



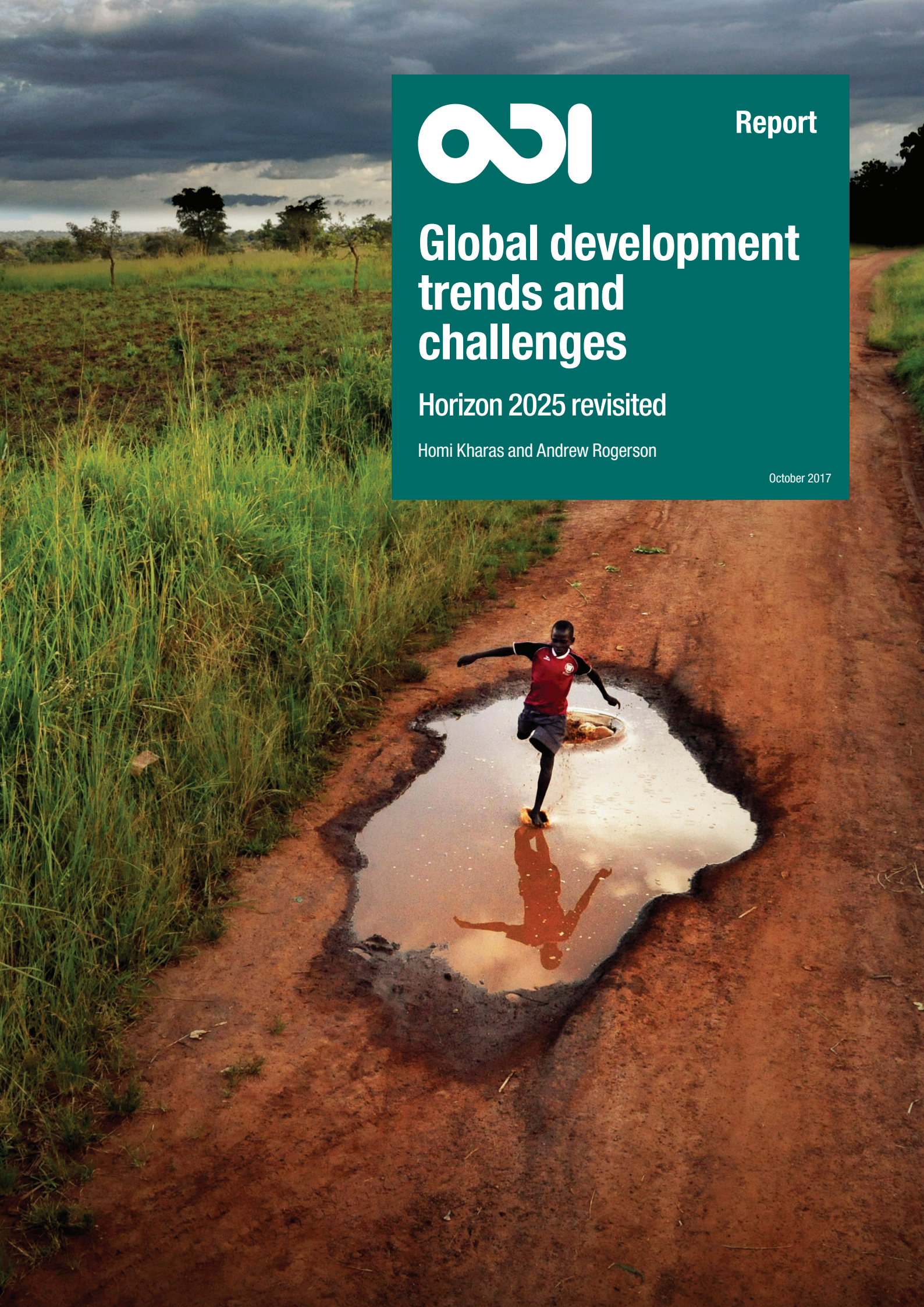
Report

Global development trends and challenges

Horizon 2025 revisited

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Cover photo: Eleven year old Willberforce runs in a puddle along an unpaved road near his home in Northern Uganda where he lives with his parents and six siblings.
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Contents

Acknowledgements	3
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Executive summary	7
-------------------	---

1. Introduction	11
-----------------	----

2. The meteors	13
2.1. The populist ‘roar’ and national-interest-first movements in the United States and Europe	13
2.2. A (much) more demanding sustainable development agenda	18
2.3. The combined conflict, refugee and migrant crises and their effects	22

3. The snowballs	27
3.1. Poverty trends and fragility	27
3.2. Business comes to the table	32
3.3. Climate: aid takes a back seat?	35
3.4. China’s ‘big push’ on development	39

4. Who’s most affected?	42
-------------------------	----

5. Conclusions	45
----------------	----

6. Key policy actions	47
-----------------------	----

References	48
------------	----

Annexes	50
Annex 1. Further information on traffic light indicators	50
Annex 2. Climate finance flows in 2013–2014 (\$ billion)	51

List of boxes, figures and tables

Boxes

Box 1. European countries' refugee spending is variable and inconsistently reported	25
Box 2. Methodological and definitional changes in poverty	27
Box 3. Indicators of donor exposure/resilience to meteors and snowballs	43

Figures

Figure 1. From weakness into strength – a virtuous cycle of aid-system responses to threats	10
Figure 2. Two decades of uneven globalisation	14
Figure 3. A crisis of confidence? 1 in 2 countries have lost faith in the system	14
Figure 4. What motivates aid: love, respect and fear, by other names	15
Figure 5. Canadian business views of the SDGs	20
Figure 6. Different regional takes on the top three SDGs	20
Figure 7. EU migrant arrivals by sea and other routes	23
Figure 8. Rising poverty in fragile states could soon end global poverty reduction	28
Figure 9. A shrinking poverty gap 2000–2030	29
Figure 10. Climate change ODA – no clear patterns of crowding out	36
Figure 11. Climate finance flows are diversifying	37
Figure 12. Resilience to future challenges: the ODI resilience index	43

Tables

Table 1. Sub-Saharan Africa now receives less net ODA (millions of current US dollars)	30
Table 2. Traffic lights for OECD aid agencies	43

Acronyms

AAAA	Addis Ababa Agenda for Action
AIIB	Asian Infrastructure Investment Bank
BMZ	Bundesministerium für Zusammenarbeit (German Development Cooperation Ministry)
BNDES	(Brazilian) National Bank for Economic and Social Development
BRIC	Brazil, Russia, India and China (a geopolitical forum)
CDB	China Development Bank
CRVS	civil registration and vital statistics
CSR	corporate social responsibility
DAC	Development Assistance Committee
DFI	Development Finance Institution
DFID	(UK) Department for International Development
DRC	Democratic Republic of Congo
DRM	domestic resource mobilisation
DRR	disaster risk reduction
EU	European Union
FDI	foreign direct investment
FSF	Fast Start Financing
GCF	Green Climate Fund
GDP	gross domestic product
GNI	gross national income
GPG	global public good
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IDC	international development contribution
IFC	International Finance Committee
IMF	International Monetary Fund
LIC	low-income country
MDB	multilateral development bank
MDG	Millennium Development Goal
MENA	Middle East and North Africa
MIC	middle-income country
NDB	New Development Bank
NGO	non-governmental organisation
OBOR	One Belt, One Road (known as Belt and Road Initiative)
ODA	Official Development Assistance
ODI	Overseas Development Institute
OECD	Organisation for Economic Co-operation and Development
OOF	other official flows
PPI	private participation in infrastructure
PPP	public–private partnership
SDG	Sustainable Development Goal
SSA	sub-Saharan Africa
SSC	South–South cooperation
TOSSD	Total Official Support for Sustainable Development
UMIC	upper-middle-income country
UNDP	United Nations Development Programme
US	United States of America

Executive summary

The socio-political phenomena that have materialised since 2012, when we first looked at the future of the development industry, have changed the aid landscape in ways that were not then imagined.

To recap: our Horizon 2025 paper was an initial effort to stimulate debate on the evolution of the aid architecture. We identified three major disruptors on the horizon: (i) high-impact philanthropy and private donations channelled through non-government agencies; (ii) South-South Cooperation (SSC) emphasising mutual interest of trade and investment, using blended aid and commercial financing instruments; and (iii) the pressures arising from a demand for climate change finance. We quantified these disruptors and identified which aid agencies might need to adapt most as these trends unfolded.

Now, five years later, we have the same motivation – to assess the implications of trends that we see as having major potential impact on aid agencies and the international development architecture. We ask whether our scenarios for 2025 have stood the test of time, what we missed, and what we have learned since.

We divide the drivers of change into *meteors*, in the sense of unforeseen and dramatic forces, and *snowballs* (as in, rolling downhill), which have gathered momentum since 2012, and in some cases changed direction.

Aid agencies need to present powerful new narratives linking aid with the national interest. This responds to the first meteor – the populist ‘roar’ and national-interest-first movement, with its associated anti-globalisation, anti-foreigner, anti-aid, anti-multilateral connotations. We look at its origins through the lens of divergent patterns of growth and stagnation by income group, and the erosion of faith that ‘the system’ still works for significant constituencies in the West. The consequence is a marked shift in development priorities in many Organisation for Economic Co-operation and Development (OECD) countries away from international altruism. Presenting ‘aid’ not as charity, but as an expansion of the source country’s investment and trade opportunities and its international ‘spheres of influence’, has become an important political defence for aid budgets. Arguments for spending public money on global challenges, such as the mitigation of conflict, migration and climate change, have a parallel self-interest logic. We foresee durable shifts in the institutional architecture, for example favouring national development banks, that can be traced to this shift, even if the populist pressures which encouraged it ultimately fade away.

The Sustainable Development Goals (SDGs) may not prove capable of transforming the development industry by 2030 and there is no indication yet that they are helping to generate greater financing. The second meteor we considered is Agenda 2030 itself, agreed in 2015. Agenda 2030 and the SDGs are not yet common currency outside a narrow intelligentsia, but they are diverse, universal and hugely demanding. We worry, however, that they may not succeed in transforming the development industry by 2030, let alone 2025, much though we may wish otherwise. Our caution is due, first, to the fact the large number of target combinations and sequencing options make it exceptionally hard to track and adapt to them, so almost anything, including business-as-usual, goes. Second, there is no indication that the SDGs are currently helping to generate more financing. The long-term impact of Agenda 2030 may lie more in its ability to inspire non-governmental, especially business, actors, to deploy disruptive technologies to achieve these goals.

The popular argument that aid can staunch migration runs counter to current evidence. This calls into question the response to the third meteor, the increase in migration and the influx refugees, a fusion of previously separable concerns with conflicts and their cumulative displacement consequences; the ‘mobility transition’, encouraging economic migrants from developing to developed countries; and, last and most toxic, hardening attitudes towards migrants in the latter, either on ‘objective’ grounds of limited absorption capacity, or prompted by baser emotions. Mainly because aid can relieve some of the financial and information constraints of the mobility transition, the consistent finding is that aid to countries with an average income of below approximately \$7,000 actually encourages migration. A more sophisticated approach to restraining migration needs to recognise the importance of non-aid policies, such as those related to visa restrictions, asylum-seeking and temporary employment, and to work more systematically with stable countries of first displacement.

The evidence suggests that the pace of global poverty reduction is slowing. There has been a snowball effect of aid agencies celebrating the rapid reduction of global poverty over the last 20 years, but this snowball is fast changing course. Global poverty has indeed shrunk rapidly, as we anticipated in Horizon 2025, but we see an end to this trend within the next five years. By then, the vast pools of extreme poverty in Asia will be largely drained, while poverty will continue to rise in fragile states, mainly in Africa. By 2018, Nigeria will be home to the largest number of absolute poor of any country in the world, and Ethiopia and Democratic

Republic of Congo (DRC) are not far behind. At the same time, however, the overall poverty gap has also shrunk, suggesting that it is now more affordable than ever to reduce poverty, especially if aid is complemented by stronger mobilisation of domestic resources. As a rough indicator, if developing countries spent just 1% of their gross domestic product (GDP) on effective poverty-reduction programmes, leaving aid to fill the rest of the gap, the additional contribution required would be about one-third of present Development Assistance Committee (DAC) aid.

The main take-aways: aid advocates that are celebrating the success in reducing poverty today will very soon need new explanations of why global poverty-reduction efforts are falling short. They will also have to pay more attention to countries' own efforts to mobilise resources and achieve effective safety-net spending.

The increase in **business engagement in development**, particularly in the infrastructure sector, is a double-edged sword for aid agencies. Core business motives are driving firms to pay more attention to the SDGs, and this momentum is snowballing with ever greater numbers of CEOs using the SDGs as a frame. Business engagement is over and above the impact-philanthropy approaches we covered in 2012 and which have grown since, albeit not spectacularly. The debate about the boundaries of business responsibility for sustainable development has a long and chequered history: the pendulum is swinging back towards recognising major win-win opportunities, especially, but not only, in green technology.

Nowhere in development is the role of business more eagerly anticipated than in the provision of infrastructure. New private investment in infrastructure projects rose from \$40 billion in 2002 to around \$220 billion in 2012, largely in telecommunications and energy. Since then, however, investment has collapsed, reaching less than \$30 billion in the first half of 2016. In part, this reflects tougher post-crisis regulatory standards on bank financing. Blended finance is complicated further by the missing catalytic role of multilateral development banks (MDBs), despite rhetoric to the contrary. In the first half of 2016, MDBs supported only \$1.2 billion in infrastructure projects with private participation (World Bank, 2016b). This resulted both from depressed demand for credit and supply-side restrictions on the MDBs' equity base and/or fiduciary ratios.

Aid agencies have been slow to partner with business on a grand scale, as they struggle to find the right balance. Without engaging (and many do not), they lose the opportunity to achieve greater impact. With engagement come risks of erosion of trust and the potential for scandal if business misbehaves. Neither option is appealing.

Contrary to most predictions, **international climate finance** has so far increased at the same pace as overall growth in official development assistance (ODA) for most DAC donors, and so has not crowded out programmes that are not climate-related. The international climate finance snowball is moving in unexpected directions. Our earlier view was that there was a risk that pressures to reorient

development aid to meet climate finance commitments would steer allocations away from poverty reduction and low-income countries (LICs). However, for most DAC donors, this does not seem to be the case.

The bigger picture is that all resource flows for climate mitigation and adaptation, of which aid was never likely to form the dominant part, have fallen far short of expectations. Climate programmes are being supported mainly by non-concessional loans and export credits, green bonds, and foreign direct investment (FDI). These flows can be oriented more towards greater climate sensitivity by new corporate-disclosure requirements, to account for environmental risk, including by depreciating and replacing higher-carbon 'stranded assets'. But they remain voluntary and vulnerable to enforcement failure in the name of 'freeing' domestic companies from red tape.

The impact of Chinese support is being felt everywhere. The huge Chinese big push on development, and the growing need for Western countries to factor it in, and play catch-up if and where possible, is a quickly growing and erratically moving snowball. We were fairly sure in 2012 that many other donors would try to emulate the Chinese example, by linking aid, trade and investment and blending the package with commercial loans. What we did not fully appreciate was the breathtaking scale of Chinese ambitions, for example in the One Belt, One Road (OBOR) cluster of mega-projects. China has provided enormous volumes of funds on commercial terms that, in the current global financial context, look extremely attractive. The two largest Chinese banks, China Development Bank (CDB) and China Ex-Im Bank, already hold roughly the same total international assets (\$680 billion) as all the Western-origin MDBs put together.

China now has the tools and programmes to challenge the West on development. This could prompt aid agencies to develop a 'competitive engagement' strategy of continuing to emphasise good governance in bilateral dealings, even where China does not, while encouraging cooperation with the new China-headquartered multilateral banks. These banks are off to a flying start and fears about lowering standards are giving way to grudging acceptance of the efficiency gains to be had, for example, from the absence of a resident Board of Directors. In terms of motivation (mutual benefit), efficiency, and perhaps effectiveness, Chinese development efforts are setting new benchmarks against which Western aid agencies will increasingly be judged.

Where does this all lead? We offer a series of reflections for all aid agencies to consider and then, as before, develop a traffic-light system to understand which are likely to be most affected.

High-level policy recommendations

Figure 1 shows a strategy to use the new drivers of change to create a virtuous circle for aid agencies. Below, we propose five high-level recommendations, but also offer a more detailed set of action areas in the Conclusions section of this report.

1. Governments will need to clarify how and to what extent international funding is allocated to non-aid national departments, such as health, environment or immigration.

Our first major point is that any new narrative linking aid to the national interest to mitigate populist pressures should involve non-aid agencies. For example, the Department of Health should concern itself with global preparedness for pandemics and the impact this might have on national health-related issues. Moving in this direction will require a greater clarity of mandates in developed economies between agencies responsible for core poverty reduction and other domestic departments, such as foreign affairs, defence, commerce, immigration, environment and health, that could support global public goods (GPGs) in areas critical to the national interest. The ‘aid-is-good-for-us’ narrative will also incorporate such features as cross-border global ‘bads’ like climate change, conflict and influxes of refugees, and accounting more systematically for any action taken.

2. To tackle global challenges effectively, rigid ‘graduation’ rules linking aid to country income levels must give way to more nuanced ‘gradation’ mechanisms, by which relatively better-off middle-income countries can be co-opted to help solve regional and global challenges, like surging migrant flows and unsustainable carbon emissions.

Due to spillover effects and the expanding regional influence of several middle-income countries (MICs), rigid rules on countries’ ‘graduation’ from receiving aid should give way to a more nuanced ‘gradation’ approach – reducing aid for richer countries but reaching an accommodation where they are part of the solution, as in the case of Jordan and Lebanon hosting Syrian refugees. One element of such an exercise should also be a focus on domestic resource mobilisation (DRM) in MICs to enable them to assume greater responsibility for their own development. Multilateral organisations often take the lead where global public goods and ‘bads’ are involved, but they are currently under stress and constrained in their dealings with MICs, so aid agencies need to support them financially and give them more leeway in operational terms.

3. Aid agencies must focus far more closely on how to achieve progress in tackling the root causes of fragility. One first simple step towards doing so is to ensure legal identity through robust civil registration and vital statistics (CRVS). Multilateral agencies operating in fragile contexts in different dimensions of security, humanitarian and development assistance must also be encouraged to work more effectively together.

How aid agencies operate in fragile contexts will become a defining issue for both multilateral and bilateral institutions. There is a desire to identify and tackle ‘root causes’ rather

than deal with symptoms of humanitarian disaster or wars, but less understanding of how to achieve that in practice. We advocate starting with the simple step of providing legal identity through CRVS, but also other measures, such as building resilience through the provision of safety nets, DRM and encouraging more private-sector jobs. Here, as in other areas, DevTech could assist, as digitalisation can mitigate many weaknesses in government functions.

4. Western aid agencies need to forge a ‘competitive engagement strategy’ with China in bilateral development cooperation, and to intensify collaboration with the international institutions that China sponsors.

Partnering with China offers opportunities for scaling up impact, for example in areas such as climate change, but also carries risks, especially for bilateral programmes where Chinese and Western approaches have differed.

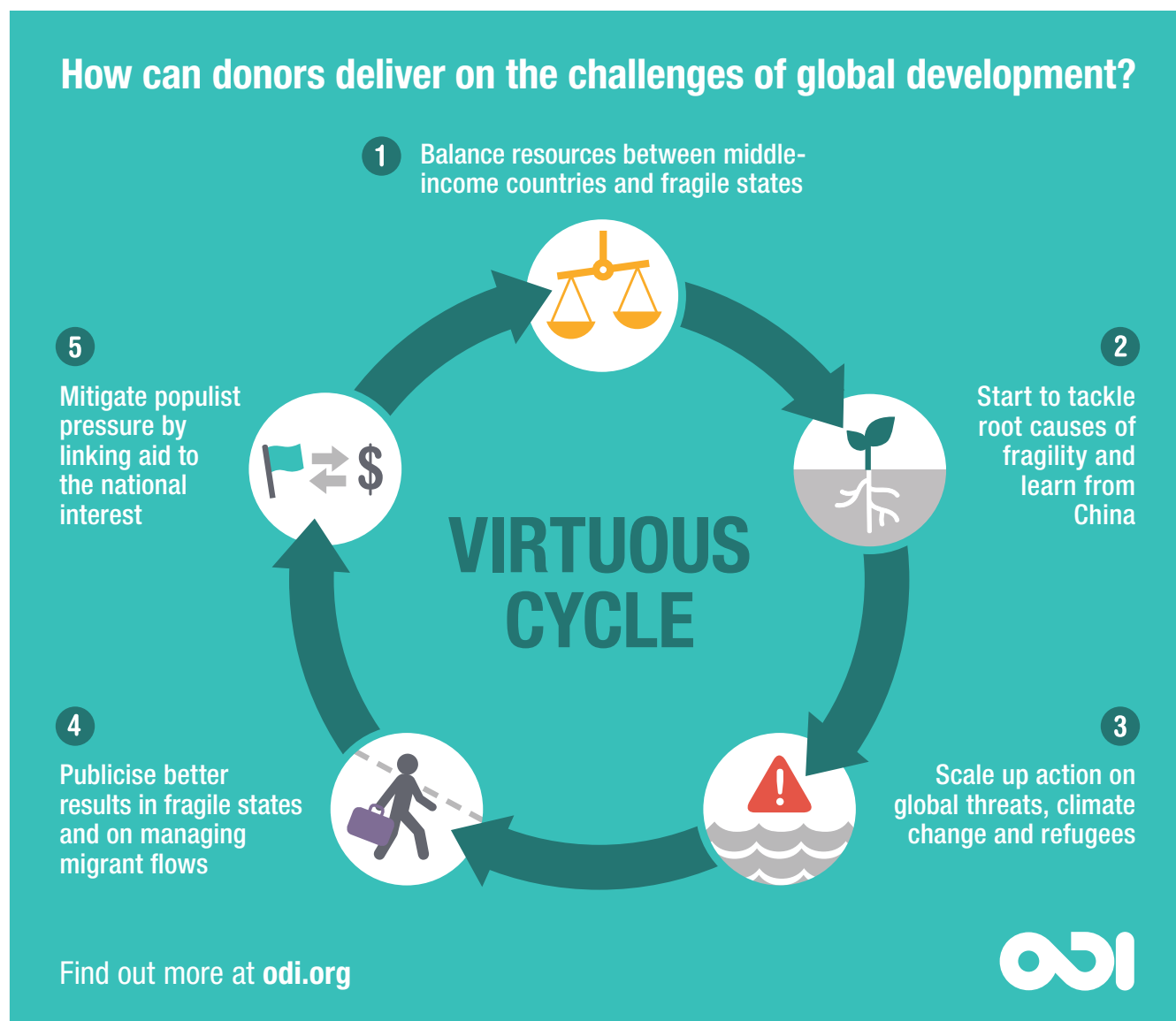
5. Blended (public–private) finance is only likely to reach its full potential if it is owned and supported by home-grown organisations. National development banks, which provide platforms that can originate projects locally, de-risk and troubleshoot implementation, and blend local and foreign private capital with concessional funds, deserve more international attention.

