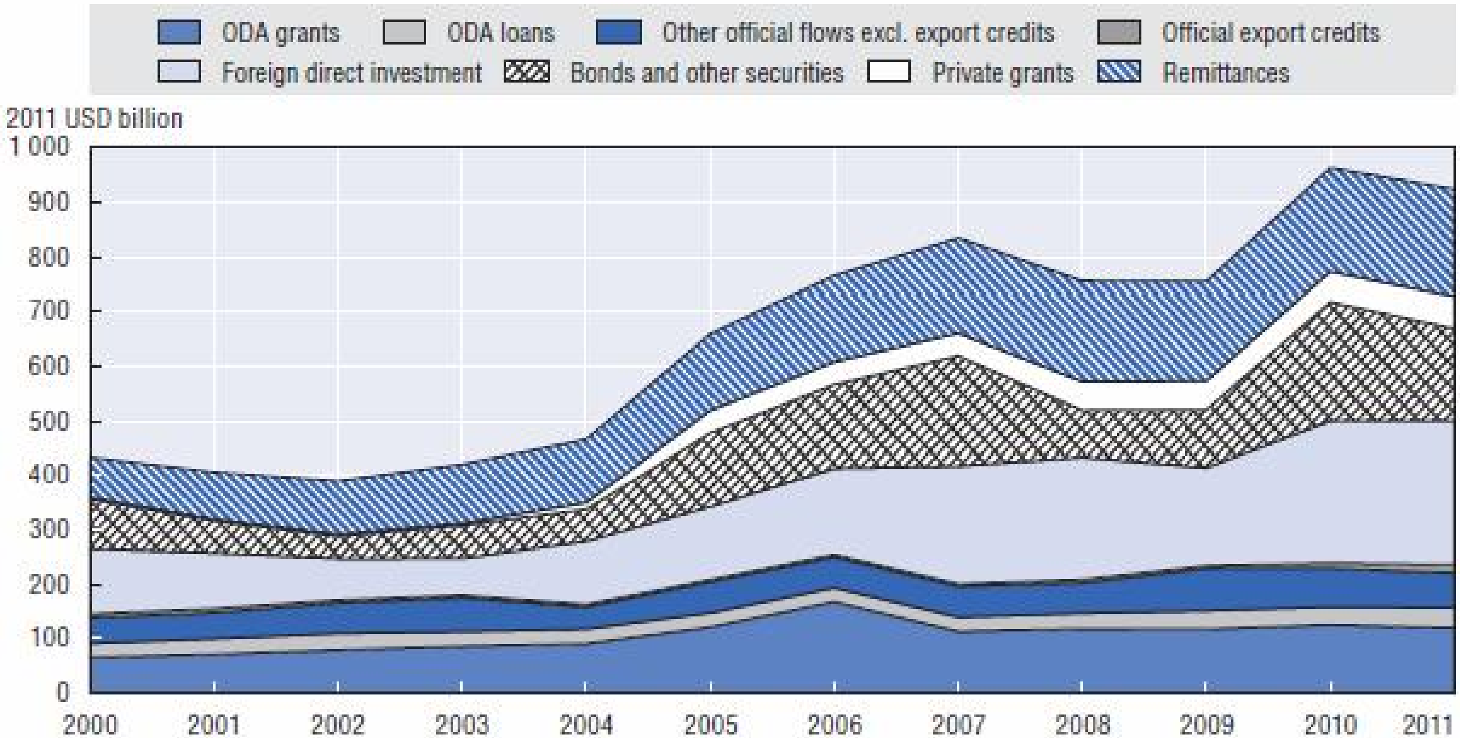
More ODA to social sectors



Source: *OECD-DAC 2010*

ODA more focused on social sectors since the adoption of MDGs

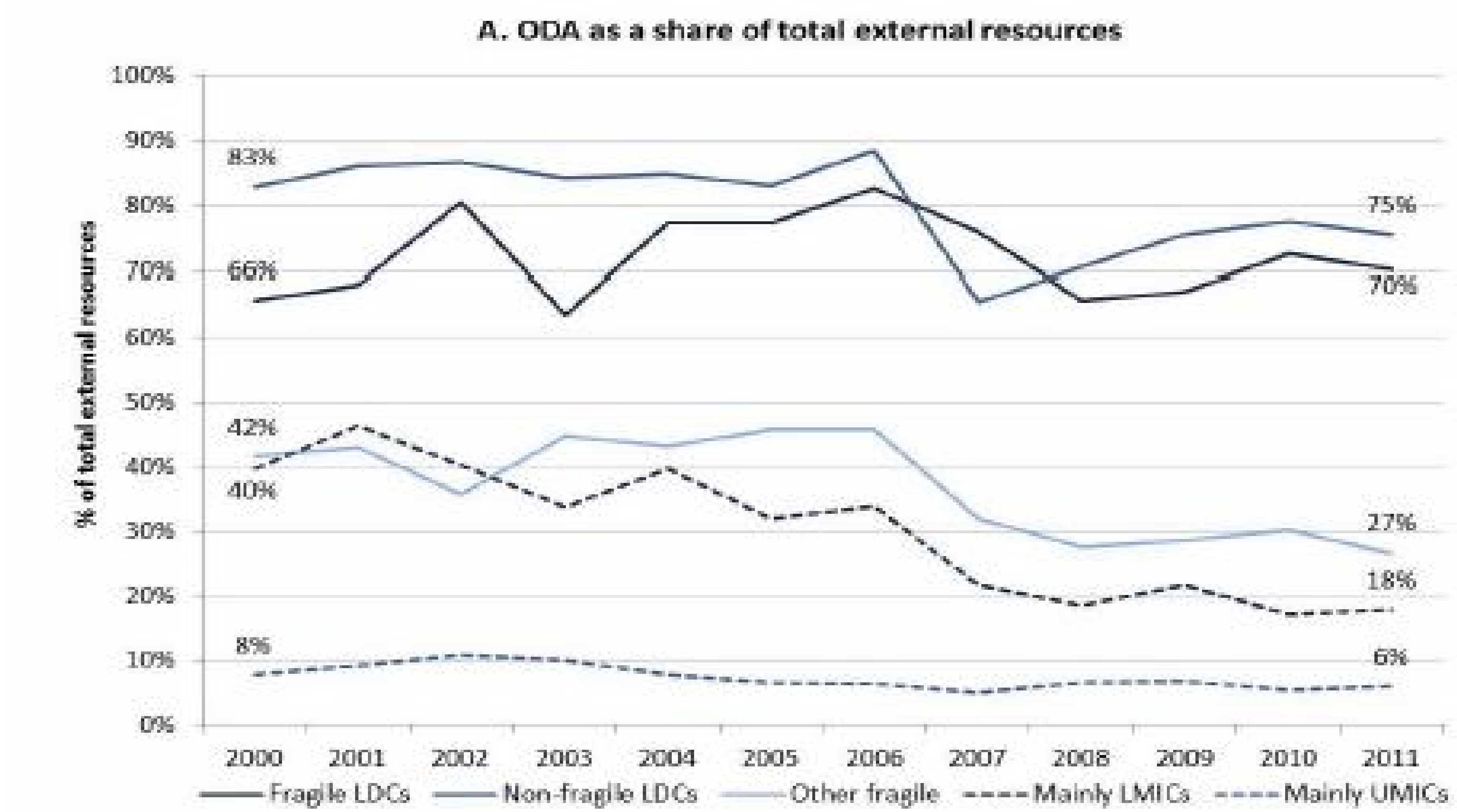
External financing



Notes: Total external financial resources include bilateral ODA, other official flows (OOF), private grants, private flows at market terms and remittances from DAC countries, and concessional and non-concessional outflows from multilateral agencies. From 2005 onwards, private grants are based on estimates from the Hudson Institute's Centre for Global Prosperity, which uses a more generous definition than DAC statistics, including, for example, the imputed value of volunteer time.