Scaling up, with domestic ownership, can also be facilitated by partnering with national development banks, some of which are developing novel platforms to facilitate project origination, mobilisation of local and foreign finance and implementation.

A world in 2025 where aid agencies can point to success in reducing fragility (and hence global poverty), mobilising business, addressing climate and refugee issues at scale, while also respecting national ownership and new geopolitical realities, will be a world where aid agencies will prosper and enjoy popular support. Conversely, weaknesses in this chain become vulnerabilities for aid agencies.

We close this report, therefore, with a review of how the changes we have described could affect aid agencies in each OECD country. Some changes are already incorporated in a ‘Donor Resilience Index’ developed by ODI, based on our 2012 approach. We reproduce this for convenience, but include additional indicators for aid agencies to ponder. Are they likely to be caught up in the ‘my nation first’ populist wave? How do they compare in current efforts to mobilise private funds? Are they operating in places where competition with China could be fierce? We suggest specific indicators to measure the relative severity of these pressures on aid agencies as our contribution to the strategic discussions and long-term scenario building that we hope continue in every country.

Figure 1. From weakness into strength – a virtuous cycle of aid-system responses to threats



1. Introduction

‘Nothing dates as fast as the study of the future.’
(Mazower, 2017)

In July 2012, we published *Horizon 2025: Creative destruction in the aid industry* (Kharas and Rogerson, 2012) – a look at some of the major forces shaping change in development cooperation, as we knew it then.

We highlighted three features of a rapidly changing global poverty landscape. Poverty was becoming ever more concentrated in fragile states, several of which had statistically graduated from low-income status. The overall poverty gap was nonetheless shrinking as a share of both global and high-income-country GDP, mainly thanks to faster growing, stable MICs, increasingly able to fund their own social programmes. And the speed at which poverty was becoming concentrated in African countries was faster than the allocation of aid flows to them, implying a growing divergence between aid deployment and its stated mission of eradicating extreme poverty.

We identified three major disruptors on the horizon: (i) high-impact philanthropy and private donations channelled through non-government agencies; (ii) SSC, emphasising mutual interest of trade and investment, using blended aid and commercial financing instruments; and (iii) the pressures arising from a demand for climate change finance. We quantified these disruptors and identified which aid agencies might need to adapt most as these trends unfolded.

Five years on, but still eight from our original 2025 horizon, we look again at our 2012 scenarios. How have they have stood the test of time, what did we miss and what have we learned since?

‘Aid’ by other names, and for different audiences. Along with ongoing changes in the structure of the ‘formerly known as’ aid industry come both semantic and real shifts in the roles of its various actors. So China and other newly developed or emerging economies have long rejected ‘aid’ terminology as disrespectful of their balanced mutual interests with other sovereign nations. Sophisticated public development finance institutions (DFIs), working with the grain of markets, talk more in terms of promoting viable investments and risk mitigation; and businesses naturally look to their bottom lines.

Development, as we discuss below, is no longer – if it ever was – a policy arena which maps neatly to a separate constituency, even within OECD member governments, where foreign, finance, commerce and defence interests increasingly come to the fore. And there are evident self-preservation incentives, given the growing public hostility to aid, for

re-badging aid programmes as something fitting more closely with the national interest, however that is defined, than with arguably nobler but more naïve notions of international generosity. In this report we are primarily concerned with generalist Western public ‘aid agencies’, regardless of the instruments they are using. We address mainly those who direct their policies and the wider community of partners, analysts and activists who influence them.

Our starting point is the enormous change in the landscape within which development finance agencies are operating. This change comes in two broad forms. There are meteors – large, unexpected (by us, back then) factors potentially causing massive change, but whose legacy might yet prove ephemeral. And then there are snowballs, rolling down mountainsides – trends which were already apparent and in most cases identified in our earlier work, but which have grown faster and/or changed direction compared to what we had anticipated, with consequently different, mostly larger, impact.

Meteors

1. The populist ‘roar’ and *national-interest-first movement*, with its associated anti-globalisation, anti-foreigner, anti-aid, anti-multilateral connotations.
2. Global agreement on the *2030 Sustainable Development Goals*, with their attendant change from business-as-usual to a transformational agenda, albeit with less consensus on how to achieve it.
3. The surge of *refugees* from conflict, and of *migrants* generally, and its lasting impact both on the content of development assistance and public support for it.

Snowballs

1. The ever-increasing *concentration of poverty in fragile countries*, with an eventual corresponding rise in global poverty, after a long period of positive trends. This context shifts the aid narrative to what can work in the toughest contexts, mainly in African countries.
2. The changed role of the *business community* from an ad hoc player, through corporate social responsibility (CSR) and impact investment, to ‘development as a core business opportunity’ and the concomitant surge of interest in blended finance and public–private partnerships (PPPs).

-
3. The continued activity on *climate change*, but the arguable reduction in the use of aid, as attention turns to more powerful, but not yet fully scaled, levers such as green finance, technology exchange and corporate reporting.
 4. *China's* 'big push' on development, which has injected a geopolitical dimension into aid.

In the following sections we first look at the meteors (section 2) and snowballs (section 3) in more depth. Each section ends with potential implications for the international aid architecture and suggests appropriate policy responses, summarised in 12 key recommendations in Section 6. Section 4 examines some indicators of the strength of these forces for different donor countries. Section 5 concludes.

Our time horizon, 2025. Mid-2025 is eight years away, but arguably this milestone is shrouded in greater uncertainty than ever before, especially in relation to fundamental but previously unforeseen challenges to globalisation and global governance. For example, it already spans a period of one year beyond what might be the consequences of a potential second Trump administration, six years beyond the scheduled end of Brexit (EU Article 50) negotiations for the United Kingdom (UK) to leave the European Union (EU), and three beyond French President Macron's first term of office. To help detach still further from current political debates, and to link up with Agenda 2030, readers can attempt to make projections to 2030 for themselves, but we would warn that there are too many unknowns for developing more than sketchy future scenarios.

2. The meteors

2.1. The populist ‘roar’ and national-interest-first movements in the United States and Europe

‘All power comes from the people, but where does it go?’
(Berthold Brecht)

The first meteor is the populist ‘roar’ and **national-interest-first movement**, with its attendant anti-globalisation, anti-foreigner, anti-aid and anti-multilateral connotations. We look at its origins through the lens of divergent patterns of growth and stagnation by income group, and the erosion of faith that ‘the system’ still works for significant constituencies in the West. The consequence is a marked shift in development priorities in many OECD countries away from international altruism. Presenting ‘aid’ not as charity, but as an expansion of the donor country’s investment and trade opportunities and international ‘spheres of influence’ has become an important political defence for aid budgets. Arguments for spending public money on global challenges such as the mitigation of conflict, migration and climate change have a parallel self-interest logic. We foresee enduring changes in the institutional architecture, for example favouring national development banks, that can be traced to this shift, even if the populist pressures which encouraged it ultimately fade away.

2.1.1. Genesis – shifts in global and local inequality

Few, if any, observers in 2012 could have foreseen phenomena like a Trump presidency or Brexit, or the hardening of existing populist sentiment in, for example, Turkey and some countries in Eastern Europe – and we were no exception. Nor are we now best placed to opine whether these political forces will prove durable

or ephemeral (for an expert dissection of populism and reactions to it see, for example, Muller, 2016) – though merely allowing for the latter possibility suggests interesting alternative scenarios. However, taking our intermediate 2025 time horizon, still eight years away, let alone peering towards 2030, we can reasonably assume that the institutional architectures of the ‘aid biz’ will have changed significantly *and maybe enduringly* in response to current political signals, even if, or when, many of the original drivers subsequently fade from the scene. It is the long-term induced effects of this ‘meteor’, even if it turns out to be a near-miss, that concern us.

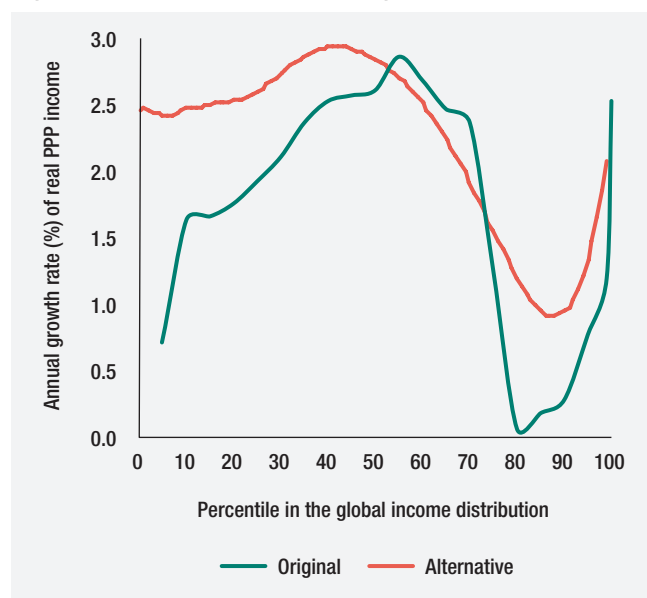
Acute observers of the apparent recent decline of Western liberal values and related mistrust of ‘elites and experts’ (see, for example, Luce, 2017) have pointed out that the seeds of anger and discontent among the middle classes in the US and much of Europe can be found in the virtual stagnation of median incomes over the past 30 years. At the same time, the incomes and the wealth of the global top 1%, most of whom were originally from these countries at the start of the period, has soared – which is consistent with modest positive overall growth rates experienced in most Western countries, apart from the worst few years of the global economic recession following 2008.

The same period has seen fast convergence towards OECD income levels in a large subset of emerging economies, and in particular the middle classes of China and India, whose income growth in two of the past three decades reached 80% (Milanovic, 2016). Even the lower-income deciles in such countries saw far higher growth rates than did the middle classes in OECD countries. Lakner and Milanovic (2013) represented these trends in their now famous ‘elephant’ chart, originally referring to the 1988–2008 pre-crisis period of ‘high globalisation’.

Figure 2 charts income growth by percentile groups across countries, at purchasing power parity, based on nearly 200 household surveys. It shows big income gains in the middle and the very top, separated by a low to zero progress group around roughly the 75th to 85th percentiles, mostly occupied (at least at the beginning of the period, see footnote ¹) by OECD middle classes. The dip in the elephant's trunk, on either side of the most successful groups, zeroes in on the locus of discontent with globalisation and the distribution of its fruits. The rump of the beast is created by the growing middle class in the MICs, initially mainly in China and India, but increasingly in other previously low-middle-income countries (LMICs).

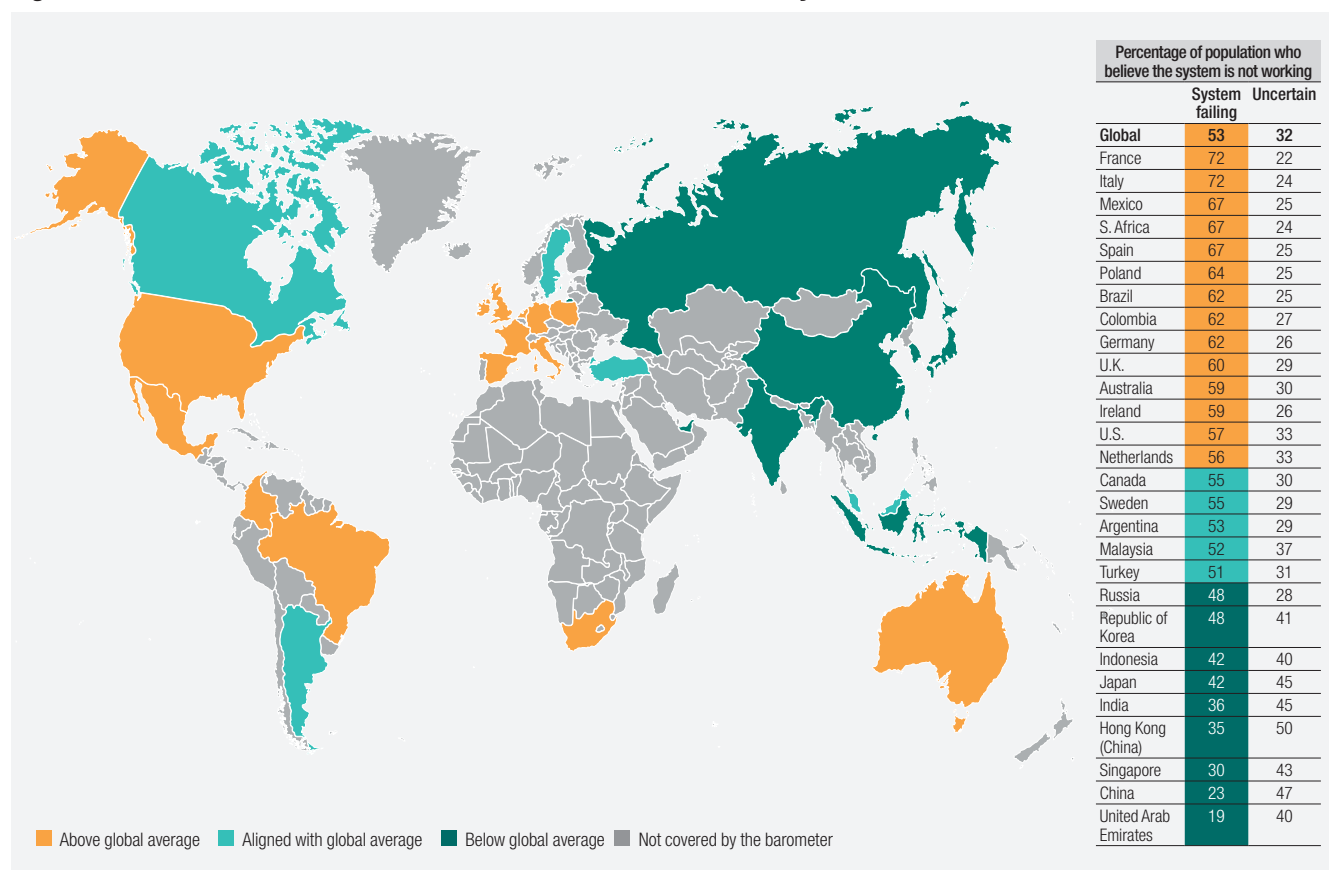
Another way to look at globalisation and its critics comes from opinion surveys. The Edelman Trust Barometer (2017) charts, among other responses, the proportion of the population who believe that 'the system is working for me'. Those with the least faith in the system are overwhelmingly in OECD countries, and those with the most in emerging economies (Figure 3).

Figure 2. Two decades of uneven globalisation



Source: Lakner and Milanovic (2016)

Figure 3. A crisis of confidence? 1 in 2 countries have lost faith in the system



Source: 2017 Edelman Trust Barometer

1 There has been subsequent criticism (e.g. Corlett, 2016) of the sometimes exaggerated policy significance of such findings, given that the more pronounced S-shape in the original case compared across time income percentile groups that did not contain the same composition of individuals, or even countries. Lakner and Milanovic's 'alternative' line above, which does try to compare like for like, sends a more nuanced message, but still broadly consistent with the original. In it, the worst performing groups near the 90th percentile reaped modest income growth (20% in 20 years), and the top 1% do slightly less well, relative to the next groups down.

Similar evidence (2017 Gallup World Poll) shows that all groups in LICs and MICs, and especially those in the lowest income quintiles, feel that they are benefiting from the global system, while the lowest three quintiles in rich countries are the least happy group (Graham, 2017). This points to an ongoing contentious debate. Most groups in developing countries think that globalisation is working very well for them, and want more of it, while high-income countries are struggling to offer alternative solutions that also benefit them widely enough. The perceived zero-sum game between progress in the middle classes in developing countries and stagnation for the same groups in developed countries ('they've stolen our jobs') is a sign of troubled waters for many aid agencies, originally designed to transfer resources from the latter to the former.

Is the engine of globalisation itself stalling? The pace of growth in emerging economies, which so effectively 'bulked up' the Milanovic mammoth before 2008, has since slowed dramatically. In 2007, growth was slowing in just one in 20 emerging economies, but, by 2013, the ratio was four out of five. Excluding China, 2% average per capita growth in emerging economies is slower than in the supposedly 'converged on' US (Sharma, 2016). Global capital flows have shrunk as a proportion of world GDP to levels last seen in 1980, trade has fallen back, and even the overall number of migrants from poor to rich countries has remained roughly stable, despite controversies regarding Syrian and other refugees from conflict (see section 2.3 below). The Brazil, Russia, India and China (BRIC) 'brand' has been seriously undermined, and with it the idea that sustained high growth rates were a given in large emerging economies. Of the BRIC nations, only India has a serious hope of growing anything like as fast in the current decade as it did in the 2000s (Sharma, 2016). Of particular concern is the slowdown in African countries, most of which are dependent on commodity prices. Without economic growth, aid will be exposed as the sole (and rather weak) engine of poverty reduction.

2.1.2. Development finance objectives: shifting towards the national interest

In our earlier report, we considered three basic motivations for 'aid', or more generally international development co-operation: *altruism*, *mutual benefit*, and *enlightened self-interest*. (Hard-boiled cynics might simplify them as *love*, *greed* and *fear*, respectively, found among the most basic human instincts: we give the benefit of the doubt to mutual-benefit approaches, including SSC, and replace 'greed' here with 'respect'.) The first motive operates mainly in social progress space, the second in the growth, bilateral investment and trade space, and the third is mostly about the protection

Figure 4. What motivates aid: love, respect and fear, by other names



of the global commons from threats such as climate change, infectious disease or the repercussions of violent conflict.

There are considerable overlaps between these purposes, both in intent and outcome. So, for example, bringing isolated and fragile countries into the political and economic mainstream improves both global stability and more mundane national trade and investment prospects. Mitigating climate change reduces a powerful driver of fragility and poverty. And so on. Nonetheless, the shift in public support for development that is arguably occurring in many OECD countries can be visualised as a move southwards, shown in Figure 4, and often also eastwards, towards national interests, enlightened or not, from an arguably more altruistic starting point somewhere above the centre of Figure 4.

National economic interest (combining elements of both direct economic benefit and enlightened self-interest) is no longer an unacceptable argument for foreign assistance – if it ever was – as we pointed out in our earlier report (see also Gulrajani and Swiss, 2017). It was already becoming part of the 'normal' development policy discourse in the UK well before the referendum on leaving the EU, and has never been far from the top of the agenda in many other countries, such as France (MAE, 2011).

Presenting what used to be called 'aid' not as charity but as an investment for mutual benefit, and for expanding the source country's investment and trade opportunities and its regional 'spheres of influence', has also become an increasingly important political defence for aid budgets under attack from 'our-nation-first' advocates.² Arguments

2 There is as yet little direct evidence of any dramatic fall in public support for international development aid in the UK: 89% of respondents say that it is important to help people in developing countries (Eurobarometer, April 2017). A smaller, but still impressive, 67% say that providing financial assistance to developing countries is an effective way to tackle poverty. Opinions are divided about whether current aid spending levels are too low (25%), too high (17%) or adequate (46%) (ibid.).

for spending international public money effectively on global-commons purposes, such as the prevention of conflict (and consequent population displacement) and mitigation of climate change, fall under a similar logic – another form of the national interest. But they also depend crucially on proponents demonstrating to a sceptical public that they can achieve results in such areas, especially by working more effectively in fragile contexts (see section 3.1 below).

There may well be another feedback loop at work, starting from the pressure to justify results to a more sceptical domestic audience, which encourages a search for short-term deliverables and the increased ‘privatisation’ of bilateral and multilateral aid into multiple discrete packages, rather than a wholly-owned and longer-term strategy on GPGs. More fragmented approaches are less likely to bring about change at scale, and risk missing the wood for the trees.