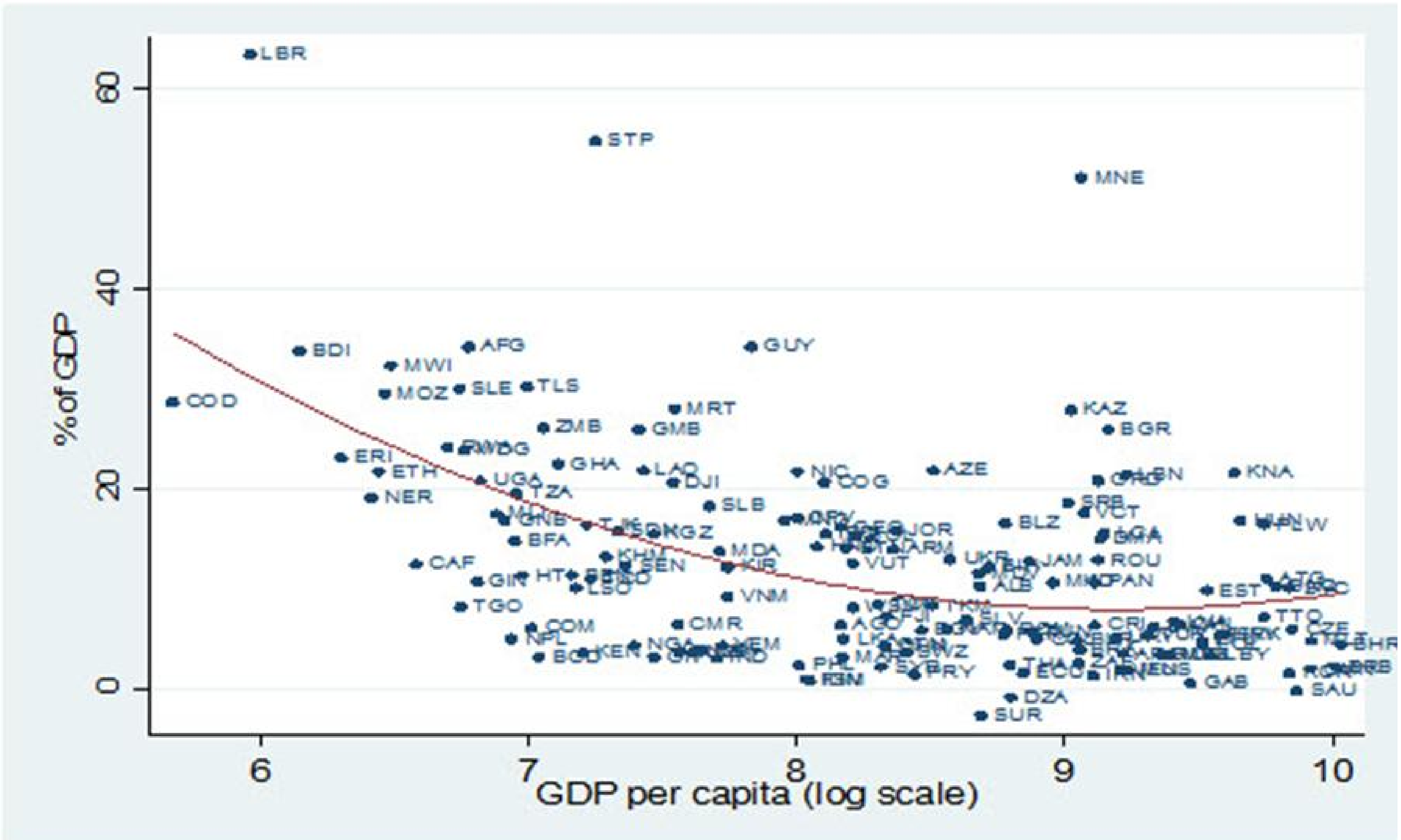
Began to rise only since the mid-2000s; driven by FDI, remittances and borrowing; ODA remained flat at around $150 billion (in 2011 price) a year since peaking close to $180 billion in 2006.

ODA volatile; but remains important for LDCs



ODA's share is declining and insignificant in Middle-income countries where global poverty is concentrated.

ODA & per capita income



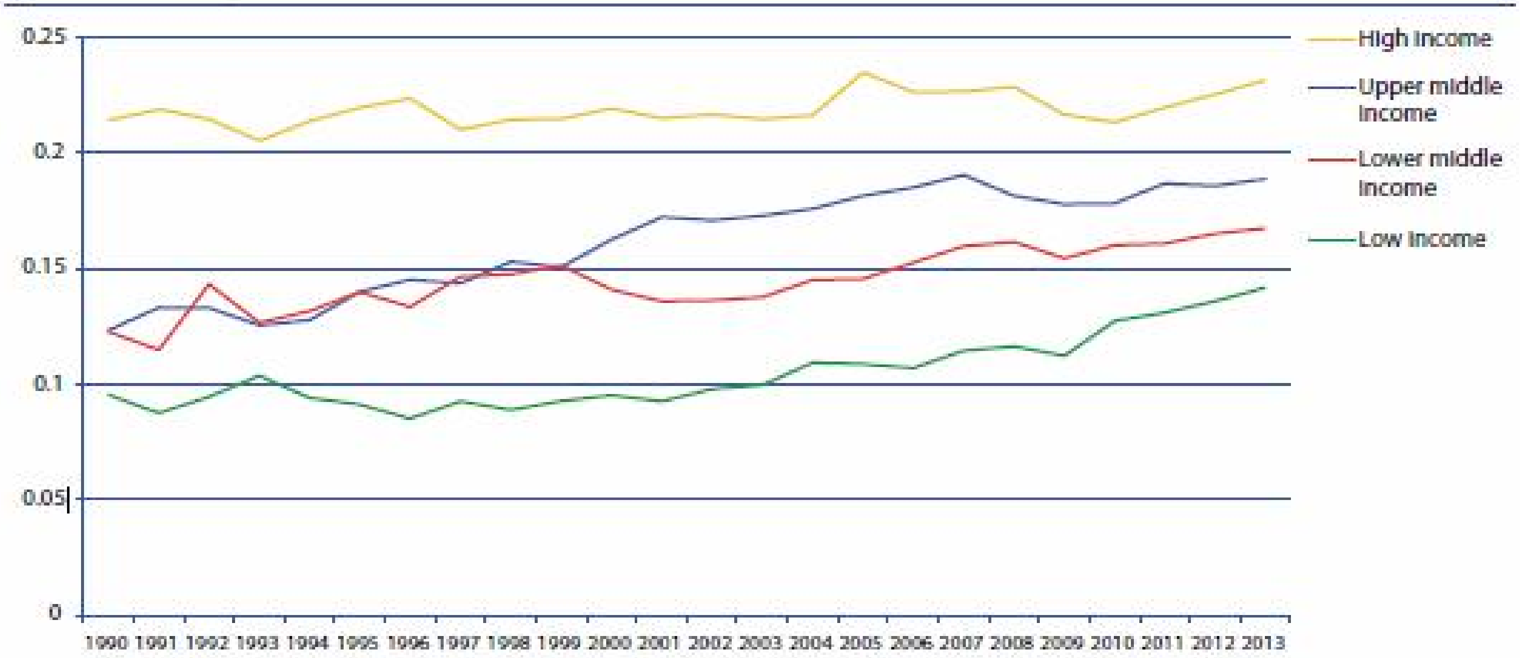
Considerable external financing > 20% of GDP for low-income countries
But that financial flow taper off as countries’ per capita income levels start to rise.

Aid effectiveness

- Reduce volatility – enhance predictability
- Remove conditionality; tied aid; budget support
- Stop aid diversion – refugee settlement, climate finance additionality
- Cautious about blended finance
- Aid does not necessarily cause real exchange rate appreciation or Dutch disease