Climate change and migration/refugee imperatives for international assistance, discussed further below, also arguably operate at different levels of urgency in a ‘post-Trump, post-Brexit’ world. This is because migratory pressures exacerbate some of the newly exposed political faultlines and anxieties in a more immediate way. Thus even the French *Front National* 2017 electoral platform advocated international aid, albeit mainly directed to reduce immigration pressure, however that might be achieved in practice (see section 2.3). Climate change, even for the vast majority who accept responsibility for reversing global-warming trends, is on a currently slower-burning fuse – yes an absolute priority, but also one that can still be displaced by more ‘immediate’ emergencies, even though time for action is fast running out (see section 3.3). The relative responsibilities of private and public action are also less sharply defined in the issue of climate change than in the refugee/migration case, which lets tangible public intervention off the hook more easily in the former.

2.1.3. Implications for the international aid architecture

Among the litany of knock-on effects of re-emergent nationalism is the increased dissociation of some developed countries from international arrangements which they believe are incompatible with national interests.

That includes the US and UK’s announced withdrawal from regional trade (and trade-plus) agreements, obviously, and from the Paris Climate Change Agreement in the case of the US. It also entails more restrictive attitudes towards migration, especially but not only, in the name of national security and absorptive capacity, in these and many more cases, for example in Eastern Europe. Such attitudes constitute an existential challenge to an internally borderless EU in view of the reluctance to spread the financial and political costs of immigration more evenly. US funding for the UN is also under severe

threat, which could fatally undermine its already thinly spread peacekeeping capabilities and much else.

Amidst all this overarching change, or threat of change, it seems parochial to single out the impact of nation-first politics on something as relatively low-profile and technocratic as the ‘development’ architecture. Aid – in the shape of DAC ODA anyway – is still by conventional measures apparently stable, even net of refugee costs (DAC, 2017). Record figures are also now being claimed for less concessional loan-based support from a growing group of MDBs, including the newest ones set up at the behest of emerging economies, like the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank (NDB) (section 3.5). These MDBs are ‘double-leveraged’ by their simultaneous ability to borrow multiples of their paid-in capital from markets on prime terms and to bring additional investors into their project syndicates. Hence their new mantra of turning ‘billions into trillions’ (World Bank, 2015). The new focus on aid for growth, trade and investment also signals a need for loans and guarantees (in large volumes) rather than grants and subsidies. All of this sounds reassuring.

But four major underlying and potentially destabilising changes are, we believe, already afoot.

First, non-development ministries’ political and budget space is expanding. The rising power of the global-commons and mutual-interest arguments for official external finance will be reflected in ever-stronger domestic moves to diversify spending control away from ‘development agencies’, with large centralised budgets which are vulnerable to envy, populist critiques and scandal. So the core agency’s influence and resources will increasingly need to be shared with departments primarily focused on, for example, foreign affairs, security, immigration, climate change, export promotion and health. In many cases, as has recently been proposed for consideration in the US and already implemented in Australia and Canada, overall responsibility for development will be fully re-integrated with foreign affairs ministries. In the UK, the Department for International Development (DFID) is now an endangered species, a stand-alone development strategy department at cabinet level, also responsible for implementing most of the development budget (BMZ in Germany fulfils the former role, but not the latter).

This diversification will necessarily lead to some loss of focus on poverty-reduction ‘basics’ at country level, in the name of the relevant thematic GPGs, where the two objectives are not perfectly overlapping. We argue below that this is already the case for both climate change and migration. A recent review of the UK’s spending to support international food and nutritional security (Rogerson, 2017) also found that DFID’s aid was exceptionally well focused on LICs compared to the DAC average, but that this was not the case for the growing proportion channelled through ministries with other overarching

priorities. Multiple-agency approaches, which can only be partially co-ordinated at source, will also necessarily lead to further fragmentation of interlocutors at country level. Fragmentation has pejorative connotations, mainly in terms of additional administrative costs, in the orthodox discourse on aid effectiveness, but aid recipients increasingly see this approach as offering them greater choice, and as diluting the conditions that might otherwise be required by a more unified group of donors (Greenhill et al., 2016).

One could envisage going deliberately further along this road, by identifying key areas of action on GPGs, where external action powers and spending authority are explicitly delegated to expert domestic communities – for example, health pandemics to health ministries working with their international peers, or practical and humane ways to tackle migrant flows to the administrations responsible for migration and asylum (see, for example, Kaul, 2017). This could be linked to robust levy-based core funding by the norm-setting agencies of the UN system, discussed in the next section. As a *quid pro quo*, ‘core’ national development agencies would perhaps be asked to focus mainly on country-specific development priorities (particularly the case of fragile states), whereas others could tackle GPGs allocated along theme-specific lines. Of course, such an approach carries risks, not least of fragmentation of resources and of undermining effective interventions. The important point, however, is not the institutional structure but the clarification of and distinction between poverty reduction and GPGs. This will require clear specification of cross-country allocation priorities regardless of whether development budgets are centralised in a ministry of foreign affairs or are dispersed across government.

Second, ODA definitions are increasingly under threat. The main external protection for national aid budgets, represented today by the totemic ODA 0.7% pledge and its associated DAC aid-content definitions, will soon erode if it alone stands in the way of this centrifugal force (see, for example, de Cazotte, 2017). There are unmistakable signs of national political pressures to broaden the definition of ODA in order to accommodate expenditure deemed more palatable to domestic constituencies, like foreign peacekeeping.³ The temptation to accommodate other primary spending purposes which have a plausible link to development will be increasingly hard to resist. It will soon, therefore, become critically important to establish a robust ‘outer budget envelope’ of such overall international action, which we call international development contributions (IDCs) (Kharas and Rogerson, 2016) and which the OECD is developing under the name Total Official Support for Sustainable Development (TOSSD).

This re-branding of development cooperation is badly needed for reasons of clarity and coherence, but also to buy off some of the main internal critics of formerly-known-as aid. The alternative would be to keep alive the fiction of a numerical ‘aid’ target as a share of national income, yet continue to include additional items into the numerator, to the point where it could seriously undermine the brand. We do not advocate this shift, but it must now be considered a serious risk (a fatal one for the DAC as an institution).

Third, expect to see the further rise of leveraged and blended finance. Existing and new DFIs will emerge and expand at both national and, as we shall discuss later, international level. These institutions share (i) the presentational advantages of operating (or appearing to operate) on for-profit business-like lines, in conjunction with national investors and exporters, as well as (ii) the benefits of financial leverage (through loans, guarantees, equity stakes, etc.), meaning that their financial calls on national budgets are much less frequent, and often much less transparent, than is the case for grant-making agencies. Using aid resources to leverage private investments also offers (iii) opportunities to keep engaged in higher-income country contexts which direct grant aid may have to abandon. Such DFIs can also (iv) park significant administrative costs off-budget and help contain or reduce the number of civil servants. They might also (v), as in the case of the German KfW (and the European Investment Bank (EIB) for its home region, and China’s CDB), operate domestically as well as internationally, which helps to spread overheads and risks. In Canada, France, Germany, Italy and the UK, among others, the growing reliance on these loan-making institutions (sometimes from a very low starting base) is clear. Only the US seems to buck this trend, with the Trump administration threatening to stop funding the Overseas Private Investment Corporation (OPIC).

The main policy caveat to rapid expansion of public–private partnerships (PPPs) and blends is the criticism that the investments they support would probably have happened anyway, without the supposed de-risking offered by the DFIs’ intervention and any subsidy element they mobilise. There are other potential disadvantages, including moral hazard, if investors believe they no longer have to observe as much due diligence as strictly as they would otherwise, and the risk of distortion of competition between firms or across sectors. We discuss these problems in section 3.2 below.

The relentless growth of domestic funding channels and expertise in the rising MICs and upper-middle-income countries (UMICs), many of which have established their own national development banks (the Brazilian National Development Bank has a larger asset base than the World

3 The UK election Conservative Party Manifesto stated that the definition of what constituted effective development spending would be discussed with Britain’s partners, but that, failing agreement, the UK would amend it unilaterally for the purposes of UK law.

Bank, for example, as does the external arm of China's CDB), with their commensurate skill bases, also means that external financial and human capital is increasingly less relevant, both there, and in other countries where they may compete.

Fourth, parts of the multilateral architecture will be unable to take heavy budget pressure for much longer. The MDBs, which we discuss in the next section, have greater built-in financial buffers. They also shelter many billions of dollars of donor trust funds to be disbursed as grants, or blended with loans, for various thematic and exceptional purposes. In so doing they compete hard, from a stronger track record of financial discipline, for ever-scarcer tax revenues with other multilateral, especially United Nations, institutions that are already on a much tighter core-funding 'leash'.

Within this latter class of grant-dependent multilaterals, there is a subset of institutions on which many others depend for their specialised knowledge, standard-setting capabilities and provision of monitoring or surveillance against such standards, most clearly in global health, food, veterinary and environmental matters. We discuss a possible way forward for them in the next section.

There will be some difficult situations to face, nonetheless, including multi-purpose agencies which do not have a clear 'brand' in politically high-demand areas, and for which attempts to diversify income sources are proving ineffectual, distracting, or both. They, and their governmental owners, will need to consider some combination of increased partnering with MDBs, raising funds from the general public, providing more fee-based services or, if necessary, downsizing or merging with other agencies. The temptation to postpone corrective action – and thereby let the proverbial frog come to the boil very slowly, so it fails to jump out in time to save itself – is nonetheless real.

Key policy recommendations

- 1 Move towards much greater clarity of mandates in developed countries between agencies primarily responsible for core poverty reduction in specific country contexts and specialised departments co-ordinating support for GPGs, including via allocations to developing countries. This will require clear specification of cross-country allocation priorities, regardless of whether development budgets are centralised in a ministry of foreign affairs or dispersed across government.
- 2 Establish a new internationally credible definition of official financial assistance, separate from ODA, against which both developed and emerging economies can benchmark their funding: for example, IDCs.

2.2. A (much) more demanding sustainable development agenda

The second meteor is Agenda 2030 itself, the **Sustainable Development Goals (SDGs)**, agreed in 2015. These are not yet common currency beyond a narrow intelligentsia, but they are diverse, universal and hugely demanding. We worry, however, that they may not succeed in transforming the development industry by 2030, let alone 2025, much though we may wish otherwise. Our caution is due, first, to the fact that the large number of potential target combinations and sequencing make it exceptionally hard to track and adapt to them – so almost anything, including business as usual, goes. Second, there is no indication that the SDGs are currently helping to generate more financing. The long-term impact of this agenda may lie more in its ability to inspire non-governmental, especially business, actors, to deploy disruptive technologies to achieve these goals.

2.2.1. What might be game-changing about the SDGs?

In 2012 we could not know the shape that any consensus on a new set of global aspirational objectives would take – what has since become known as Agenda 2030, or the SDGs. The SDGs are a meteor in the sense that they represent a complete paradigm change, from the North–South aid-for-human-capital arrangement to a universal, 'leave no one behind' transformation of all countries towards inclusive, sustainable growth.

The earlier experience with the Millennium Development Goals (MDGs), which were fast approaching their 2015 deadline, had suggested, in particular (see e.g. Fehling et al., 2013; Fukuda-Parr et al., 2014), that development and sustainability aspirations were being approached disjointedly. This was because there was inadequate concern for peace and institutions; a mechanistic focus on overall poverty risk disengaging MICs, and ignored large pockets of poverty within them; there was insufficient focus on jobs and equity; there was excessive emphasis on international transfers rather than on DRM; countries had insufficient say in the shaping of priorities; there was too much emphasis on areas that were relatively easily measured; and the role of non-state actors, particularly the private sector, was underdeveloped.

Fast forward to 2015 and today, and most of these concerns have found major expression in the SDGs, which are a vastly more demanding, indeed transformational, undertaking than the MDGs, in several key ways including:

- Far wider scope: there are now 17 goal areas and 169 'targets' (yes, really, although only 34 are quantifiable outcomes).
- 'Going for 'zero': complete elimination, not just reduction, of income poverty and other undesirable conditions.
- Universality: every nation, including the richest, should frame and own its ambitions.

- Leave no one behind: an explicit concern with inequality, not just average progress levels.
- Heightened focus on sustainable consumption patterns as well as on air, water and land use, and city life.
- Explicit concerns with peacebuilding and human security, the rule of law and good governance.
- A balance of responsibilities: priorities set at country level, supported by international partnerships.

2.2.2. How are they to be funded and delivered?

Before the final adoption of the SDGs at the United Nations General Assembly, but when their broad contour was already known, agreement was reached on a similarly multi-faceted set of delivery and financing recommendations, known as the Addis Ababa Agenda for Action (AAAA), or the Addis Agenda. This established the primacy of DRM to fund the SDGs, as well as suggesting an array of key international supporting roles and tasks, ranging from tax cooperation to intellectual property rights, debt resolution and much else, and confirming the imperative of meeting existing aid efforts (ODA/GNI (gross national income (GNI)) and focusing on meeting the targets of the least developed countries.

While these processes constitute remarkable feats of international consensus-building and have already energised large numbers of people in diverse constituencies – and hopefully will continue to do so in the monitoring of progress through the UN system – it is fair to say that the practical way forward on how to fund and achieve the SDGs is still much less clear than the overarching package of aspirations as such. This lack of clarity is due to at least three fundamental reasons. First, national governments are (quite rightly) free to select the particular ‘mix’ of making progress towards achieving the SDGs (in terms of areas and relative speed) that matters most for them, but that balance will take time to establish, will shift over time, and may frequently leave major external partners as well as internal stakeholders lagging behind, or out of step. As we suggested in a preparatory paper for Addis (Kharas et al., 2014), the detail of country-level SDG financing plans will involve sequencing choices that are not necessarily intuitive, such as favouring building roads before constructing schools to expand education, for demand-side reasons, or choosing to borrow rather than increase taxes to fund infrastructure investment, or vice versa. There may therefore be very uneven progress across and within countries, dictated more by intrinsic capacity and coordination limitations than access to finance in general, let alone the shape of external assistance in particular. On the plus side, individual countries and the international community will not lack for benchmarks of progress against which to measure themselves and each other, and that benchmarking can galvanise the search for solutions.

Second, the imperative to ‘leave no one behind’ can likewise be legitimately viewed from different, arguably equally valid, perspectives, especially when those furthest behind are not those to whom additional services can be delivered most cheaply in the short run. That implies giving higher (implicit

or explicit) social weights to certain groups, failing which investment will gravitate towards choices offering higher economic returns. The data and analytical methods required to differentiate these cost–benefit relationships fully by income, ethnic and regional group, not to mention the practical political complications of taking decisions on that basis, are daunting (Grenhill and Rabinowitz, (sic), ODI, forthcoming). Some donors are rightly starting to focus on how best to support this process. To the extent that some governments may not give high priority to those who are left behind, aid agencies may be tempted to provide funds in less fungible forms, for example via non-government organisation (NGO) channels, to improve overall targeting (ibid.). In more sophisticated public finance environments, however, especially where external aid is very small relative to domestic spending, national and local governments will often be able to adjust their financing so as to frustrate such aims.

Third, and perhaps most significant, already at Addis and since then, classic collective-action problems are surfacing, particularly in terms of constructing the platforms to sustain more robust engagement on international tax systems, social safety nets and other matters. The faultline is often between a UN-led process that has, arguably, more legitimacy but less expertise, and one led elsewhere (for example by the OECD) that offers the opposite mix. Some effective combination of the two should logically emerge, but such compromises are proving hard to promote, particularly in an environment of US intransigence regarding UN institutions more generally. The Global Partnership on Effective Development Cooperation, in principle harnessing the DAC and the United Nations Development Programme (UNDP), but still woefully lacking in political clout among both ‘old’ and ‘new’ aid constituencies, may be a case, or casualty, in point.

2.2.3. So what? A permissive framework, not a blueprint

These challenges should not deter us from, indeed they could well spur us into, action. On the other hand, we should not naïvely assume that this ‘meteor’ has already revolutionised international development as we knew it. Indeed, we think it has not yet done so, and, at the risk of sounding politically incorrect, might not do so over the next 13 years either. It is striking that, in the US, beyond a small community of New York development experts, there is little awareness of the SDGs (OECD, 2016). But it could have other important effects beyond aid agencies, and these could, in turn, influence aid behaviour. It is worth unpacking why that might be so.

The SDG ‘quest’ will generate multiple alternative solutions, internationally, nationally and across different interest groups within countries. A good illustration (Figure 5) is provided by the rankings offered in a survey of Canadian businesses just after the SDGs were adopted in 2015.

The most obvious asymmetry is between what is advocated for the world, for one’s own country and, to some extent, for one’s company or community. A second feature is that a number of the new SDGs – including

stalwarts like human rights and good governance – do not so far make it onto any of these lists. A third feature is the consistent emphasis on decent and productive work, which reminds us of concerns about stagnant real incomes that can spark a populist backlash. Indeed, in larger SDG opinion surveys differentiated by region (Figure 6), this is

the leading preoccupation in North and Latin America, Europe, and South-East Asia, but not, interestingly, in some other regions, notably China and the Middle East and North Africa (MENA). The Chinese emphasis on good governance and sustainable land use, not replicated elsewhere, is also striking.

Figure 5. Canadian business views of the SDGs



Source: SDG Survey 2017, Global Compact Network Canada

Figure 6. Different regional takes on the top three SDGs



Source: SDG Survey 2017, Global Compact Network Canada

2.2.4. Implications for the aid architecture

These patterns further emphasise the eminently political nature of the SDG process, and how far removed it is likely to be from the typical comfort zone of a ‘technical’ aid (or development finance) agency. As a thought experiment, imagine one that is equally committed, and equipped, to help all its ‘clients’ deliver all the top priorities in all regions, including its home country in the case of national development banks. This is implausible, to say the least. The implementation of the SDGs more generally requires a combination of *systemic* and *contextual* approaches. This involves awareness of where the weak links are, which set the limits to systemic responses, and an understanding of the ever-shifting country context of those links and of the politics behind them.⁴

For aid agencies, the SDGs present a quandary. The multiplicity of goals means that ‘anything goes’ – almost all interventions can be justified as contributing to Agenda 2030. But at the same time, the agencies’ political bosses and shareholders are demanding more exacting results-chain depictions of the impact of aid dollars; hard to produce when these are thinly spread across countries and themes.

What is more likely is that the SDGs will provide a legitimising framework for the engagement of new actors, largely independent of ODA, such as the private sector. They will also provide a large-scale canvas for the introduction of high-profile funding initiatives by the MDBs, and imply more robust support for norm-setting specialised agencies. We discuss these three prospects in turn.

Making the most of a DevTech revolution. Blockchain, satellite imagery, digital IDs, smart cards, geo-engineering, battery storage, driverless cars, carbon capture and storage, telemedicine – all these are examples of scientific discovery and innovations that have the potential to disrupt the way in which development happens. Rwanda is already using drones operated remotely using 4G networks to deliver blood supplies. At tech conferences everywhere scientists and engineers are presenting products to improve the efficiency and effectiveness of development interventions.

There are similar advances in business models – solar panels can become collateral for small loans. Big data (in the case of Alibaba, customer transactions) can model creditworthiness at very low cost. Training companies can convert unskilled teenagers into skilled computer coders if their motivation is high, regardless of their level of formal school attainment.

At the same time, there is a dark side to technology. Automation can threaten jobs, especially in the manufacturing sector, still the ‘Holy Grail’ for African countries looking for transformation. Privacy concerns are lower in developing than in developed countries, according to surveys, but this could change if protections and safeguards are not put in place.

This world of rapid upheaval is a far cry from the old world of development. There is knowledge about the science

and technologies now on offer, but procedures and staff skills in aid agencies have yet to adapt. Some of the new technologies, like virtual reality, can be used to build empathy and support for development projects. They can provide the means to tell a compelling story in a way that reports and evaluations cannot do, and may yet be more valuable for aid agencies than deploying the flashy new tools that other technologies promise.

Aid agencies cannot afford to neglect the opportunities or ignore the risks offered by new technologies. Partnerships with development entrepreneurs and with their own scientific and business communities could be a bridge to the future. But some of the fads might fade in favour of traditional interventions in support of service delivery and policy and institutional strengthening. It is up to agencies to strike the right balance.

Scaling up the MDBs by taking reasonable additional risks onto their balance sheets. Obviously, existing MDBs, like national DFIs, are less exposed to direct budget pressures. Indeed, as many observers have pointed out (e.g. Humphrey, 2017; Kharas et al., 2014; Birdsall and Morris 2016), these institutions could expand substantially without calling for new equity, via changes in statutory leverage ratios and /or other forms of balance-sheet optimisation, such as borrowing against the idle capital effectively represented by their soft-loan receivables books. Alternatively, some of their backers could provide selective loan guarantees, functioning as quasi-equity, only a fraction of which would need to be paid up-front (Humphrey, 2017; Education Commission, 2017). Granted, such changes may involve an element of governance complexity, and possibly of additional market-rating risk, and could shift the balance of institutional priorities in unexpected ways, and so will require careful case-by-case assessment. But it would be irresponsible not to look into them.

There may also be greater scope for partnering *between* MDBs, for example to spread regional portfolio risks through judicious asset sales among them, or sharing certain specialised staff skills that require a significant ‘critical mass’. It is debatable, though, whether management incentives for such networked solutions are likely to be sufficiently strong without very robust signals from the institutions’ (mostly) joint owners.