Domestic resource rising

Median tax/GDP ratio (%) by income grouping, 1990–2013



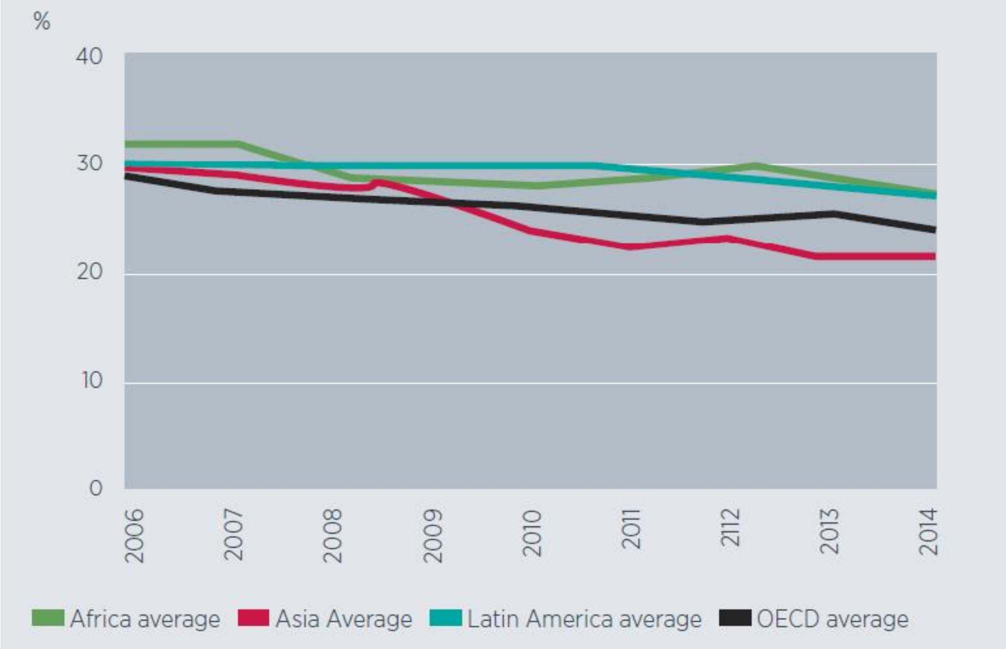
Source: United Nations Department of Economic and Social Affairs calculations, based on International Monetary Fund World Revenue Longitudinal Data (WoRLD), 13 July 2015. Note: Tax revenue as a percent of GDP, country classification according to World Bank Group country income groups 2015.

Most developing countries improved their domestic resource mobilisation; but still need to do more

Domestic resource mobilisation

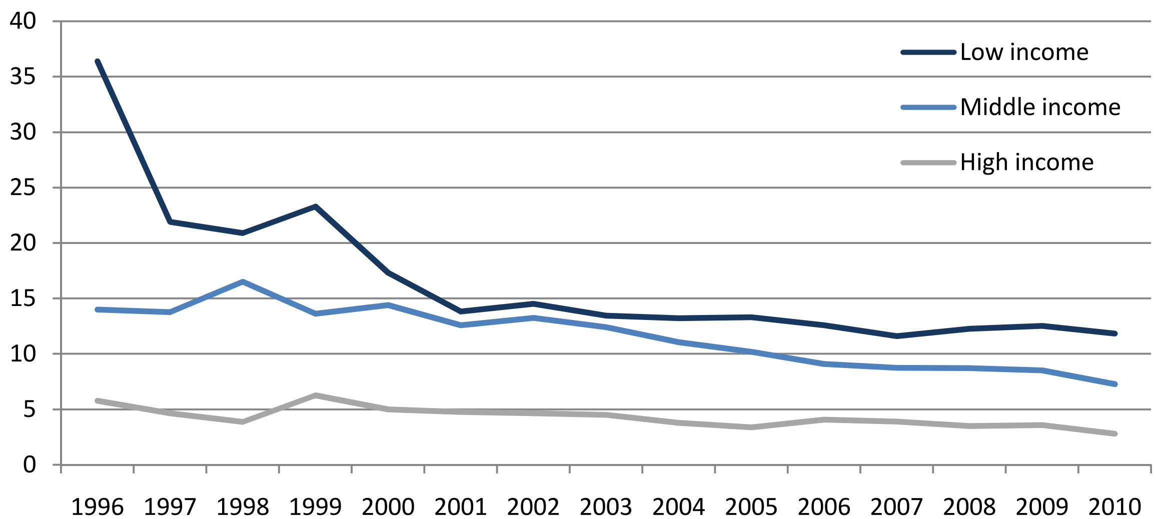
- Reverse the tendency to cut personal & corporate income tax
  - 34 of the 149 countries with data lowered the tax rates for the highest income earners in 2014, compared to the 2010-13 period.

Corporate profit tax rates (% of GDP)



Domestic resource

- Stop tax competition
  - Tax concession is not a main determinant of FDI (OECD)
  - The revenue loss from tax concessions to foreign investors is more than the benefits. Forgone tax revenues ranged between 9½ and 16% of GDP per year, whereas total foreign direct investment did not appear to depend on concessions (IMF).
- Reconsider trade tax



Revenue losses from trade liberalisation NOT compensated by other indirect taxes, especiall y VAT

Domestic resource

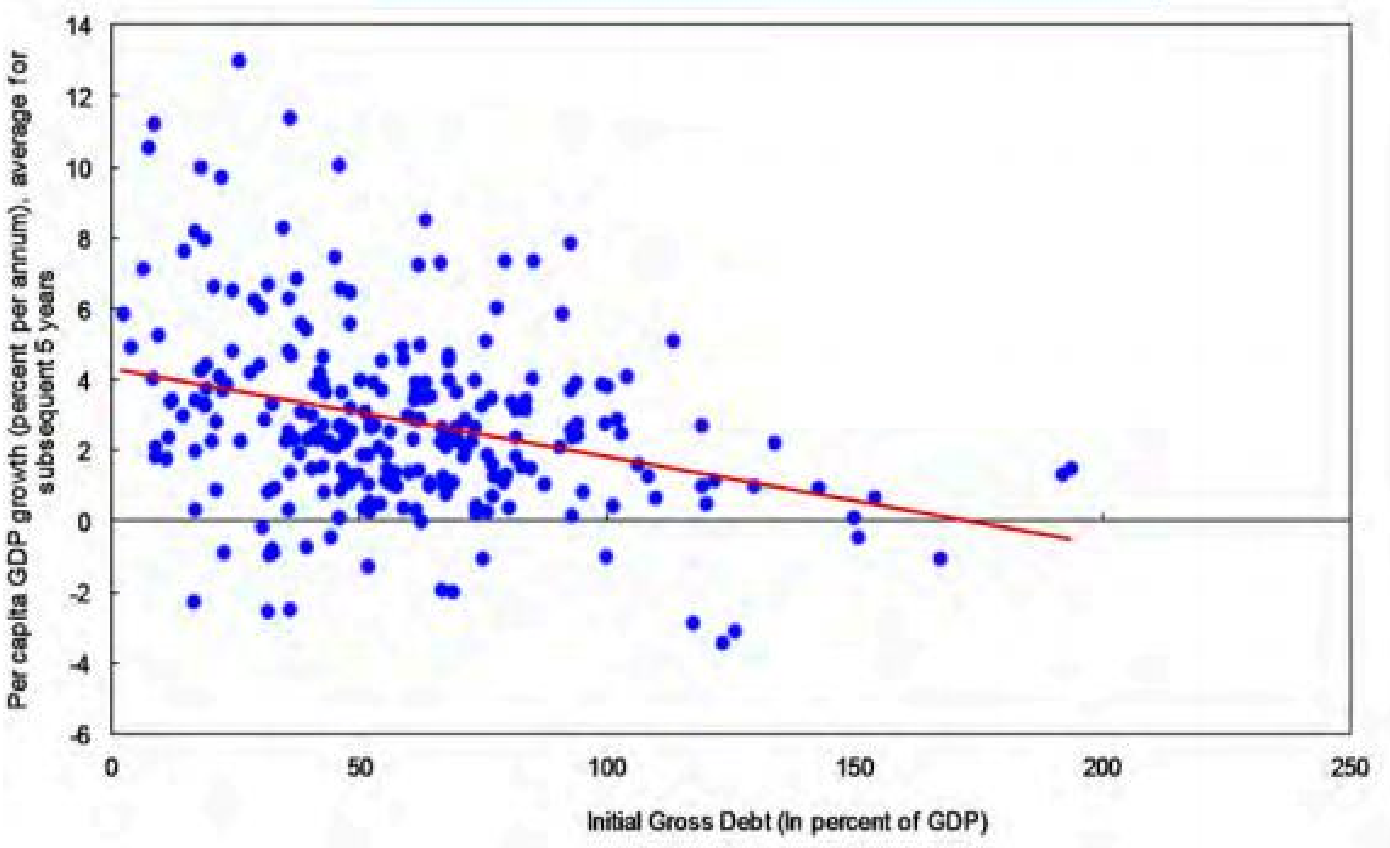
- VAT – limited in scope… greater efforts needed in taxing elites and high-income/wealth individuals (IMF); given its regressive nature VAT should be on luxury goods (ILO)
- Excise taxes have a buoyant base and can be administered at low cost - currently amount to < 2% of GDP in low-income countries
- New taxes – e.g. environmental tax; “sin” tax; financial transactions tax; resource rent
- Efficiency and profitability of SOEs
- Strengthened tax administration