Shoring up the core funding of norm-setting and global monitoring agencies. The SDGs depend in no small measure on the continued leadership of global standard-setting and monitoring agencies, especially, but not only, in key GPG areas, such as public health and veterinary standards, biodiversity and financial stability. There is a serious risk that reduced funding by historically important donors to parts of the UN system, in particular, will undermine this work and its continued progress. One positive way forward is that such agencies act more explicitly as the central membership-service body, funded mainly by earmarked levies

4 Systemic-contextual models are more familiar terms in the field of social psychology. We are indebted to Cyrille Bellier (personal communication) for making this connection.

from the corresponding budgets of the national public-goods departments operating in their area. It is unacceptable that so many national funders of development and GPGs should rely on the work of these norm-setting and monitoring agencies, but then ‘free-ride’ by refusing to pay adequate contributions to sustain this core work – a version of the ‘tragedy of the commons’. In exchange, these global agencies should refrain from fragmenting themselves by launching multiple non-core fundraising initiatives, and recognise that others in the development industry may offer more effective technical assistance at the country level, based on the standards the apex body develops; they should not attempt to do everything themselves.

Key policy recommendations

- 3 Development agencies must invest more up-front in identifying and assessing DevTech prospects, and be selective about which to support, why, and how.
- 4 The owners of the MDB system must urgently consider balance-sheet optimisation alternatives, overall and in specific thematic areas, which can greatly expand their operations while taking on prudent levels of additional risk.
- 5 Core standard-setting and monitoring functions of specialised international agencies should be protected financially, including via a more robust system of earmarked levies on the GPG budgets of their national member departments.

2.3. The combined conflict, refugee and migrant crises and their effects

The third meteor is **migration and refugees**, a fusion of previously separable concerns with conflicts and their cumulative displacement consequences; the ‘mobility transition’, encouraging economic migrants from developing to developed countries; and last, and most toxic, hardening attitudes to migrants in developed countries, either on ‘objective’ grounds of limited absorption capacity, or prompted by baser emotions. In terms of impact on the aid industry, paradoxically, the argument that aid can staunch migration has never sold better politically than in today’s context, even though it runs counter to current evidence. Mainly because aid can relieve some of the financial and information constraints on migration, the consistent finding is that aid to countries with an average income of below approximately \$7,000 actually encourages it. A more sophisticated approach to restraining migration needs to recognise the importance of non-aid policies, such as those related to visa restrictions, asylum-seeking and temporary employment, and to work more systematically with stable countries of first displacement.

2.3.1. Genesis – a toxic mix

This meteor was to some extent visible in 2012, after the so-called Arab Spring, arguably in the form of three distinct challenges that have since effectively combined into one, and also interact with populist politics in ways we had not considered.

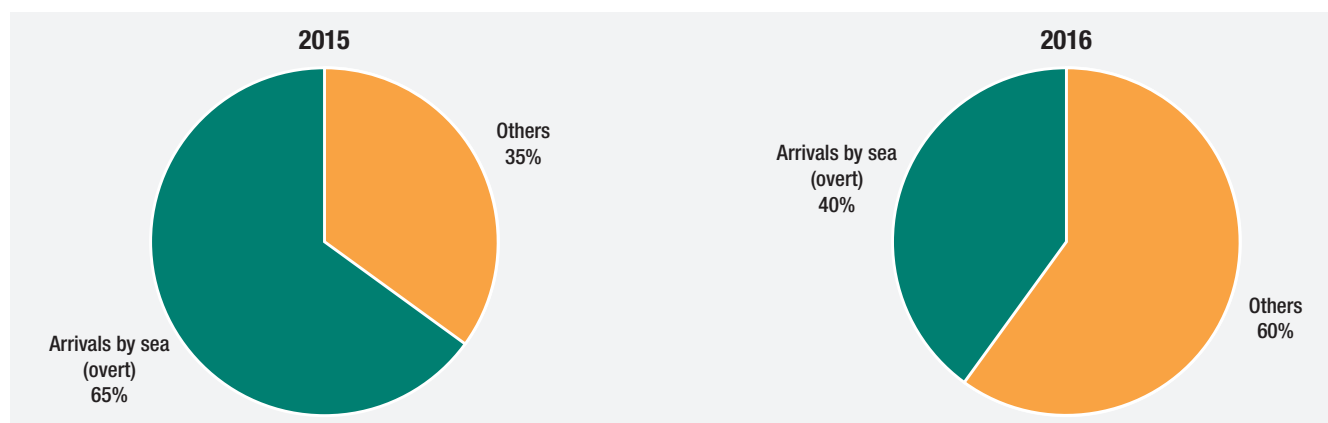
The first is the international community’s repeated failure to prevent, or speedily help bring to a close once under way, **violent conflicts**, especially but not only in the Middle East and Central Asia. This includes disputed and at least partially unsuccessful external military interventions and their bitter aftermath, and the ramifications of extremism, not justified but certainly fuelled by such grievances, both within and far beyond the conflict zones. The nature of conflict has changed, with a greater role of non-state actors and greater systemic risks posed by the emergence and empowerment of cross-border, sometimes ‘virtual’, destabilising movements. The lack of effective development cooperation responses to state fragility, noted above, may have made a modest contribution to this. However, one of the lessons of the Arab Spring was that fragility – the chronic condition ultimately leading to state break-up – can also affect MICs and even UMICs with apparently robust institutions. This raises the challenge of ‘state-building’ to a whole new level of complexity. (A different, growing, and so far much less discussed, threat of mass displacement comes from climate change-induced population movements, whose power and frequency we are still only dimly able to visualise. These potentially link climate change and migration challenges in explosive ways. Climate change is discussed in the next section.)

The second component, partly linked to the greater duration of major conflicts, and therefore the larger cumulative scale of the attendant family displacement and humanitarian costs, is **substantial refugee flows**. These are still relatively concentrated by origin – 55% of refugees are currently from Afghanistan, South Sudan and Syria, and 86% are still mostly located in LICs and MICs (UNHCR, 2017). In the Syrian case, displacement tends to involve relatively skilled adults and youth, who increasingly have an indeterminate time horizon, and form an exceptionally high share of the resident population in nearby countries (9% of registered Syrian refugees relative to the Jordanian, and 17% to the Lebanese population (ibid.)). (For an informed perspective on their ‘displacement life histories’ see Bellamy et al., 2017.) Sustainable new livelihood opportunities in the countries of first arrival are low to non-existent, increasing the likelihood that the more resilient and mobile migrants will try to move on quickly from such staging posts, towards developed economies, particularly EU Member States. Some take their families, but many do not in the first instance.

Global refugee numbers are back to their 1990s’ peak of about 20 million, from a recorded low of 13 million in 2005 (World Bank, 2017b).

Overall refugee arrivals in the EU are expected to fall in 2017 compared to 2016, as they did from 2015 to

Figure 7. EU migrant arrivals by sea and other routes



Source: Massa, 2016a

2016. This may be partly a reporting quirk, as many more are likely to be entering via ‘covert’ channels, including overstaying student visas as well as using circuitous land routes, counted among ‘others’ in the orange section of Figure 7. It is also possible that new refugee arrivals will soon start to ebb, but migration pressure overall will remain high. For example, reported sea arrivals in Italy in the first half of 2017 (85,000) are 19% above the number for the same period in 2016 (*Financial Times*, 2017). What these short-term shifts also illustrate is the considerable volatility of migration routes and volumes.

Refugees, and particularly males of working age, therefore increasingly merge with pre-existing ‘economic’ migrant flows from LICs, especially in Africa, where conditions may not be quite so violent but are still dismal, meaning that the relative pull effect of high-income countries is just as strong, if not stronger. These flows had been falling in the immediate aftermath of the post-2008 global economic recession, but have since started to rise again – they tend to correlate with economic cycles in the major destination countries. Refugee/migrant counts are also complicated by international rules governing asylum (such as the Dublin Agreement in the case of the EU), which force claimants to stay in crowded points of first entry, rather than being able to move on in search of better prospects. In reality, the distinction between refugee and economic migrant, vital though it may be in human rights terms, is fast breaking down. By current estimates (Massa, 2016), the largest national origin recorded in 2015 at Italian sea arrival ports was, by far, Nigeria. The second was Eritrea, with its more obvious association with refugee movements and its unique colonial history.

Restricting migration policies in the destination countries can have powerful and sometimes perverse effects on such numbers. If legal migration, such as student or tourist visas, is hardened or barred altogether, many who have already entered through those routes will not risk leaving, potentially raising net migration numbers, and some of those barred from legal routes may resort to

more tortuous ones, raising private and public costs and potentially endangering lives (Marta Foresti, personal communication).

The third component is **anti-migration sentiment** in destination countries. There is mixed evidence about its relative strength and recent evolution, behind the headlines. Analysts point to a growing ‘anxious/conflicted’ middle ground across Europe, sandwiched between roughly equal welcoming and hostile segments (Dempster and Hargrave, 2017). Attitudes to migrants are also now intertwined (ibid.) with wider anxieties about globalisation (see section 2.1). Civilised ‘liberal’ political discourse tries to distinguish between legitimate migration concerns, based on economic, social and cultural absorption constraints – the inability of social services, housing and the community and cultural fabric to adjust quickly enough to large migrant surges – and less palatable ones, based perhaps on underlying xenophobia, though the boundary between the two is quickly crossed. More recently, a fear of imported extremism has been added, irrational though that may seem when most terrorists prove to be home-grown, even if sometimes radicalised remotely.

But the resulting opposition to migration is equally real now, regardless of motive.

It is increasingly impervious to evidence of the economic costs of restricting migration, such as risks of skills shortages arising from lower US visa quotas for Indian migrants hampering the IT sector in California, for example, or the negative effects of fewer students and researchers coming to the UK. It also ignores the technically, if not politically, accepted net fiscal benefits of skilled economic migration (which should in theory allow destination countries to finance ‘corrective’ social infrastructure to mitigate absorption constraints). Ironically, such restrictions might eventually lead to the perverse result of more, rather than fewer, business processes and jobs moving abroad. A Balkanisation of EU external migration approaches, if it came to that, would likewise seriously – some argue fatally – damage the

once-borderless internal market. The EU's failure to be seen to have a workable immigration policy, and harrowing pictures of everyday tragedies around its borders, has in turn contributed powerfully to damaging its image in the eyes of voters. There is, therefore, a risk that anti-migration sentiment, by engendering bad policy and consequent economic self-harm, could become self-perpetuating.

Meanwhile, otherwise sensible proposals to expand skilled migration quotas from developing countries for win-win benefit, such as those of Clemens and Postel (2017), are unlikely to find receptive political ears in this context, even though they could offer higher investment returns than providing additional international aid.

2.3.2. Implications for the aid architecture

So this meteor is already big and potentially dangerous, but can it be slowed or diverted with some help from 'development' forces, and especially aid? And, if so, with what consequences for the aid industry?

A basic fallacy. The irony is that using aid to prevent, or slow, migration from LICs and MICs to rich economies is an idea that sells well politically, but does not work in practice. If anything, aid is associated with *rising* migration flows from developing countries until they reach UMIC status (at around \$ 7,000 per capita, on a purchasing power parity basis) (see, for example, Parsons and Winters, 2014).

Reviews of what leads to this inverted-U-bend of 'mobility transition' as countries develop (Clemens, 2014) reveal the importance of credit and information constraints, among other factors, in initially holding back emigration, hence the likely role of aid in relaxing both. For lower-paid workers, relatively small financial stakes generated by external assistance, including cash-benefit programmes, can help tip the scales towards being able to afford to migrate. For higher-skilled migrants, networked information on opportunities and conditions in the destination country and connections with the resident diaspora can make the difference, and these links are often associated with bilateral aid.

Triangular schemes and working through UMICs. Many of those displaced or migrating from LICs and MICs alike, to more stable and prosperous neighbouring countries, will soon move further afield, especially if local labour regulations and other restrictions stop them from integrating in the country of first arrival, as discussed earlier. This point is well illustrated by the quandaries facing donors struggling to stabilise a rapidly deteriorating refugee situation in the Middle East. Vast numbers of Syrians settling in Jordan and Lebanon were threatening to overrun these countries' systems. In 2014, the risk of destabilising spillovers was considered to be high. But due to graduation rules, neither country was eligible for grants

or concessional loans from the World Bank Group or other agencies because they are listed as UMICs.

In the event, a creative solution has been found by using concessional loans to Jordan and Lebanon to create special economic zones (SEZ) to permit local citizens as well as refugees to find productive employment in industries enjoying export trade preferences to the West. Issues of graduation were made subservient to issues of assisting people in desperate straits and of preventing social instability with its attendant risks of additional conflict from spreading to Syria's neighbours.⁵

This is an illustration of a bigger strategic challenge. Rigid rules are being tested by a rapidly evolving global context in which national income levels are no longer a good proxy for where to allocate resources. The toughest issues arise with the pursuit of GPGs and with aid for mutual benefit. In both these instances, MICs, and often UMICs, may be important partners. Sometimes the two overlap.

Similar arguments have been advanced to support aid to MICs for climate mitigation, and pandemics and infectious disease control. The question of appropriate burden-sharing of course arises, but this differs according to the issue being addressed; it may be linked to past history (as in climate change or overfishing), to current activities, or to reasonable dimensions (affordability of, say, treatment for HIV and AIDS).

Aid for mutual strategic purposes can also involve MICs; think, for example, of recent agreements between Indonesia and Australia, on the one hand, and the EU and Turkey, on the other, both directly involving responses to migration pressures.

Tensions regarding MIC aid allocations are not new but are newly pertinent. In 2005, aid from all donors to UMICs was around 30% of ODA net disbursements and it seemed sensible to reduce this level. By 2015, UMICs accounted for just over 10% of ODA receipts. For donors moving to priorities other than pure altruism, this may be a shift too far. But what is the right level? Given the uncertainty in global conditions we do not believe that it makes sense to codify any given percentage of aid to UMICs. Rather, we favour a softer approach, which could be termed 'gradation', that accepts the desirability of a decline in aid as recipient countries become wealthier, but that can permit different aid allocations as conditions and motivations change, especially where there is a strong GPG dimension.

Upstream assistance and prevention. We have already discussed conflict prevention and effective responses to underlying fragile situations, which have an enormous, though uncertain and lagged, potential investment payoff. Unfortunately, few development agencies are either sufficiently equipped or incentivised to help delay or shorten civil strife as a core goal, as opposed to

5 This type of migrant integration approach is not limited to UMICs. For example, a considerable fraction of Eritreans displaced into Ethiopia, a fast-growing country on the cusp of LMIC status, might be willing to settle there under similarly improved conditions, brokered with donor support (Mallett et al., 2017).

providing humanitarian relief or longer-term ‘development’ programmes after the fact. The costs of humanitarian assistance have been rising steadily as a share of ODA (from 10% to 15% between 2010 and 2015), so that the share of proactive ‘aid’ is falling in relation to reactive responses. This spending is not limited to responding to conflict situations, of course, and includes relief for natural disasters, for which similar arguments are made – that we chronically underinvest in preparedness and hence have to invest in remedial action. For some categories of quantifiable risks, insurance-based approaches like the World Bank’s recently launched Pandemic Disease Facility (World Bank, 2016a), are clearly the way forward. The underspend is partly also because many agencies still compartmentalise humanitarian and ‘development’ responses, although the duration of humanitarian emergencies continues to lengthen so much as to progressively blur the practical distinction between them.

Immediately downstream is support to refugees in neighbouring countries, for which budgets have grown enormously, especially in the US and UK, and for which innovations in blended finance have recently allowed development banks to provide subsidised loans, as discussed above. On the one hand, such approaches enable aid to be delivered in bulk to family units in large supervised settings (camps), although a growing proportion of refugees (perhaps half) no longer live in these camps. It can also be argued politically to be an effective way to use aid to relieve onward migration pressures on high-income countries (HICs) further afield. It could be, and occasionally is, linked to earlier and faster treatment of their applications before asylum seekers embark on even more perilous journeys. But the corrosive effect of limited work and integration opportunities in the initial host countries, and some perverse incentives for countries receiving support for refugees on a per-capita basis, can partly undermine the intended effect. Equally, proponents of third-country schemes need to work with the grain of political sentiment in the relevant countries, which argues for significant burden-sharing by HICs, without which limits to absorption and to the community consensus will quickly be reached in the former, just as they may have been in the latter. There are already instances of MICs’ migration policies being influenced by those of developed countries (Hargrave and Pantuliano, 2016).

This leads to the next phase of expenditure: safe passage across land and, especially, sea borders – an astonishing mix of huge private outlay for smugglers (a large multiple of air fares, which are blocked by visa restrictions placed on airlines) and substantial official and charitable outlay for rescue, with the unspoken, immoral and evidently unworkable, premise that the risk of death acts as a deterrent. Ironically, most of this component does not count as ODA – if it did there might be some discussion on how to allocate funds more efficiently, as well as more humanely.

Finally, we come to **refugee costs absorbed by countries of ‘final’ destination**, such as Germany, and their partial scoring under ODA.

Proportionately within the DAC the latter share is especially significant for Switzerland (refugee costs amount to 17% of ODA) and Sweden (19%), and far less for countries like the US and UK (5% and 3% respectively) in 2016 (DAC, 2017). Currently, the DAC recognises only first-year costs and payments to refugees/asylum seekers in the ODA definition – a longer period or a broader cost pool would sharply raise the share at current migration levels. As it is, ODA overall, excluding refugee costs, is barely increasing (DAC, 2017). So fears that refugee costs will ‘crowd out’ other development aid are not unfounded.

Preliminary analysis of this prospect (SEEK, 2016) distinguishes some countries like Norway and Sweden, for which a single combined budget line established for development aid and refugees can lead to curtailment of the former to fund the latter, especially as their aid commitments as a share of GNI have reached a plateau. This compares to the case of others, such as Germany, in which ex-post reporting of refugee spending eligible for ODA (on a very limited basis compared to its huge overall refugee budget) is not fungible with the international development budget, so both elements are rising independently along with total ODA. A third group, including the UK, reports negligible levels of domestic refugee costs as eligible for ODA.

But the bigger picture is that destination countries currently report only a small fraction of their refugee expenditure as ODA, and that they have wide variations in both coverage and (sometimes by an order of magnitude) unit costs. Box 1 summarises recent ODI findings on this.

Box 1. European countries’ refugee spending is variable and inconsistently reported

- The UK and Italy experienced the highest per-capita reception and procedural costs in 2015.
- Belgium, Germany and Norway provide the highest amounts per capita to cover basic needs, such as food, clothing and accommodation, among others.
- Denmark, Sweden and the UK pay the most in per-capita terms for refugee-related procedures.
- Germany, Italy and Sweden shouldered the highest overall costs in 2015.
- In several cases, officially reported costs are under/overestimated, in particular by omitting claim-processing, health and education costs.
- As a share of GDP, budgetary expenditures for refugees appear to be still manageable in the selected sample of European countries.
- The key recommendation is that European countries should use a harmonised framework to report on refugee costs.

Source: Based on Massa, 2016b

We strongly suggest that a whole-of-government approach to public support for all phases of the displaced person/refugee/migrant journey, or tragedy, whether scored as development aid or, more likely, under some new aggregate like IDC (section 2.1), would be a far better way to tackle this combination of challenges. This should start from a candid recognition that aid offers no simple solution for the many negative aspects of migration, from either the migrants' or the host countries' perspective, or both. This meteor will not be diverted easily.

Key policy recommendation

- 6 Refugee-targeted interventions through stable third countries illustrate the need for a more nuanced approach, which we call 'gradation', to providing enhanced loan support to UMICs when there are clear GPG arguments for it.

3. The snowballs

3.1. Poverty trends and fragility

‘There are people in the world so hungry, that God cannot appear to them except in the form of bread.’
(Mahatma Gandhi)

The first snowball is the profoundly changing **global poverty landscape**. Global poverty has fallen rapidly, as we anticipated in Horizon 2025, but we see an end to this trend within the next five years. By then, the vast pools of extreme poverty in Asia will be largely drained, while poverty will continue to rise in fragile states, mainly in Africa. By 2018, Nigeria will be home to the largest number of absolute poor of any country in the world and Ethiopia and DRC are not far behind. At the same time, however, the overall poverty gap has also shrunk, suggesting that it is now more affordable than ever to reduce poverty, especially if aid is complemented by stronger DRM. As a rough indicator, if developing countries spent just 1% of their GDP on effective

poverty-reduction programmes, leaving aid to fill the rest of the gap, the additional contribution required would be about 33% of present DAC aid. The main take-aways: aid advocates that today are celebrating the success in reducing poverty will very soon need new explanations of why global poverty-reduction efforts are falling short. They will also have to pay more attention to countries’ own efforts in mobilising resources and effective safety-net spending.

3.1.1. Sharply falling poverty rates – for now

The global poverty map continues to change fast. Much has changed since our initial paper was published in 2012. The methodology and definition of extreme poverty has been updated (Box 2), and new data reveal a different pattern. The measures of income and consumption derived by the purchasing power parity exercise conducted in 2011 suggested that households in Africa and Asia were far richer than had previously been thought, by 18–26% in several cases (Deaton and Aten, 2015).

Box 2. Methodological and definitional changes in poverty

Since 2008, poverty has been measured by the World Bank as the number of people living below \$1.25 a day in 2005 purchasing power parity terms. In October 2015, the World Bank set a new threshold for extreme poverty at \$1.90 per person per day in 2011 purchasing power parity terms. The Bank explains the change in terms of the evolution of prices across the world. It took the national poverty line in 2005 in each of the 15 poorest countries, adjusted it for inflation in each country to arrive at a 2011 national currency poverty line, and then used the 2011 purchasing power parity exchange rates to bring these lines into a common currency. It then averaged the new 2011 national poverty lines. The result was \$1.90 per person per day.

There is considerable debate on whether \$1.90 in 2011 is the same benchmark as \$1.25 in 2005. It would not be the case for the US, the benchmark country for the exercise, where cumulative inflation between 2005 and 2011 was 15%. A simple updating by US inflation would have generated a global poverty line of \$1.44/day. The concern with the World Bank approach is that it relies heavily on the consumer price index, notoriously one of the least reliable macroeconomic statistics, in some of the world’s poorest countries. In some countries, the implied 2011 national poverty lines look very high compared

to the lines used in other countries. In 2005, when the averaging method was introduced, most poor countries had very similar poverty lines expressed in purchasing power parity, so the choice of countries to put into the average did not matter too much. But with the updates, this similarity disappeared, raising questions about the selection of countries whose poverty lines would feed into the global averages. A different choice of countries would yield a very different average global poverty line. Large countries with considerable poverty, notably India, were excluded from the definition of global poverty.

It is important to understand the new methodologies and definitions because of their sizeable impact on global poverty numbers. We could have expected that measures of global poverty would be raised by the apparent increase in the global poverty line. But the opposite has happened. Global poverty appears to be far smaller than anticipated because most households seem to be richer according to the new purchasing power parity analysis. As conventionally measured, the global poverty headcount may now be around 650 million people (and far less than that if adjustments are made for the discrepancy between survey means and national accounts as we, somewhat controversially, did in our original report).

Changing poverty metrics do not actually reflect changes in the real living standards of anyone. But a further explanation for faster poverty reduction is strong rural income growth associated with rising global prices for agricultural commodities. The International Monetary Fund (IMF) food and beverage price index climbed by 83% between 2005 and 2011 before moderating in more recent years. This probably helped to reduce poverty because of its concentration in rural areas. Poor smallholder farmers benefited directly from improved terms of trade, and, in many cases, landless peasants also benefited thanks to stronger off-farm demand for their labour by rich farmers investing in upgraded housing and rural businesses.

Combining new definitions and new data, the basic account of a rapid fall in poverty driven by progress in non-fragile states remains unchanged. If anything, the shift in poverty towards fragile situations has become more marked. Fragility rather than country income level is the relevant lens for development agencies.

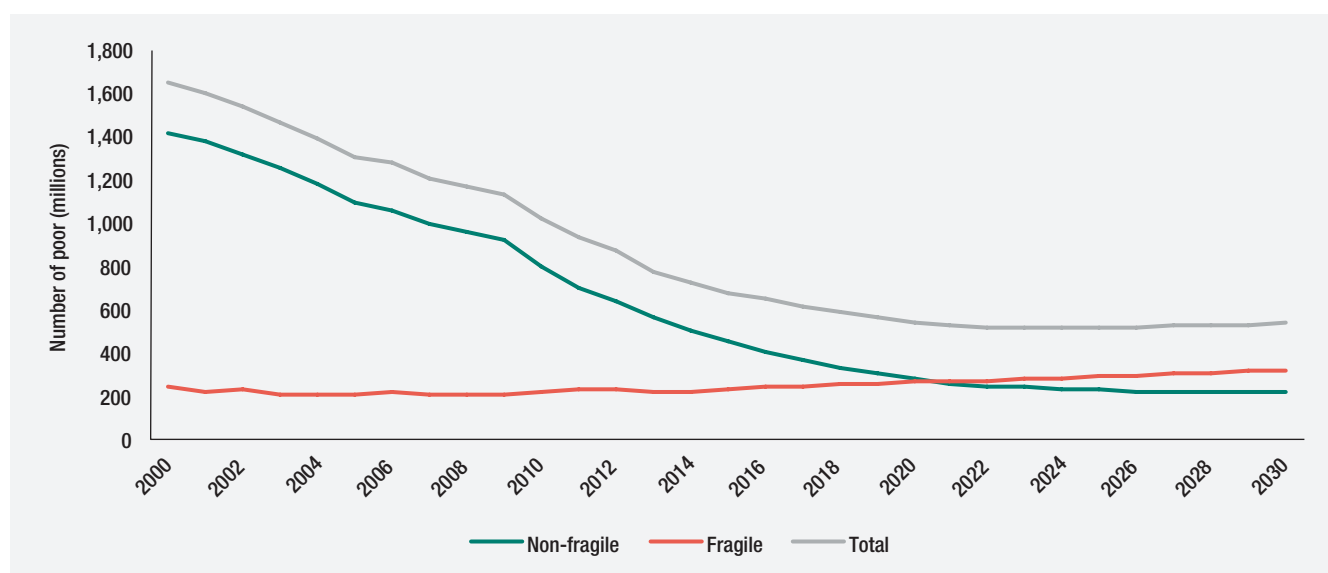
The continued rapid decline in poverty in non-fragile contexts has meant that the concentration of poverty in fragile contexts has increased even faster than we had anticipated. Already, poverty levels in non-fragile contexts, like India and Viet Nam, have fallen fast (despite well-known upward biases in Indian poverty reporting compared to other countries). As a consequence, Nigeria looks set in 2018 to become the country with the largest number of people living in absolute poverty.⁶ Other fragile states with large absolute numbers of people living in poverty include Afghanistan, DRC and Ethiopia.

The concentration of poverty in fragile contexts follows from three facts. Their annual economic growth is usually low, so there are few opportunities to escape poverty. Even when growth is rapid for a few years, it is not sustained, so the long-term average growth rate remains low; annual growth tends to be volatile, with any gains in one year offset by set-backs later, either due to conflict, natural disaster or other economic and political shocks. Long-term growth forecasts, therefore, either extrapolating from a decade of growth from IMF sources or using the shared socio-economic pathways developed by the International Institute for Applied Systems Analysis (IIASA) and the OECD for climate modelling, are also low. In addition, overall population growth in fragile states is higher than in non-fragile contexts, reinforcing the poverty dynamics. As Figure 8 shows, the number of extreme poor living in fragile states is rising and will soon exceed the number living in non-fragile states.

3.1.2. A shrinking gap between aid availability and need

A second trend we had identified in Horizon 2025 was the narrowing global poverty gap – the amount of money it would take to bring everyone above the poverty line with perfect targeting and no administrative costs. With the new understanding of lower global poverty rates, the poverty gap has fallen considerably. We now estimate it to be somewhere around \$75 billion per year, looking just at income poverty of those living on less than \$1.90 a day. This is a strikingly low number compared to global GDP

Figure 8. Rising poverty in fragile states could soon end global poverty reduction



Source: World Data Lab, 2017

⁶ Nigeria's household survey data is of problematic quality, so it is advisable not to put too much faith in these numbers; its household surveys capture only 25% of total household expenditure as measured by national accounts. One or the other is wrong, but we don't know which and by how much. Also, Nigeria has several different household surveys. For example, the World Bank in its internal reports uses a different survey than the official one available on its PovCal website. Here we follow the World Bank PovCal usage.

(just 0.1%). It suggests that innovative thinking on how to structure the provision of aid, perhaps through targeted social-protection programmes, could yield substantial benefits in terms of reducing poverty (more on this below).

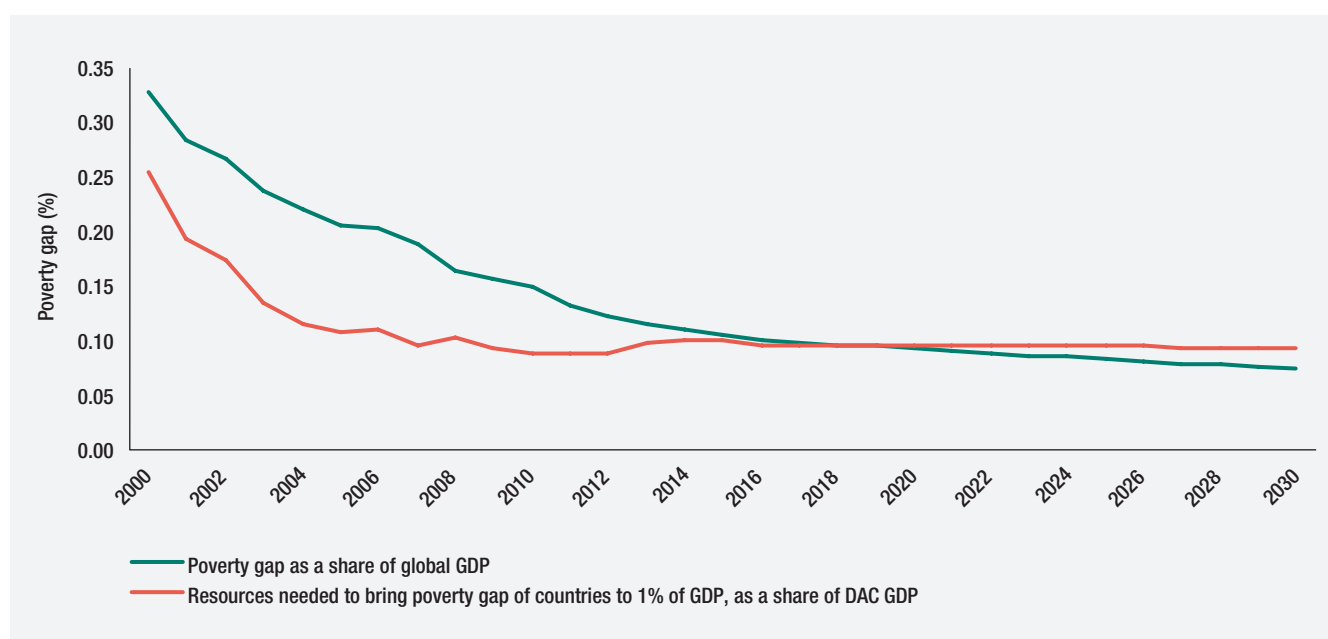
Of course, figures on the size of the poverty gap should not be confused with the cost of programmes to eradicate poverty. Leakage and administrative costs are significant and delivery mechanisms may be lacking in many places. Almost by definition the poorest of the poor are to be found among those who are isolated due to geography, caste, ethnicity, gender or lack of access to markets. They cannot be easily reached. Much poverty is also transient. There is a churn with perhaps one-third of the poor rising above the poverty line and a similar number falling below it each year. Brown et al. (2017) point to the practical difficulties with targeting households and the additional complications arising from the lack of most social assistance programmes to address intra-household inequalities. And income poverty is just one of many dimensions of poverty that need to be addressed. Nevertheless, the poverty gap is indicative of the overall magnitude of the problem. It also allows for a discussion on the 'fair' distribution of the burden between DRM and external aid.

DRM was a major theme of the Addis Agenda. It seems plausible that countries should be able to allocate at least 1% of their national income to new anti-poverty social assistance programmes. The rapid spread of bank accounts (700 million more account holders between 2011 and 2014) suggests that modern technology can allow some programmes, such as cash transfers, to take place with very low administrative costs. In India, for instance, digital IDs have been issued to over 1 billion people, removing a central obstacle to targeted programmes.

The gap to be potentially filled by aid becomes significantly smaller when DRM is taken into account. As a first approximation, we look at the size of the residual poverty gap if all countries allocated an extra 1% of their GDP from domestic resources to closing it, in addition to all existing spending programmes. We calculate that about \$45 billion (0.1% of DAC country GDP, or about a third of DAC ODA) would then fill the remaining poverty gap (Figure 9). Others have similarly pointed out the desirability of factoring in domestic resources, notably Ravallion (2009), who proposed looking at the upper bound of marginal tax rates. The point, however, is the same. Understanding the dimensions of the poverty gap is an important reminder of ambition. The \$45 billion amount would not 'solve' global poverty as there are administrative costs, targeting design and inevitable errors, and delivery mechanisms to be worked through, but it does suggest that aid should no longer be thought of as a drop-in-the-bucket of poverty needs. Instead, it could become a materially significant resource that, in combination with DRM efforts, could make a very large dent in global poverty.

Aid agencies have traditionally favoured narrow targeting of social assistance programmes, often in the form of in-kind delivery, as the most efficient use of scarce resources to reduce poverty. The problem is that targeted programmes do not enjoy widespread popular support and, historically, have not been scaled up. A poor–middle-class alliance that delivers a package of social insurance and social assistance is more likely to offer greater absolute benefits to the poorest, even though the bulk of such programmes is allocated to richer quintiles. Aid agencies can now afford to reconsider their approach to targeting, recognising that from a political economy perspective universal programmes are more sustainable (Desai and Kharas, 2017).

Figure 9. A shrinking poverty gap 2000–2030



In absolute terms, the poverty gap has narrowed steadily every year for decades. This trend is now changing and the poverty gap may already have bottomed out. As Figure 9 shows, the poverty gap continues to reduce slowly and is now only about 0.1% of global GDP. But our calculations suggest that the poverty gap could soon start to increase, even though the number of people in extreme poverty continues to fall. This is because a dozen countries are now experiencing negative income growth per capita and are expected to have lower per capita spending in 2025 than in 2015. There are already over 100 million people living in poverty in these countries, but with the combination of negative per capita income growth and continued population growth, this number is growing by about 4% per year.

Despite much talk, however, the aid industry has not really responded to fragility in any meaningful way. An independent review of the New Deal – the set of principles developed through the International Dialogue on Peacebuilding and Statebuilding – concludes: ‘Implementation of the New Deal so far has not been easy, reflecting a need for political leaders to recommit to the principles of the New Deal. This is especially true for political processes that bind all relevant actors into a shared vision for “what” needs to be achieved and “how”.... the fragmentation of aid and development partners across the SDGs, and growing pressures on humanitarian aid, could make matters worse in the SDGs era... This is why partners should commit to a New Deal for the New Deal’ (Hearn, 2016). This is simply a polite way of saying that the New Deal is not working and is not being taken seriously enough by major players.

3.1.3. Africa

The third theme of the shifting poverty map is the concentration in Africa, where over 400 million people,

two-thirds of the world’s poor, live. By 2025, Africa may have even more people living in poverty than today, given current growth prospects, while the global total will hopefully have shrunk. Africa could by then become home to 80% of the world’s extreme poor.

Our thinking in Horizon 2025 was that this would inevitably drive a reallocation of resources towards Africa. Unfortunately, the reverse has happened. Poverty in Africa has indeed risen, but aid flows have not followed. In 2015, ODA from all donors to sub-Saharan Africa (SSA) was \$42.9 billion compared to \$45.5 billion in 2011.⁷ The 14th replenishment of the African Development Fund (\$7.08 billion for 2017–19), the only multilateral concessional fund specifically dedicated to African development, was lower in nominal terms than the previous replenishment (\$7.3 billion). The Gleneagles (2005) promise to focus aid on Africa seems very far away.

3.1.4. The end of a story – and the start of the next

It has become a matter of principle for development proponents to highlight the indisputable massive reduction in poverty over the years. The World Bank’s 2016 *Poverty and Shared Prosperity* report notes that 1.1 billion people have escaped poverty since 1990. Max Roser, an economist at the University of Oxford, put it starkly in a recent tweet, “Number of people in extreme poverty fell by 130,000 since yesterday” should have been the headline every single day in the last 2 decades’.

Coincidentally, 130,000 people per day works out to 1.5 people per second and this is exactly the average speed of poverty reduction that is required to reach the Agenda 2030 goal of eradicating poverty by 2030. Hence, there is some cause for celebration. On the surface, we appear to be on track for meeting Agenda 2030’s most important goal.

Table 1. Sub-Saharan Africa now receives less net ODA (millions of current US dollars)

	2011	2012	2013	2014	2015
Europe, total	8 944	8 083	7 456	8 632	6 847
Africa, total	51 592	51 765	56 805	54 299	51 210
South of Sahara, total	45 507	45 028	46 093	44 445	42 852
America, total	11 509	10 097	10 292	10 015	10 109
Asia, total	38 091	33 516	44 566	54 009	45 572
Oceania, total	2 242	2 191	2 165	1 881	1 914
Developing countries, total	141 755	133 671	151 165	161 705	152 603
Sub-Saharan Africa (% developing countries total)	32.1%	33.7%	30.5%	27.5%	28.1%

Source: DAC 2a, extracted 23 May 2017

7 If anything this flatters the progression of programmable ODA to SSA countries as a growing share of ODA to Africa is made up of regional or non-country-specific programmes.

The problem, not surprisingly, is that past performance is no guarantee of future performance. Thanks to slowing growth in many developing countries (section 2.1), as well as the fact that the poverty counts of the large masses of poor people in China, India, Indonesia and Viet Nam have shrunk so far already, the future pace of poverty reduction has already slowed and is expected very soon to slow further.

In 2017, the speed of poverty reduction is estimated at around one person per second (net), meaning that every day just under 100,000 people are escaping poverty (World Data Lab, 2017). Under current growth trends, as forecast by the IMF, however, within two years the speed of poverty reduction will have fallen to 0.8 people per second, while the speed needed to eradicate poverty will have risen to 1.6 people per second (the required speed rises because the shortfall on progress since 1 January 2016 has to be made up). In other words, by 2019 we will only be making progress at half the required rate to achieve SDG 1. By 2025, poverty reduction might have fallen to one person every five seconds. Thereafter it might stop altogether, and even begin to rise again slowly (Figure 7). This will be a quite different narrative.

The main take-away: aid advocates that today are celebrating the success in reducing poverty will very soon need new explanations for why global poverty-reduction efforts are falling short. These narratives must address how aid is helping people in the places that are hardest to reach.

Given the usual ‘what have you done for me lately’ political discourse, the evidence that aid agencies will need to provide to overcome aid fatigue will have to focus on its impact on addressing poverty in fragile states, or on reducing the flow of refugees (see below). Neither is an easy explanation to justify. Aid agencies will need to start preparing now.

3.1.5. Implications for the aid architecture

Some donors are indeed now building up a new narrative on fragility. Fragility was included as a special theme in the most recent International Development Association (IDA) replenishment (IDA 18), and one of its most tangible outcomes was the creation of a special set-aside for refugees in MICs. Elsewhere, there are encouraging experiments with cash transfers, both conditional and unconditional, but more research is needed about the most effective design (ICAI 2017).⁸

So motivation to act is arguably high, but what to do, and what works, is less clear – rather like the case of using aid to reduce migration pressures (section 2.3), though there is even less evidence of good practice in the latter case.

With slow or negative per capita growth in fragile states, there is more impetus to put in place cash-based social assistance to reduce poverty. Indeed, in many countries, ideas of a Universal Basic Income have been mooted. There is debate on whether this is a more effective way to reduce poverty compared to the provision of public goods and basic education and health services, but the speed with which the concept has grabbed attention (albeit with different definitions) suggests it has tapped into something significant. Aid agencies can help in three ways: (i) they can help develop the new technology frameworks for delivering cash, in the form of smartcards or more sophisticated digital IDs, like India’s Aadhar system; (ii) they can advise countries on mechanisms for channelling domestic resources into such programmes while avoiding adverse selection and moral hazard problems (particularly important for resource-rich states); and (iii) they can fill the gap in resource requirements, especially in the poorest countries.

How is fragility defined? Perhaps the first point is that fragility is itself a heterogeneous concept, incorporating countries in conflict, those that have been hit by natural disaster and those that simply have bad or corrupt governments, despite often having sophisticated institutions, democratic ones excepted. Understanding fragility, and tailoring approaches to different circumstances, is key.

Unfortunately, there is no consensus on how to identify a fragile state. One commonly used approach by the World Bank and other MDBs is to measure country policies and institutions on a cardinal scale and to define fragile states as the set of countries that fall below a given threshold. Another, broader, definition is used by the OECD. This combines the World Bank list with that developed by the Fund for Peace, a non-profit organisation that undertakes a conflict assessment for 178 countries around the world based on judgments about economic, social and political stresses.

We prefer a results-based measure of fragility. In our view, fragile countries are best thought of as those where poverty prevalence is high and where the rate of improvement is slow. This definition mostly overlaps with the OECD one, but is simpler to measure and is more directly operational for aid agencies.

Institutions and centralised civil registration are also key. All fragile states have one thing in common, even if that feature does not adequately define them as a group. Their institutions are weak. Institution-building is therefore a favoured option for donors. Such programmes also tend to be relatively cheap compared to, say, building infrastructure. But with a weak human capital base and/or festering social and political divisions, building institutions is not easy and a donor must be prepared for a long-term engagement, and

⁸ Some organisations, like BRAC, combine weekly stipends with hands-on entrepreneurship training, health care and other interventions in a package approach. Others, like the private charity GiveDirectly, are experimenting with lump-sum cash transfers versus guaranteed basic income flows. These trials will provide the evidence base for scaled-up programmes in the future. They are perhaps the best hope for reaching the ultra-poor who might be left behind by economic growth, natural disaster or conflict. Aid agencies should pay close attention and help countries to scale up programmes that work.

a high risk of failure, to make a real difference. This risk of failure will become more concentrated as operations shift increasingly towards fragile states, and more frequent scandals (on corruption, waste and/or human rights violations) will in turn damage public support for aid – which therefore ideally needs to be politically prepared for a long-term effort, punctuated by unsettling reversals. Not an easy sell.

Using aid to fragile states as an allocation tool would favour a stronger focus on sub-Saharan Africa. Paradoxically, two of the largest African fragile states, Nigeria and DRC, have high poverty levels alongside enormous natural resource wealth. These are particularly fruitful situations in which to explore institutional innovations like cash transfers. Such programmes, however, cannot be instantly put in place. They need institutional preconditions, notably civil registration (civil registration and vital statistics (CRVS) in the jargon), which is the prerequisite for effective delivery of social services and much else. Making this universal is a concrete intervention that aid agencies can get behind. Perhaps boring for a political story, but vital for talking seriously about results.