Illicit transfer of funds

- Transfer pricing
- Tax evasion and avoidance
  - developing and emerging market economies lost US$7.8 trillion in illicit financial flows from 2004 through 2013, with illicit outflows increasing at an average of 6.5% per year—nearly twice as fast as global GDP
- International & regional tax cooperation

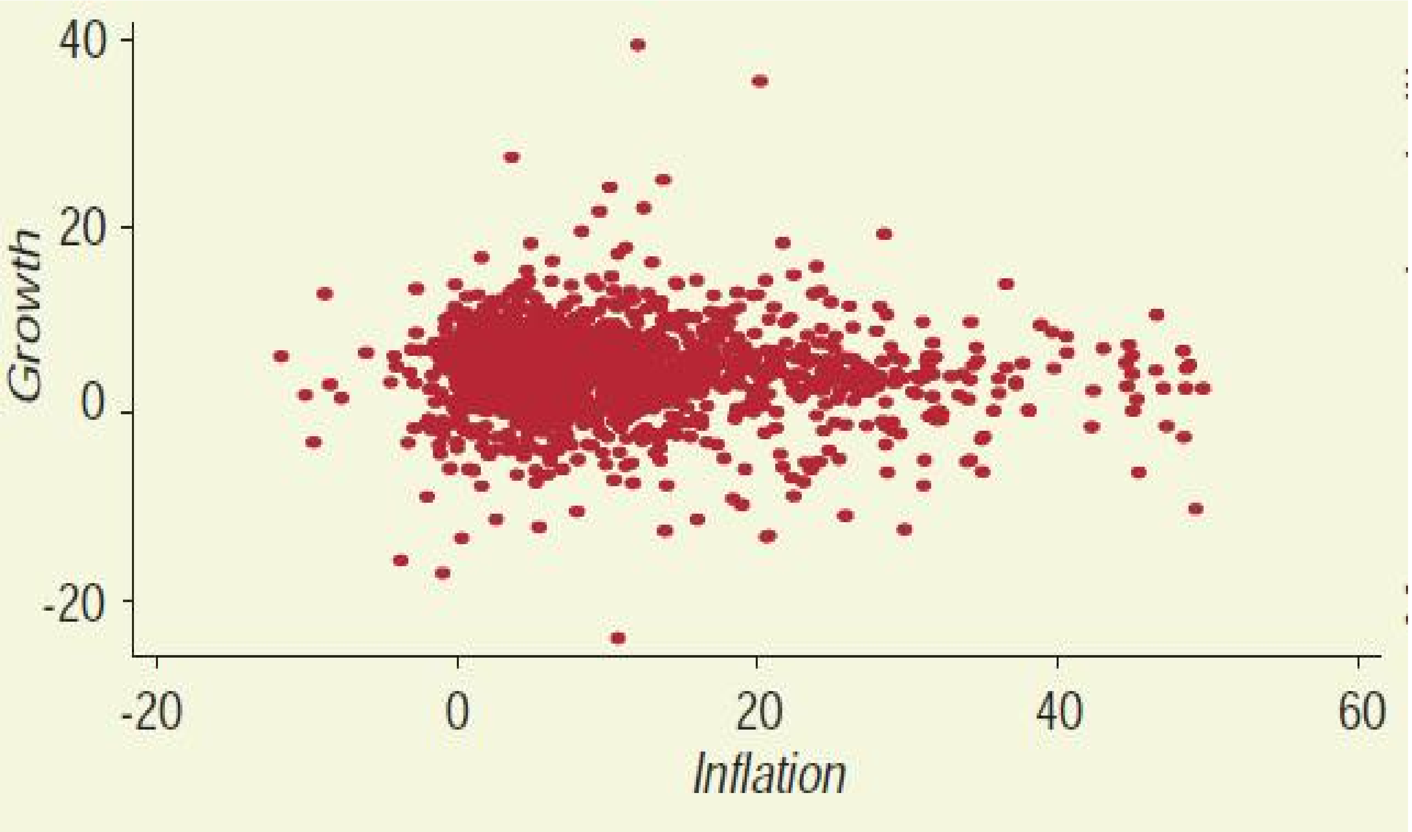
Counter cyclical policy space

- Debt financing – does not necessarily retard growth; but should be mindful of external debt



Counter cyclical policy space

- Moderate inflation does not retard growth; should consider causes of inflation



Moderate inflation does not harm poor!!!

Figure 5a: The Income of the Poor and Avereage Inflation

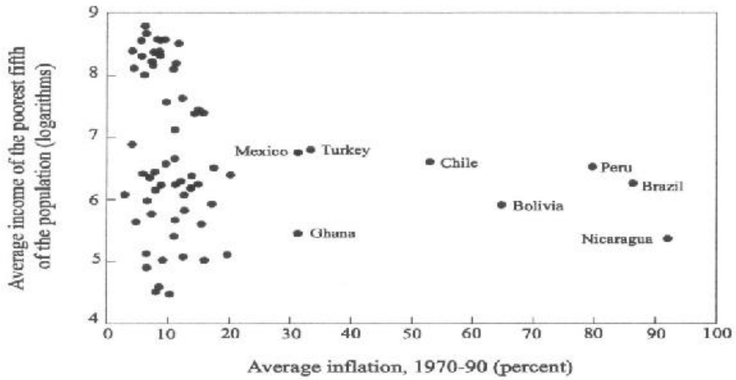
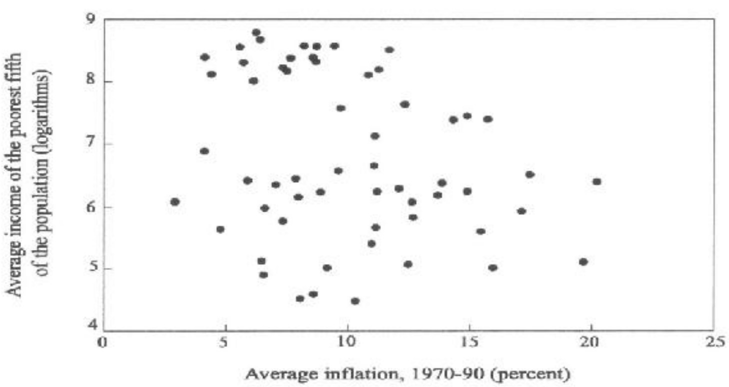


Figure 5b: The Income of the Poor and Average Inflation Excluding Outliers



Source: Romer & Romer (1998) based on Deininger and Squire (1996), Summers and Heston (1991) & World Bank's World Data CD-ROM (1995 edition)

- Hyper inflation is found only in countries where social & political order breaks down
- Inflation does not generally accelerate even when it is in the range of 15-20%
- Inflation reduces real wage; but lower real wages lead to higher employment

Fiscal consolidation???

- "…lowers incomes in the short term, with wage-earners taking more of a hit than others; raises unemployment, particularly long-term unemployment..." (IMF)
- Need to ease budget constraints and allow for an increasing degree of deficit spending, especially to support social investments (IMF)
- helps quick recovery, minimises social impacts of economic shocks, especially poverty.
- At the same time, growth repairs the budget as tax revenues rise and social protection expenditures (e.g. unemployment benefits) decline

Concluding remark

- Fiscal space is crucial
- Depends on dependable export earnings, tax revenues, aid & debt relief – they require international / regional cooperation
- Debt & inflationary financing should not be ruled out
- Counter cyclical policy measures and social protection are essential to reduce vulnerability