More joined-up use of the multilateral system in fragile contexts. This arena of fragility and resilience at the country level has egregious institutional gaps and overlaps, but also some major opportunities which could be seized. How many concurrent institutional approaches are needed, or defensible, to assist the same fragile state? Could a unified multilateral platform not serve it better? If so, what might bringing the UNDP and World Bank, for example, together more closely look like? Such questions have been asked for years, but new urgency may be instilled by the severe budget pressures (section 2.1 above) under which many grant-dependent multilaterals will be labouring over the next decade. Merely continuing the present practice of expanding the search for ‘non-core’ or ‘multi-bi’ financing for special country (especially conflict-recovery) situations may not be sustainable much longer, so some more innovative and/or radical solutions may be needed.

Key policy recommendations

- 7 Improve funding allocations to fragile African states, in line with global poverty shifts, until new domestic resource mechanisms can be built up: prepare donor public opinion for the long haul, and for frequent setbacks.
- 8 Focus on ‘boring’ institution-building essentials: prioritise CRVS as an ubiquitous springboard for basic services, and insist on more joined-up collaboration between the major UN and MDB bodies in fragile contexts.
- 9 Experiment with universal cash-based social assistance programmes based on digital technologies.

3.2. Business comes to the table

The second snowball is **enhanced engagement by the business community**, based on their core business motives. These come over and above the impact-philanthropy approaches which we covered in 2012 and have grown since, albeit not spectacularly so. The debate about the boundaries of business responsibility for sustainable development has a long and chequered history: the pendulum is swinging again towards recognising major win-win opportunities, especially, but not only, in green technology. Nowhere in development is the role of business more eagerly anticipated than in the provision of infrastructure. New investment in infrastructure projects with private finance rose from \$40 billion in 2002 to around \$220 billion in 2012, largely in the telecoms and energy sectors. Since then, the numbers have collapsed, reaching less than \$30 billion in the first half of 2016. In part, this reflects tougher post-crisis regulatory standards on bank financing. The blended finance story is complicated further by the missing catalytic role of the MDBs, despite rhetoric to the contrary. In the first half of 2016, MDBs supported only \$1.2 billion in infrastructure projects with private participation. This resulted both from depressed country demand for credit and supply-side restrictions on the MDBs’ equity base and/or fiduciary ratios. The emergence of business interest in development is a double-edged sword for aid agencies. Without engaging, they lose the opportunity to scale up impact. With engagement come risks of erosion of trust and the potential for scandal. Neither prospect is appealing.

3.2.1. A shift towards core business motives and instruments

In Horizon 2025, we thought the main drivers of private-sector engagement with the ‘bottom of the pyramid’ would be private philanthropy and the charitable parts of business, namely CSR programmes and social impact investments. We believed the combination of money and technological innovation in these partners would undermine the comparative advantage of aid providers seeking to deliver social services through government channels.

We’ve not been disappointed in the growth of private philanthropy and social impact investment. The latest data on private philanthropy shows at least \$64 billion from DAC countries (compared to \$137 billion of ODA from these same donors (Hudson Institute, 2016)). In some countries, notably the US, private giving (\$44 billion) outstrips official aid (\$33 billion). Ten years earlier, US private giving, using the same methodology, was estimated at \$24 billion, compared to \$20 billion in official assistance.

Despite the vagaries of stock markets and budget deficits, it looks as if the trend towards faster growth in private giving compared to official aid remains. Private philanthropy has taken its place as a major player in development financing, but it is perhaps less overwhelming

than we had predicted, with considerable promise as yet unmet. For example, despite all the talk, only two social impact bonds have been issued in developing countries.

The other elements of private giving, through the business sector, have also continued to grow. CSR efforts are included in the private philanthropy estimates cited above, but social impact investments are not. The Global Impact Investing Network identified \$77.4 billion in assets under management in 2015, with about one-half in developing countries. About \$15 billion per year in new deals are being committed (half in developing countries), but the growth in market size has been modest.

The novel feature is the interest being taken by the business community and by private financial investors and fiduciaries. Of 1,000 CEOs surveyed by the UN's Global Compact, 90% are personally committed to ensuring their company leads on the sustainable development agenda, 87% agree the SDGs provide an essential opportunity for rethinking business strategies, and 80% feel that a purpose-driven commitment is a key element of competitiveness in their industry. The mantra today is that business is shifting from CSR to embedding sustainability into core business practices – and in so doing firms will contribute more to the development agenda.

While the statistics above are eye-catching, there is reason to be cautious about a business-driven sustainability revolution. The OECD believes that only \$27 billion of private money was mobilised by official development finance interventions (and hence specifically oriented towards development purposes) and, of this, 75% went to projects in MICs.

3.2.2. A sustainability revolution in business?

One visible sign of growing business attention to sustainability is a letter issued in May 2017 by 30 CEOs of major US businesses. These companies argued (although with little impact on the Trump administration) that US participation in the Paris Agreement would support investment by setting clear goals which enable long-term planning and would encourage market-based solutions and innovations. The letter was one of the clearest signals of an alignment between corporate and sustainable development interests.

The argument that what is good for business is good for development has been best articulated by the Business and Sustainable Development Commission (2017). Its report analyses four main economic systems to review the overlap between making profit and doing good – and the conclusion is that there is a \$ 12 trillion opportunity in food and agriculture, cities, energy and materials, and health and well-being. In these four areas, the Commission

report identifies 60 sub-sectors where business can do more to build sustainability into production. Many are traditional private-sector markets – reducing packaging waste, electric vehicles, end-use steel efficiency, and advanced genomics, for example. But others are in areas traditionally dominated by aid agencies and governments – forest ecosystem services, urban public transport, energy access, better maternal and child health. These examples of business seeing profit opportunities in traditionally 'development' areas offer the prospect of scaling up development impact in a way that could never be envisaged by reliance on public-sector (domestic and international) efforts.

But is it the business of business to contribute to the SDGs? This long-standing debate is entering its ninth decade. Adolf Berle and Gardiner Means recognised in the 1930s that 'the organizations which they [the few people in control of giant corporations] control have gone far beyond the realm of private enterprise – they have become more nearly social institutions' (Berle and Means, 1932), but went on to argue that corporate executives should solely consider the financial interests of shareholders. E.M. Dodd advocated that corporations should also take responsibility for their local communities. A generation later, in the 1950s, Berle himself had come round to this point of view, believing that without corporate intervention, governments would strive to address social ills in a less efficient and costlier way.

The echoes of Berle's conversion are being heard again today with about the same time lapse. This year is the 30th anniversary of the Brundtland Report, which called on business and government to adopt sustainability. An impressive number of business leaders have signed up to the concept, in one way or another. Institutional investors are reasserting control over companies in which they invest by becoming passive investors, but active owners. Business schools have published a growing body of empirical evidence linking better long-term corporate financial performance with greater attention to sustainability in a number of dimensions.⁹

Echoing some of these debates, there remains a suspicion that business will not pursue sustainability aggressively, preferring voluntary standards and anecdotes of doing good to responsibility embedded in government regulations. Without clear codes of conduct, business leaders are suffering a collapse in trust. The Edelman barometer for 2017 suggests that only 37% of respondents worldwide believe that CEOs speak with credibility, and the numbers are worse in emerging economies than in developed ones. Whether business will be seen as a valued partner or a development obstructor is still an open issue.

⁹ Meta-analysis studies that have reviewed over 2,000 individual academic research papers find over 90% show a positive relationship between environmental sustainability and financial performance at firm level (Friede et al., 2015). These studies almost exclusively focus on firms in developed countries, and data limitations weaken the case. Quantitative studies require a ranking of a firm as to its 'sustainability'; but there are no established standards for undertaking such rankings in a comparable fashion. Firms also change over time. For example, BP moved towards 'beyond petroleum' and then back to being a fossil-fuel focused company. Should it be ranked as a company with strong focus on sustainability or the reverse?

3.2.3. Blended finance

Nowhere in development is the role of business more keenly anticipated than in the provision of infrastructure. For a couple of decades, the private provision of infrastructure has been a dominant theme in development. Total investment in projects with private finance rose from \$40 billion in 2002 to around \$220 billion in 2012, largely in telecommunications and energy. Since then, investment has collapsed to \$71.5 billion in 2016. In IDA countries, only \$2.9 billion was committed to infrastructure projects with private participation in 2016 (World Bank, 2017a).

In part, the collapse of private participation reflects the tougher standards on bank financing imposed since the global economic recession. Regulators have reduced incentives for risk-taking so there is now a ‘triple whammy’ of regulatory hurdles on private financing of infrastructure – each characteristic of ‘developing country’, ‘long-term’, and ‘infrastructure’ is seen as adding a layer of risk. Commercial bank cross-border financing for such projects has, not surprisingly, collapsed.

Aid agencies are trying hard to swim against this tide. Brave comments about de-risking (or more commonly risk-shifting) must contend with a basic economic reality – current regulatory hurdles raise the opportunity cost of investing in infrastructure to levels that preclude the bankability of many projects. And when projects do go ahead, if the services remain unaffordable they can add to social inequities.

The blended finance narrative is complicated further by the insufficiently catalytic role of MDBs. In the first half of 2016, MDBs supported only \$1.2 billion in infrastructure projects with private participation.¹⁰ MDBs are uniquely positioned to advance private participation in infrastructure (PPI). They can provide policy and technical support and apply due diligence on social and environmental standards to de-risk projects. They can intervene at the highest level of government when re-contracting is needed (and this is a ‘when’ not an ‘if’ in most cases). They are preferred creditors whose projects usually enjoy strong government support. If MDBs do not scale up, the potential for PPI will remain just that – a potential, not a reality.

The reasons for limited MDB engagement relate to both supply and demand. On the supply side, the largest MDBs, such as the International Bank for Reconstruction and Development (IBRD) and International Finance Corporation (IFC), are starting to feel the pinch of too little equity. Their conservative shareholders are keeping them on a short leash, offering neither additional paid-in capital nor relaxing prudential lending standards or other balance-sheet optimisation choices (see section 2.2 above). On the demand side, many developing countries are cutting back on public investments in the wake of tightening credit conditions.

One new development bucking this trend is the increasing role of domestic development banks in emerging economies. In many MICs, there are growing pools of long-term institutional capital, concentrated either in national development banks or in government pension funds and insurance companies. Examples of how to mobilise these resources are growing, both locally and internationally, but systematic practices have yet to emerge.

3.2.4. Implications for the aid architecture

Many aid agencies are ill-suited to partner with business in their current configurations. They operate on slower timescales. They have less first-hand understanding of technology. Their classic operating model of pilot–evaluate–scale is at odds with a business model that emphasises learning by doing and constant innovation (despite much recent discussion of ‘adaptive programming’ in the development aid context). Business can make profits from operations aimed at the near-poor; aid agencies are primarily concerned with the most poor. Business looks to recover costs, while agencies look to transfer money to the poor. Where the two compete, as they do with principles of whether and how to charge for technical advice, or even for basic services, the frictions are evident and sharp. Most fundamentally, aid agencies are vulnerable to accusations of favouritism when they deploy financial instruments in partnership agreements with the private sector, and that risk inhibits them.

Mobilising private finance – a definitional quagmire. There is a palpable desire to leverage or mobilise private finance as a way of stretching aid flows and increasing their impact. Every aid agency has anecdotes about how it is innovating in this space. Few have an actual strategy. The problem starts from the fact that there are no currently agreed comparable data on the share of aid going into projects or programmes that try to leverage private capital. Indeed, there is no agreed-upon methodology, although work is under way in the DAC to develop the key elements of a framework on blended finance.¹¹ This framework starts from the twin premises that the finance being considered must have a development objective, and mobilise otherwise ‘non-development finance’. In other words, there should be some additionality to the finance; a noble idea but one that can be complicated to implement, as was made clear from the experience of tracking the ‘additional’ aid for climate change promised at Copenhagen.

Moving from a framework and general understanding to more tangible principles and best practices will not be straightforward and is likely to be a process that evolves over time as experience with different types of blended finance grows.

10 Private Participation in Infrastructure Database, World Bank.

11 See [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DCD/DAC\(2017\)9&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DCD/DAC(2017)9&docLanguage=En)

One important element is to keep track of additional amounts mobilised. The most recent DAC survey suggests \$27 billion in 2015. The DAC has also identified 140 other facilities with a stock of around \$30 billion of private funds under management. These volumes are sizable but far from the levels needed to get from ‘billions to trillions’. Hence the potential for scaling up should also be a feature of blending.

Part of the conceptual difficulty with thinking about new forms of PPIs is that there are many indirect ways that public policies can influence the allocation of private investments. Policy change is an obvious example. Imagine a country that imposes a carbon tax with technical support from an aid agency, and this carbon tax then leads to large-scale private investment in solar generation. Should the latter be counted as ‘mobilised’ private finance? Equally, many aid agencies provide analytical support or institutional strengthening to ease the cost of doing business. The World Bank even tries to measure the amount of private investment that is generated by such changes.

More direct blending tools and approaches. These indirect ways of mobilising private finance are perhaps too intangible to be counted as blended finance, but are important ways of allocating public funds. Four more direct ways are: (i) the provision of payments for GPGs (eco-services, for example); (ii) financial support, usually through shifting risk from private financiers towards public funders (guarantees, first-loss arrangements) or raising returns (blending with concessional public loans or grants); (iii) provision of technical assistance to de-risk projects; and (iv) support for project identification and origination.

Blended finance is likely to reach scale only if it is owned and supported by home-grown organisations. There are interesting experiences of national development banks providing platforms that can originate projects locally, de-risk and troubleshoot implementation, and blend local and foreign private capital with concessional funds. Early-stage support from aid agencies for such platforms could incubate later efforts to scale up blended finance.

Most blended finance projects to date are invested in upper-middle-income countries. There is therefore a concern that efforts to expand impact through this route may work against efforts to allocate more funds to fragile (and generally poorer) states. The IDA 18 window for mobilising private finance in conjunction with IFC is an early experiment to see if this tension can indeed be resolved.

At this stage, the most that can be said is that aid agencies should take a common-sense approach to new partnerships with the private sector. They would be wise to start immediately adopting metrics on the mobilisation of private funds, while keeping in mind that such metrics are only one way of understanding the impact of using public funds in ways that help align private investments more closely with development needs. Innovation and experimentation will dominate this space for a few years to come. Being aware of what is happening elsewhere and learning lessons are the immediate priorities.

Key policy recommendation

- 10 Accelerate efforts to define and track ‘mobilised’ private finance, starting with full participation by DAC members in its annual mobilised finance survey.

3.3. Climate: aid takes a back seat?

The third snowball is **international climate finance**. Our earlier view was that there was a risk that pressures to reorient development aid to meet climate finance commitments would shift allocations away from poverty reduction and LICs. However, for most DAC donors, climate-related aid has so far increased at the same pace as overall growth in ODA, and so has not crowded out non-climate-related programmes. But the bigger picture is that all resource flows for climate mitigation and adaptation, of which aid was never likely to form the dominant part, have fallen far short of expectations. Climate programmes are being supported mainly by non-concessional loans and export credits, green bonds and FDI. These flows can be oriented more towards greater climate sensitivity by new requirements for corporate disclosure, to account for environmental risk, including depreciating and replacing ‘stranded assets’ which are higher-carbon. But they remain voluntary and vulnerable to enforcement failure in the name of ‘freeing’ domestic companies from red tape.

3.3.1. Genesis – if support for climate change mitigation had relied mostly on aid...

In Horizon 2025, written midway between the Copenhagen (2009) and Paris (2015) Climate Conferences, we singled out climate change finance as the archetypal example of how development finance would have to be deployed differently in donors’ enlightened self-interest than it would from a purely poverty-reduction perspective.

Our logic was that unless new, supranational resources, such as levies on a new global carbon-trading regime, were mobilised at scale very soon for this endeavour (the Copenhagen Consensus called for an additional \$100 billion a year from 2020 in financial support from developed economies, including private and non-concessional flows), attempts to draw on development finance budgets as the primary funding source would powerfully distort aid allocations. That redistribution would occur both between purposes more closely related to climate change, and those not so closely aligned (such as energy versus education), and between emerging economies which are high carbon emitters, and fragile, high poverty-gap countries which are mostly not such high emitters (such as India versus Burundi). Financial engineering, such as the deployment of grant–loan blends and guarantees via the DFIs, would help blur the latter distinction, but not remove the allocation problem entirely.

Since 2012, additional official climate-change financing has not developed as fast as we had expected, and many hoped. The initial three-year pledge period after Copenhagen (known as Fast Start Financing or FSF) delivered commitments of \$30 billion, of which 80% came from aid budgets (ODA), and the rest mainly classified as non-concessional loans, export credits, guarantees and insurance (Nakhooda et al., 2013). Some 60% of this funding was for mitigation. An analysis of the top FSF recipients shows that MICs like India and Indonesia received significantly higher shares of FSF than they did of ODA (ibid.). This implies that if this distribution became representative of a much larger pool of international public finance for climate change, the overall country balance of ‘sustainable development’ funding would shift quite dramatically, in line with the Horizon thesis.

It also maps well to the broader rationale for assisting MICs with some other form of public international finance – not necessarily grants (Kharas et al., 2014). In practice, broad income classifications, as opposed to more granular considerations of fragility, fiscal capacity and credit-worthiness, are an increasingly poor criterion for allocating the grant element of international public finance (ibid.).

But the surge of largely aid-based public finance for climate change we predicted has not yet happened, despite the subsequent start-up and rolling resourcing of the Green Climate Fund (GCF). GCF pledges of approximately \$8 billion have been recorded for 2015–2018, net of the US pledge which has recently been withdrawn. Its total

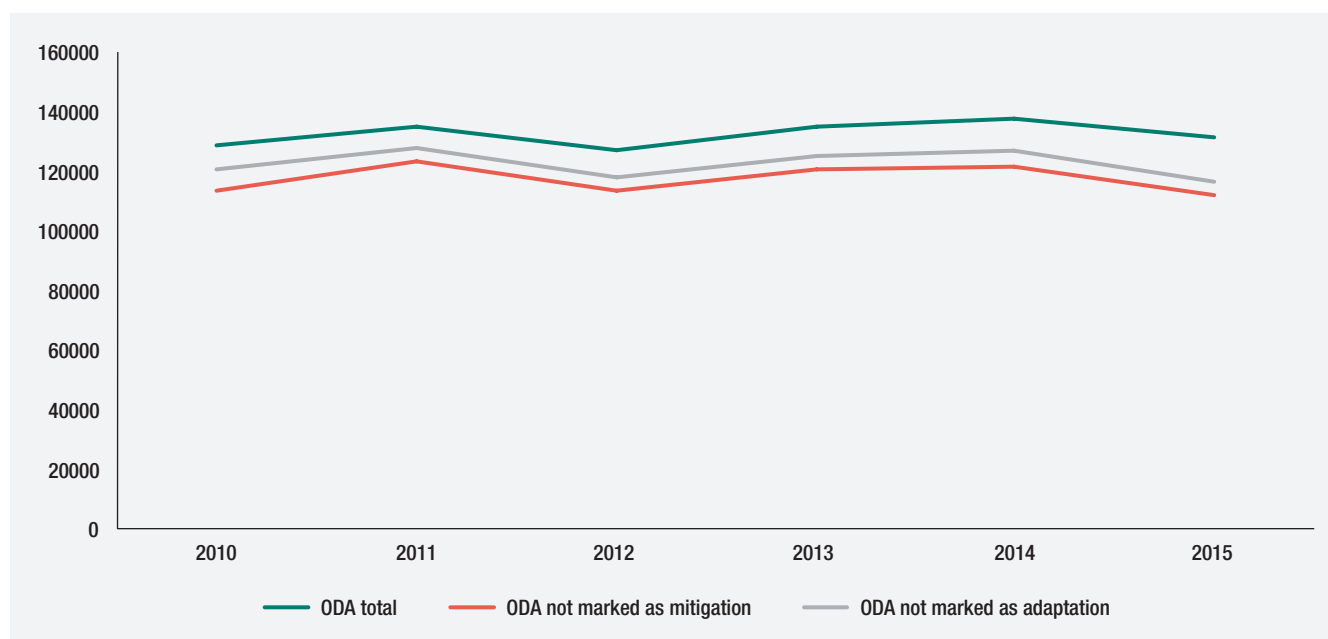
commitment authority recently stood at \$1.5 billion, above funding decisions of \$2.4 billion already made (GCF, Status of Resource Mobilisation, March 2017).

The overarching pressures to act, in line with Paris in order to remain within a 2°C warming band, definitely remain nonetheless. Indeed, every postponement of action increases the subsequent speed of change required to stay within this band. So is it possible that this disruptive force we foresaw in 2012 has merely been temporarily obscured or delayed by other factors – including resistance from the Trump Administration of course – but that it will inevitably return with a vengeance before 2030?

3.3.2. The bigger picture – climate action now relies more on other types of flows and regulatory action

Analysis of ODA headline trends suggests that development programmes with climate mitigation ‘markers’ and, coincidentally, adaptation markers, have increased faster than has aid as a whole (Figure 10), but that the absolute value of the development portfolio not earmarked for mitigation has nonetheless risen a little. Moreover, using these markers is like seeing coloured syrup in a glass of water – you know it is there, but cannot know how much there is unless you sample it, glass by glass, i.e. project by project (Kharas et al., 2014). Nor do the data show whether the climate components are improving the project in question (e.g. by reducing power consumption and/or adding resilience) or if they are solely climate-focused and therefore competing with other priorities.

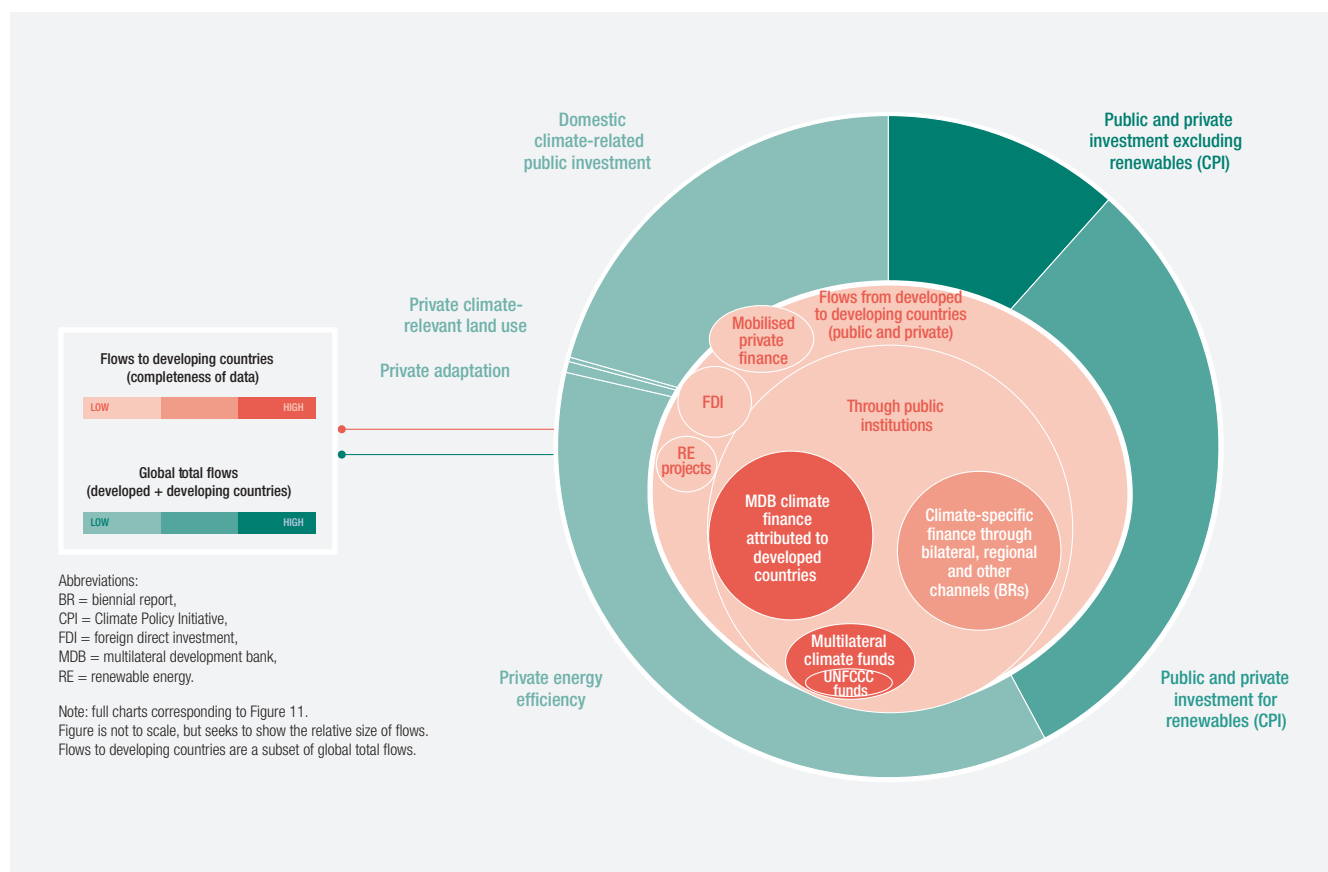
Figure 10. Climate change ODA – no clear patterns of crowding out¹²



Source: DAC CRS

¹² Some programmes may be marked for both adaptation and mitigation.

Figure 11. Climate finance flows are diversifying



Source: UNFCCC, *Biennial assessment and overview of climate finance flows, 2016*. Detailed table composition is in Annex 2

So one cannot state categorically that development finance linked to climate change is crowding out other priorities, though that possibility remains, especially for donors whose ODA is not growing overall. Even for them, the overlap between development purposes and adaptation, in particular, is near-total, as we discussed in *Horizon 2025*, so thinking about displacement is the logical equivalent of asking whether education programmes crowd out other development purposes.

But this is probably not a major part of the climate finance story today. International grant aid for climate change, as such, is being dwarfed by other types of flows encouraged by national and international carbon-related commitments and by various forms of blended finance, and egregiously, by good business opportunities for investment in, for example, renewable energy, supported by relevant regulation and tax incentives.

Recent authoritative assessments (UNFCCC, 2016) cite climate finance provided by MDBs from their own resources (mostly scoring as other official flows or OOF) as nearly reaching parity, at about \$26 billion each in 2014, with flows from bilateral regional and other channels. Of the MDB half (not yet including the AIIB and NDB), between half and two-thirds is in turn attributed to developed countries (*ibid.*).

Projections to 2020 (OECD, 2016), based on national and MDB pledges, conclude that up to \$67 billion per year can be mobilised through these same channels, and an additional \$24 billion could be mobilised from private co-financing, also attributed to developed countries, assuming every dollar of public finance in 2020 mobilises private finance in the same proportion as it did in 2013–2014. This is not to be taken for granted. It is important to understand that aid and non-aid flows for climate-related activities are not necessarily substitutes, but that they often go together, when aid plays its appropriate catalytic role.

Beyond such public and private-blended international flows there are much larger estimates (\$192 billion per year in 2014), of domestic climate finance, including that provided by national development banks. Above and beyond this there are estimates of global private investment in renewables of \$285 billion and in energy efficiency of \$337 billion, the latter being subject to greater uncertainty than the former (OECD, 2016). Action at national and international level to encourage such investment, whether through technology transfer facilitation and intellectual property rules, carbon pricing and the removal of subsidies on fossil fuels, trading regimes, or other forms of regulatory support, could quite easily become much more important than ‘development finance’ as such, even broadly defined.

There are many definitional caveats embedded in such snapshots. Among the main ones are that conflating the face value of partially, or barely, subsidised loans and grants flatters the generosity of countries and institutions who offer the loans, and that the basis for reporting privately mobilised finance is still inconsistent and/or non-transparent. Also there is the chicken-and-egg debate as to whether development bank loans today are effectively ‘mobilised’ more by their borrowers, who pay financing costs plus margins, or by their original equity owners, whose own credit ratings enabled the banks to tap markets on prime terms. This feeds back into broader questions of how much further the balance sheets of the MDBs can be ‘optimised’ responsibly (see section 2.2).

Also of policy interest is a different perspective, which involves comparing the costs and benefits of climate action, in particular for adaptation, with disaster risk reduction (DRR) and more generally insurance against global ‘bads’, including ever-larger migrant flows driven in part by climate-induced distress. An estimated 5 million people in SSA have moved across borders as a result of weather anomalies between 1960 and 2000; that is 130,000 people a year (Marchiori et al., 2012). Stern has suggested that by 2050 there would be 200 million people affected by climate change that could induce migration (Stern, 2007). Millock’s (2015) review of the literature on environmental migration finds that the evidence that climate change will lead to mass *international* migration is weak, compared to stronger findings on regional population movement and displacements within national borders.

The international community chronically under-invests in these preventive expenditures, compared to vast estimates of the stock of infrastructure, let alone human beings, potentially exposed to inaction. The political trade-offs between present adaptation and more expensive relief and repair in the future are not being made forcefully enough – perhaps the more powerful galvanising effect of imminent catastrophe at the gates of developed countries is what is necessary, possibly because of scepticism that the remedial investments will work well. Moreover, the adaptation agenda is lagging far behind the mitigation one in terms of understanding and measurement (and so is justification for aid and other financial flows), aggravated by the fact it is ‘only’ a national public good and so has a less obvious claim on international attention.

In any event, it is highly implausible that a large fraction of the adaptation finance needs of developing countries by 2030, estimated by the United Nations Environment Programme (UNEP) (UNEP, 2016) to be in the \$ 140–300 billion a year range, can be met solely by ODA. On the basis of current ODA shares and projected donor incomes, this could potentially eat up all aid (Oxfam International, 2016). Obviously, some rationing of grant aid for adaptation to those countries most severely in need, especially the least developed countries (LDCs), will be required (Kharas et al., 2014). But, beyond that, some thinking along subsidised

insurance lines, perhaps linked to the stocks of donor-funded investments at risk, might be helpful.

A powerful new driver of change in private climate finance behaviour comes from **corporate disclosure requirements**, treating climate-related risks as a key sub-set of reporting requirements for both financial (e.g. pension funds, banks) and non-financial (especially energy and transport) companies. The FSB Task Force on Climate-Related Financial Disclosures (CRFD, 2016) pointed out that in most G20 jurisdictions, companies with public debt or equity already have a legal obligation to disclose material risks in their financial reports – including material climate-related risks. This includes transparency on ‘stranded assets’ (BoE Governor and Task Force Chair Carney, 2015) which are high-carbon and for which mitigation actions, including write-downs, are needed now, not at some distant date. This could ultimately exert an impact on asset values and hence choices of all classes of investors, including households. The Task Force designed a set of recommendations for consistent disclosures. Financial disclosure is bound to be evolutionary, but a ‘variety of stakeholders, including stock exchanges, investment consultants, credit rating agencies and others can provide valuable contributions toward adoption of the recommendations’ (ibid).

One powerful potential feature of the financial disclosure lever is that it already operates in the marketplace through thousands of actors, largely beyond the daily remit of central administrations, like the current US government, which as we now know intends to withdraw from the Paris Agreement, i.e. this lever is, to a degree, resilient to the populist ‘meteor’.

Where that degree lies remains unclear. The US has already rolled back Sections 1502 and 1504 of the Dodd-Frank Act, dealing with corporate disclosure of payments for resource extraction and the traceability of minerals to conflict-free zones. The new philosophy is revealed in a February 2017 speech by (then) Acting Securities and Exchange Commission (SEC) Chairman Michael Piwowar: ‘I believe it is categorically wrong to use shareholder assets to fund a humanitarian effort better left to executive agencies with the requisite experiential knowledge’ (Piwowar, 2017). Disclosure forces may yet be blunted by regulatory enforcement failure, whether by deliberate choice or inertia.

We remind readers, finally, that both the climate change finance ‘snowball’ and the conflict–refugee–migrant ‘meteor’ are central illustrations of the case for building up a better, more comprehensive set of international development metrics than we have today – which we call international development contributions (IDC) (Kharas and Rogerson, 2016) and have already introduced in section 2.1 above.

Key policy recommendation

- 11 Emphasise greater regulatory coherence in support of non-ODA incentives for climate action and finance, such as corporate disclosure requirements and the tax system.

3.4. China's 'big push' on development

The final snowball is the huge **Chinese big push on development**, and the growing need for Western countries to factor it in, and play catch-up if and where possible. We were fairly sure in 2012 that many other donors would try to emulate the Chinese example, by linking aid, trade and investment and blending the package with commercial loans. What we did not fully appreciate was the breathtaking scale of the Chinese ambitions, for example in the One Belt, One Road (OBOR) cluster of mega-projects. The impact of Chinese support is being felt everywhere. The Chinese have delivered enormous volumes of funds on commercial terms that, in the current global financial context, look extremely attractive. The two largest Chinese banks, China Development Bank (CDB) and China Ex-Im Bank, already hold roughly the same total international assets (\$680 billion) as all the Western-origin MDBs put together. China now has the tools and programmes to challenge the West on development and aid agencies could develop a strategy of 'competitive engagement', continuing to emphasise good governance in bilateral dealings, even where China does not, while encouraging cooperation with the new China-headquartered multilateral banks. These banks are off to a flying start and fears over lowering standards are giving way to grudging acceptance of the efficiency gains to be had, for example, from the absence of a resident Board of Directors. In terms of motivation (mutual benefit), efficiency, and perhaps effectiveness, Chinese development efforts are setting new benchmarks against which Western aid agencies will increasingly be judged.

3.4.1. China reaches for scale

When China's Premier Xi Jinping presided over the Belt and Road Forum in May 2017, he underlined China's extraordinary ambitions to become a leader in global development. At the Chinese G20 Summit in Hongzhou, China championed an Action Plan based on high-level principles to underline its leadership in implementation of Agenda 2030.

In Horizon 2025, we had recognised the trend towards national trade and investment interests and the likely use of aid to promote expansion of markets, exemplified by the Belt and Road Initiative. But we believed that the need for infrastructure resources was so vast that there would be plenty of scope for all development agencies to continue to deliver products. Indeed, we concluded that 'the risk of a collapse in demand for growth-related financing (from development agencies) is modest overall'.

We did not appreciate the speed and scope of the transition. Already China is committing around \$150 billion per year to the 68 countries that participate in the Belt and Road Initiative, although China, like other countries, tends

to make announcements that exceed actual commitments. The largest package, nevertheless, totalling some \$4 billion, has been signed with Pakistan, with road, rail, port, energy and special economic zone investments already identified. By contrast, total foreign aid to Pakistan from donors reporting to the DAC is only \$1.7 billion per year, with a further \$650 million in gross disbursements of non-aid flows mostly from multilateral agencies such as the World Bank and the Asian Development Bank (ADB). And taken together, DAC countries are reducing their exposure to developing countries in the form of export credits at the rate of several billion dollars per year (OECD DAC1).

The impact of Chinese support is being felt everywhere. Unlike Western aid, the Chinese have not massively expanded grants or concessional loans. But they have promised (and delivered) enormous volumes of funds on commercial terms that, in the current global financial context, look extremely attractive. For China, such projects could be a triple win. If successful, they will generate yields on China's external foreign assets that are (risk-adjusted) superior to those available on US treasury bonds. They may also help sustain demand for Chinese companies, especially construction companies, which would otherwise be faced by declining demand within China as investment slows. And by linking China to markets abroad, it becomes easier for trade with China to expand, both in natural resources and in other goods and services.

China's commitments to developing countries can no longer be dismissed as too small to have an impact on other agencies. Kevin Gallagher of Boston University estimates that the two largest Chinese banks, CDB and China Ex-Im Bank, already hold roughly the same total international assets (\$680 billion) as all the Western MDBs put together. In addition, China has announced concessional funds totalling another \$116 billion.¹³ The two new MDBs that it helped co-found, the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank (NDB), are up and running. AIIB's investment capacity could be as much as \$250 billion by 2020 according to its Articles of Agreement. By then it could have more paid-in capital than the World Bank.

Meanwhile, Western development agencies are in limbo. The US government's 2017 'skinny' budget ceased funding for its commercial lending arm, the Overseas Private Investment Corporation (OPIC). While this budget is unlikely to be the last word in what actually gets implemented, it signals the prevailing view in many Western capitals that publicly provided commercial finance competes with, rather than complements, private capital. These governments, the shareholders of the major multilateral agencies, do not seem to have the same drive to achieve scaled-up volumes of financing to MICs. The World Bank, for example, is already sharply cutting back on its planned lending volumes, fearing that it might not be able to get a

13 See https://www.bu.edu/pardeeschool/files/2016/05/Fueling-Growth.FINAL_.version.pdf

capital increase that would permit it to sustainably maintain or grow above 2016 lending volumes. The same is true in other international financial institutions. Chris Humphrey cites analysis done in the G20 working group in late 2016 that finds that the five major Western multilateral agencies have around half a trillion dollars in unused financial capacity ('headroom') because of conservative financial practices reflecting major shareholders' cautious approach to risk (Humphrey, 2017).

While competition from China is fierce, there is no guarantee that its overseas development projects will succeed. Snide assessments ('one belt, one trap') abound. Infrastructure projects are notoriously difficult to implement. China's desire to ensure that its projects meet international standards could handcuff its construction companies. Issues ranging from public procurement practices to the adequacy of environmental and social safeguards to country creditworthiness constraints could well move from anecdotal and episodic to systemic problems. Yet, given the high political priority attached to its schemes, it would be unwise to rely on China's ambitions tripping over their own feet.

Japan was the first country to respond to China's initiatives with a \$110 billion infrastructure investment plan of its own in Asia. But more recently, Japanese focus may have shifted towards infrastructure investment in the US, aligning with Trump's 'America First' slogan. Similarly, Saudi Arabia has announced a \$40 billion plan for a joint participation with Blackstone for investing in infrastructure, mostly in the US.

The combination of Chinese expansion abroad and Western re-orientation domestically is still playing out in aid agencies. Some governments, such as the French, have announced a major expansion of commercial lending, along with an expansion of grants to blend with agency loans. Others, like the Canadian government, are experimenting with commercial lending but on a small scale. The UK also appears set to increase the share of public commercial lending in its total development cooperation.

The Philippines recently announced its intention to refuse EU aid if conditions on human rights are included (in this case related to the death penalty that the Philippines imposes in its war on drugs). China, of course, explicitly excludes any policy conditionality in its activities.

China has demonstrated a proclivity to lend into fragile situations, partly because this is where many natural resources lie. For example, it has committed around half of its loans to Latin America (now totalling about \$115 billion from the two large banks) to Venezuela. In Africa, Chinese infrastructure investments are running at about \$10 billion per year, again concentrated in a few countries: Angola, DRC, Ethiopia, Kenya and Sudan (Dollar, 2017).

3.4.2. Implications for the aid architecture

Competitive engagement with China. Although China is reaching scale in its overseas investments, largely bypassing

grants in favour of commercial loans, it is taking far larger risks than Western aid agencies, or indeed Western export credit agencies. With large risks comes the likelihood of failures. China has yet to be tested on how it responds to these but it clearly sees the dangers. It is now an observer at the Paris Club where debt-distress situations are reviewed.

Chinese investments are partly in countries in which Western aid agencies tend not to have a funding presence. In this sense, China does not compete with them. But that is too simplistic a view. In reality, both China and Western agencies are using aid and overseas investments as a tool to build their spheres of influence, notwithstanding a formal 2015 Memorandum of Understanding between the United States Agency for International Development (USAID) and the Ministry of Commerce of China. The initial battlegrounds are in South-East Asia, Central Asia and parts of Africa. Perhaps this will be extended to all the 68 countries participating in the Belt and Road Initiative, but it is too early to tell how strongly this set of mega-projects will focus Chinese investments. Experience to date suggests not much, but that could change over time. Meanwhile we think Western agencies could usefully track their own portfolio exposure in OBOR countries, and have produced a simple index to help them do that in section 4.

China now has the tools and programmes to challenge the West on development. For the time being, it prefers to work within the framework set out by the United Nations partly because, unlike developed countries, within that framework it has no specific obligations to live up to. The new development banks that are headquartered in China are off to a flying start and fears over lowering standards appear to have given way to grudging acceptance of the efficiency gains to be had from the absence of a resident Board of Directors. In terms of motivation (mutual benefit), efficiency, and perhaps effectiveness, Chinese development efforts are setting new benchmarks against which Western aid agencies will be increasingly judged.

Working more closely with emerging economies and the institutions they control. Given the multiple demands on 'Western' development finance, and the political difficulties of sustaining it, there is, or should be very soon, a high premium on working much more closely with the new institutions created, largely by China but also with backing by other BRIC nations, like the AIIB and the NDB, as well as the huge array of Chinese, (mainly, for now), national development banks with a large external arm, like the CDB (see preceding section).

This enhanced cooperation could take the form of project-specific or programmatic co-financing, as well as selective or general capital increases. The funding could be linked to specific procurement undertakings or quotas that could be presented favourably to domestic taxpayers. Traditional 'old-money' donors should accept minority-partner status with good grace. By the same token, if emerging economies are willing to provide selective capital to traditional banks, perhaps in the form of guarantees

associated with new facilities operating under special governance rules, traditional donors should by all means welcome such approaches. As part and parcel of this pragmatism, ‘old’ MDB shareholders should abandon, where they still exist, any mechanical ‘graduation’ approaches for UMICs’ eligibility to borrow from MDBs on non-concessional terms. We presented an alternative ‘gradation’ perspective in section 2.3.

Key policy recommendation

- 12 Western aid agencies should establish a ‘competitive engagement’ strategy with China for bilateral aid, and track where their main overlaps and gaps lie, as well as developing a collaborative approach for joint investment across the multilateral development system, including the new MDBs.

4. Who's most affected?

A world in 2025 where aid agencies can point to success in reducing fragility (and hence global poverty), mobilising business, addressing climate and refugee issues at scale, while at the same time respecting national ownership and new geopolitical realities, will be a world where aid agencies will prosper and enjoy popular support. Conversely, weaknesses in this chain become vulnerabilities for aid agencies. We close, therefore, with a review of how the changes we have described could affect aid agencies in each OECD country. Some changes are already incorporated in an aid 'Resilience Index' developed by ODI, taking up our 2012 approach. We reproduce this for convenience, but add additional indicators for aid agencies to ponder. Are they likely to be caught up in the 'my nation first' populist wave? How do they compare in current efforts to mobilise private funds? Are they operating in places where competition with China could be fierce? We suggest specific indicators to measure these pressures as one way for agencies to understand their relative severity as our contribution to the strategic discussions and long-term scenario-building that we hope continues in every country.

In 2012 we constructed a simple traffic-light 'exposure' index which aimed to stress-test the portfolios of major development agencies against the four main disruptive forces we discussed in that report, that is, to the agency's exposure to a risk of becoming irrelevant.

The first was the demand-side pull towards the imperative of operating increasingly in fragile and/or high poverty-gap contexts. The second was the supply-side shift of attention towards global-commons challenges, including climate change but also disease pandemics and similar issues. The third was the need to prioritise growth, infrastructure and trade. And the fourth was a down-rating of the importance of subsidising social-sector provision through public services, given the growing ability of other actors, including NGOs and social impact investors, to contract and part-fund them. By definition, we apportioned all DAC donor activities into one or other of the last three categories and gave them relatively arbitrary weights, most strongly in favour of the first two effects.

Our present framework maintains these key themes, noting the growing concern with climate change and migration, of course.

To this agenda we have added three factors of exposure or resilience revolving around domestic support and influence, namely populist and anti-globalisation pressures from citizens; mobilisation of corporate interest; and foreign policy influence drivers, specifically linked to China. Each can be thought of as mapping to a different interest group.

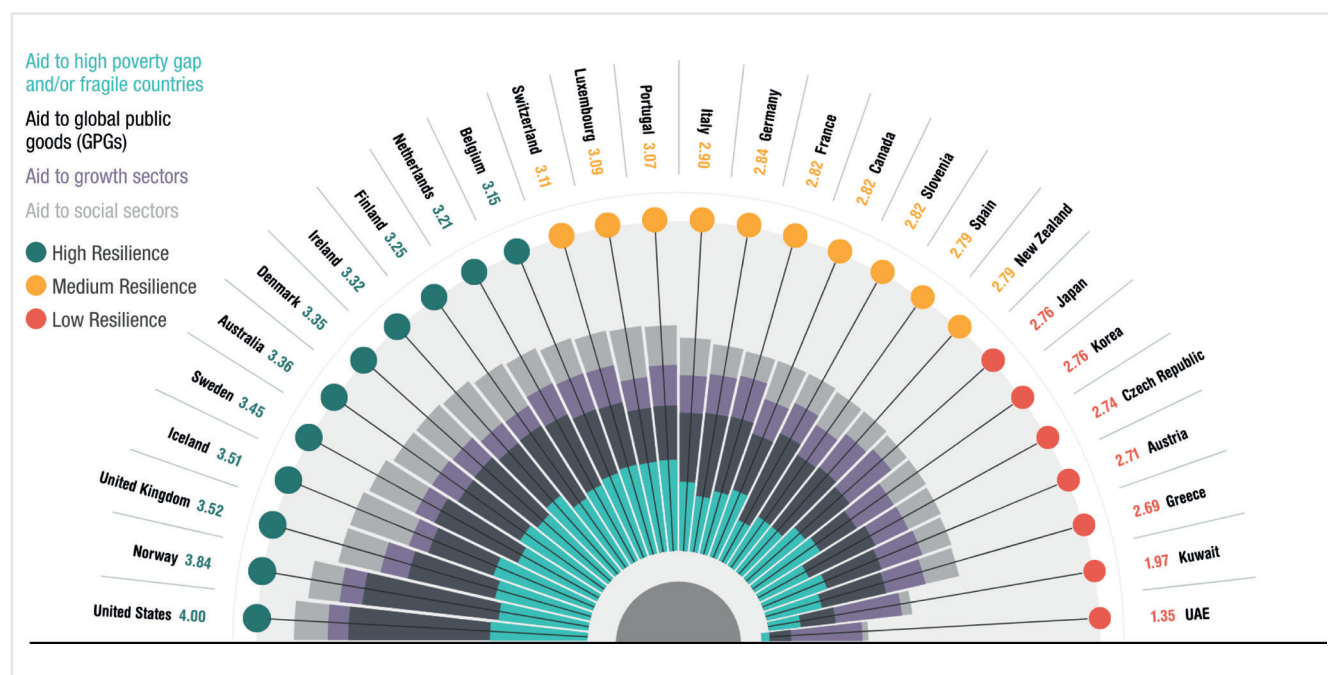
On the first set of outcome drivers, ODI has recently developed, updated and improved our ratings into a 'Resilience Index', available online with user-determined weights (Figure 12 below). It illustrates how prepared donor countries currently are for addressing those future development challenges. They line up from left to right, from green (high resilience) through amber (medium) to red (low resilience).

The Index considers that the two biggest development challenges we face now and in the foreseeable future are state fragility and extreme poverty, and global and transnational phenomena, such as climate change, pandemics and refugee flows. As such, it concludes that those donors that currently spend more of their aid on addressing fragility and extreme poverty, and on supporting GPGs, are more resilient and responsive to the future.

The Index is not intended as an assessment of performance, but to encourage donors to think in the long term and to stimulate debate on future priorities. Since donors have their own areas of comparative advantage, the Index also allows countries to compare priority areas of spending with others in the hope of stimulating a discussion on a better division of labour across the system.

We can readily agree, with both our previous analysis and this recently revised Index, that fragility and its impact on the locus of poverty, and global-commons challenges including both climate change and migration, are right at the top of the factors which will test these agencies most severely between now and 2030. We also suggest three other signposts, or indicators of possible advantage or exposure, which are related more directly to the three other 'domestic constituency pressures'.

Figure 12. Resilience to future challenges: the ODI donor resilience index



Source: ODI, 2017 (available at <https://www.odi.org/opinion/10423-donor-resilience-index>)

Box 3. Indicators of donor exposure/resilience to meteors and snowballs

Meteor 1 (new): Populist ‘my-country-first pressures’. (Inverted) country scores on Edelman Trust Barometer (Figure 3), low confidence in global system = high exposure.

Meteor 2: Agenda 2030: implicitly included in the Resilience Index. No direct indicator available.

Meteor 3: Refugees and migrants: partly included in Resilience Index. Reporting of refugee costs unreliable.

Snowball 1: Poverty trends and fragility: explicitly included in Resilience Index.

Snowball 2 (new): New business roles: private-sector funds mobilised as share of ODA described in OECD Survey.

Snowball 3: Climate change: explicitly included in Resilience Index.

Snowball 4 (new): China’s big push. Share of donor ODA portfolio going to 68 OBOR countries.

Table 2. Traffic lights for OECD aid agencies (white=not rated)

ODI Resilience Index	Populism	Business	China
United States	United States	United States	United States
Canada	Canada	Canada	Canada
Norway	Norway	Norway	Norway
Iceland	Iceland	Iceland	Iceland
United Kingdom	United Kingdom	United Kingdom	United Kingdom
Netherlands	Netherlands	Netherlands	Netherlands
Sweden	Sweden	Sweden	Sweden
Australia	Australia	Australia	Australia
Ireland	Ireland	Ireland	Ireland
Denmark	Denmark	Denmark	Denmark
Luxembourg	Luxembourg	Luxembourg	Luxembourg
Finland	Finland	Finland	Finland
Republic of Korea	Republic of Korea	Republic of Korea	Republic of Korea
Belgium	Belgium	Belgium	Belgium
Portugal	Portugal	Portugal	Portugal
Japan	Japan	Japan	Japan
Italy	Italy	Italy	Italy
Switzerland	Switzerland	Switzerland	Switzerland
France	France	France	France
Austria	Austria	Austria	Austria
Germany	Germany	Germany	Germany
Kuwait	Kuwait	Kuwait	Kuwait
New Zealand	New Zealand	New Zealand	New Zealand
Greece	Greece	Greece	Greece
Spain	Spain	Spain	Spain
Czech Republic	Czech Republic	Czech Republic	Czech Republic
Slovenia	Slovenia	Slovenia	Slovenia
United Arab Emirates	United Arab Emirates	United Arab Emirates	United Arab Emirates

Source: Authors’ calculations (see methodology and sources in Annex)

Including the additional issues in our assessment of challenges facing aid donors suggests that indeed the meteors and snowballs are having a differential impact. Countries like France, Germany, Italy and Spain are among those where the population feels most disenchanted by globalisation; we worry that they risk a backlash against aid, especially as they do not have the same tradition or legal basis for aid support as is the case for Scandinavian countries or the UK. At present, Germany and France are among the few donors actually expanding aid faster than national income, so it is especially important for global aggregates that they maintain this by communicating clearly the national benefits associated with higher aid contributions. By contrast, the major Asian DAC donors, Japan and Republic of South Korea, continue to enjoy widespread popular support for global interventions.

A quite different story emerges with respect to aid agencies' dealings with business. Over half of our sample is severely challenged by this snowball. Some agencies do not even collect data on the volume of mobilised private capital: we give an automatic 'red card' to non-reporting DAC members. Others report extremely low levels, less than 1% of their aid flows. Lack of experience with partnering

with business will hamstring these agencies and they will need alternative mechanisms to achieve major impact. Lack of engagement with the business community may be a particular problem for countries that also have a populist bent. Where will additional support for aid come from?

Our third new traffic light relates to China. We believe that China will concentrate its aid in countries that form part of its OBOR initiative. These countries will then be in stronger positions to pick and choose among other donors, creating particular difficulties when policy and institutional reform are considered as preconditions for aid. Our analysis suggests that Germany and Australia, among major donors, have the greatest overlap of country aid programmes with China, but so do smaller donor countries with an aid hinterland at one end or the other of the Road.

The diversity and complexity of the changes in the development landscape that we have identified underlines our central thesis: aid agencies in most rich countries are facing significant challenges in at least one area that should be cause for senior management attention. There are threats lurking around many corners. We hope that our framework and data help inform the conversations in these agencies on how they should adapt.

5. Conclusions

The context in which aid agencies operate is shifting fast. The technocratic space to help reduce poverty and save lives, based on rigorous evidence, has shrunk: the poverty gap is within reach, but the pace of improvement is slowing just as aspirations have expanded. At the same time, support for globalisation in many forms, including aid and multilateral action, has fractured.

Official aid agencies are increasingly being forced to: (i) justify their actions based on their own national interest; (ii) respond effectively to the ambitions of the SDGs; (iii) address both the practical and political problems arising from an influx of refugees and migrants; (iv) demonstrate effectiveness in fragile states, the new frontier for poverty reduction; (v) develop new forms of engagement with business; (vi) become catalytic drivers for climate mitigation and adaptation; and (vii) react to a far larger footprint of China. The first three of these issues are new, seizing global attention, like meteors, in the past couple of years. The last four issues are old, but have picked up speed and taken unexpected turns that, like snowballs rolling down mountainsides, have amplified their impact. We have discussed each in turn and drawn out scenarios and implications for official aid agencies. We asked which agencies are likely to be most affected and in what ways, by quantifying indicators that reflect the new trends, and setting them alongside the old.

We offer five high-level policy recommendations below, and then in section 6 recap the 12 more detailed policy suggestions presented in earlier sections.

1. Governments will need to clarify how and to what extent international funding is allocated to non-aid national departments, such as health, environment, or immigration.

Our first major point is that any new narrative linking aid to the national interest to mitigate populist pressures should involve non-aid agencies. For example, the Department of Health should concern itself with global preparedness for pandemics and the impact this might have on national health issues. Moving in this direction will require a greater clarity of mandates within advanced economies between agencies responsible for core poverty reduction and other domestic departments, such as foreign affairs, defence, commerce, immigration, environment and health, that could support GPGs in areas critical to the national interest. The ‘aid-is-good-for-us’ narrative will also

feature containing cross-border spillovers of global ‘bads’ like climate change, conflict, and refugees, and accounting more systematically for such action.

2. To tackle global challenges effectively, rigid ‘graduation’ rules linking aid to country income levels must give way to more nuanced ‘gradation’ mechanisms, by which relatively better-off middle-income countries can be co-opted to help solve regional and global challenges, like surging migrant flows and unsustainable carbon emissions.

Due to spillover effects and the expanding regional influence of several MICs, rigid rules on countries’ ‘graduation’ from receiving aid should give way to a more nuanced ‘gradation’ approach – less aid for UMICs but an accommodation by which they become part of the solution, as in the case of Jordan and Lebanon’s hosting of Syrian refugees. Part of such an exercise should also be a focus on DRM in MICs to allow them to take on greater responsibility for their own development. Multilateral organisations are often in the lead where global public goods and ‘bads’ are involved, but they are currently under stress and constrained in their dealings with MICs, so aid agencies need to support them financially and give them more operational leeway.

3. Aid agencies must focus far more closely on how to achieve progress in tackling the root causes of fragility. One first simple step towards this goal is to ensure legal identity through robust systems of civil registration and vital statistics. Multilateral agencies operating in fragile contexts in different dimensions of security, humanitarian and development assistance, must also be encouraged to work more effectively together.

How aid agencies operate in fragile contexts will become a defining issue for both multilateral and bilateral institutions. There is a desire to identify and tackle ‘root causes’ rather than deal with symptoms of humanitarian disaster or wars, but less understanding of how to go about that in practice. We advocate starting with a simple step of providing legal identity through civil registration and vital statistics (CRVS), but also other measures, such as building resilience through safety-nets, domestic resource mobilisation, and encouraging more private-sector jobs. Here, as in other areas, DevTech could assist, as digitalisation can mitigate many weaknesses in government functions.

4. Western aid agencies need to forge a ‘competitive engagement strategy’ with China in bilateral development cooperation, and to intensify collaboration with the international institutions that China sponsors.

Partnering with China offers opportunities for scaling up impact, for example in areas like climate change, but also carries risks, especially for bilateral programmes where Chinese and Western approaches have differed.

5. Blended (public–private) finance will be likely to achieve its potential only if it is owned and supported by home-grown organisations. National development banks, providing platforms that can originate projects locally, de-risk and troubleshoot implementation, and blend local and foreign private capital with concessional funds, deserve more international attention.

Scaling up, with domestic ownership, can also be facilitated by partnering with national development banks, some of which are developing novel platforms to facilitate project origination, mobilisation of local and foreign finance, and implementation.

A world in 2025 where aid agencies can point to success in reducing fragility (and hence global poverty), mobilising business, addressing climate and refugee issues at scale, while also respecting national ownership and new geopolitical realities, will be a world where aid agencies will prosper and enjoy popular support. Conversely, weaknesses in this chain become vulnerabilities for aid agencies.

Figure 1 (in the Executive Summary and reproduced below for convenience) visualises a ‘virtuous cycle’ of strategic responses by governments and aid agencies to counter these threats and deliver on the challenges.

Figure 1. From weakness into strength – a virtuous cycle of aid-system responses to threats



6. Key policy actions

Populism (section 2.1)

- 1 Move towards much greater clarity of mandates within developed countries, between agencies primarily responsible for core poverty reduction in specific country contexts and specialised departments coordinating support for global public goods (GPGs), including via allocations to developing countries.
- 2 Establish a new internationally credible definition of official financial assistance, separate from ODA, against which both developed and emerging economies can benchmark their funding: for example, international development contributions.
- 3 Development agencies must invest more up-front in identifying and assessing DevTech prospects, and be selective in which to support, why, and how.

Development agenda (section 2.2)

- 4 The owners of the multilateral development bank (MDB) system must urgently consider balance-sheet optimisation alternatives, overall and in specific thematic areas, which can greatly expand their operations while taking on prudent levels of additional risk.
- 5 Core standard-setting and monitoring functions of specialised international agencies should be protected financially, including via a more robust system of earmarked levies on the GPG budgets of their national member departments.
- 6 Development agencies must invest more up-front in identifying and assessing dev-tech prospects, and be selective in which to support, why, and how.

Migration (section 2.3)

- 7 Refugee-targeted interventions through stable third countries illustrate the need for a more nuanced approach – which we call ‘gradation’ – to providing enhanced loan support to upper-middle-income countries (UMICs) when there are clear GPG arguments for it.

Poverty trends and fragility (section 3.1)

- 8 Improve funding allocations to fragile African states, in line with global poverty shifts, until new domestic resource mechanisms can be built up: prepare donor public opinion for the long haul, and for frequent setbacks.
- 9 Focus on ‘boring’ institution-building essentials: prioritise civil registration and vital statistics as a ubiquitous springboard for basic services, and insist on more joined-up collaboration between the major United Nations and MDB bodies in fragile contexts. Experiment with universal cash-based social assistance programmes based on digital technologies.

Private sector (section 3.2)

- 10 Accelerate efforts to define and track ‘mobilised’ private finance, starting with full participation by DAC members in its annual mobilised finance survey.

Climate change (section 3.3)

- 11 Emphasise greater regulatory coherence in support of non-ODA incentives for climate action and finance, such as corporate disclosure requirements and the tax system.

China (section 3.4)

- 12 Western aid agencies should establish a ‘competitive engagement’ strategy with China for bilateral aid, and track where their main overlaps and gaps lie, as well as develop a collaborative approach for joint investment across the multilateral development system, including the new MDBs.
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Annexes

Annex 1. Further information on traffic light indicators

This appendix presents the numerical version of Table 2, describes the methodology and details the source of the data used for the construction of the three scores. The colour coding reflects the tercile of each normalised scores' distribution.

ODI Donor Resilience Index	Populism	Business	China
United States	0.31	0.79	0.64
Canada	0.35	0.01	0.64
Norway	N/A	0.15	0.87
Iceland	N/A	N/A	0.95
United Kingdom	0.24	0.31	0.57
Netherlands	0.33	0.31	1
Sweden	N/A	0.24	0.86
Australia	0.27	0	0.27
Ireland	0.27	N/A	0.82
Denmark	N/A	1	0.83
Luxembourg	N/A	0.05	0.68
Finland	N/A	0.24	0.65
Republic of Korea	0.49	N/A	0
Belgium	N/A	0.07	0.84
Portugal	N/A	0.09	0.72
Japan	0.61	0.01	0.15
Italy	0	N/A	0.5
Switzerland	N/A	0.1	0.67
France	0	0.42	0.68
Austria	N/A	N/A	0.37
Germany	0.2	0.19	0.42
Kuwait	N/A	N/A	N/A
New Zealand	N/A	N/A	0.85
Greece	N/A	N/A	0.36
Spain	0.1	0.04	0.61
Czech Republic	N/A	N/A	0.08
Slovenia	N/A	N/A	0.19
United Arab Emirates	N/A	N/A	N/A

The ODI Donor Resilience Index: is available at: <https://www.odi.org/opinion/10423-donor-resilience-index>.

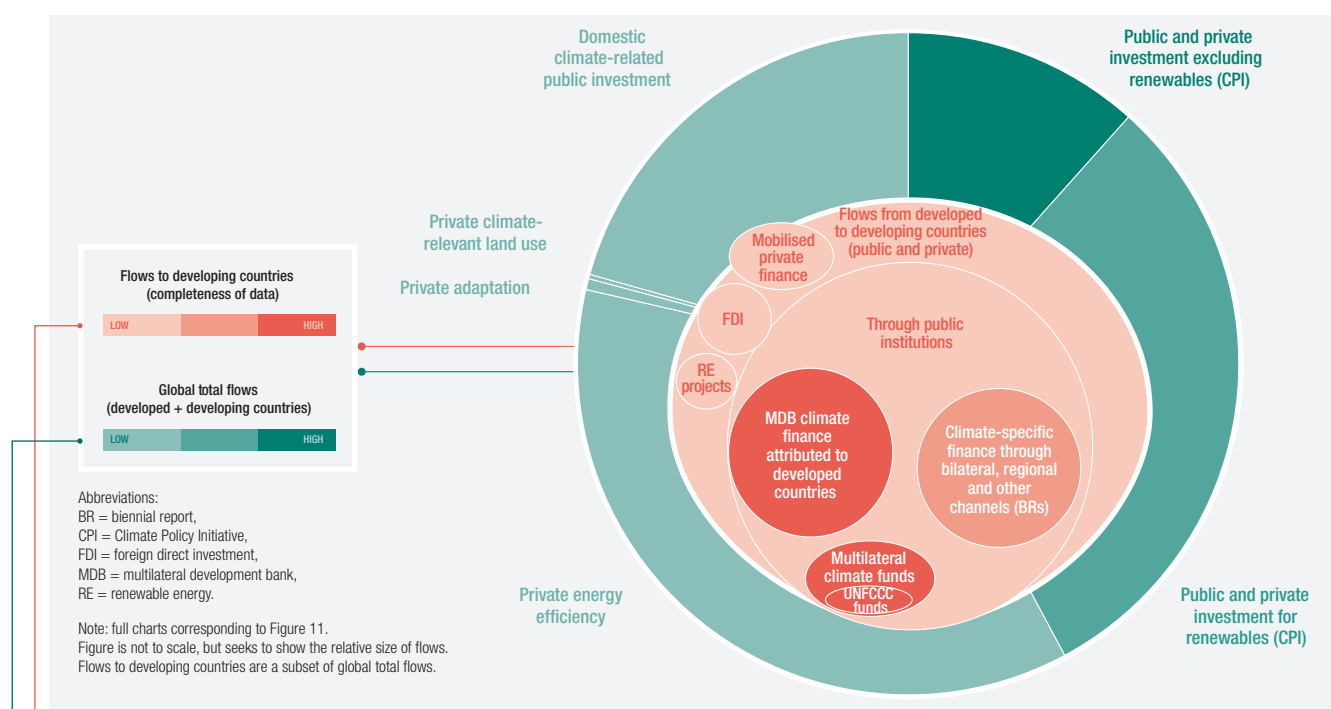
The methodology can be found at: https://www.odi.org/sites/odi.org.uk/files/data-vis/odi_donor_resilience_index-methodology_note_-_web.pdf.

Populism: populism score is derived from the Edelman Trust Barometer (2017). It corresponds to the normalised percentage of inhabitants of each country who have 'faith in the system'. The Edelman Trust Barometer (2017) is available at <http://www.edelman.com/trust2017/>.

Business: business score is derived from the 2015 DAC Survey on mobilisation. Private flows considered in the survey are defined as 'amounts mobilized from the private sector by official development finance interventions in form of guarantees, syndicated loans, shares in collective investment vehicles (CIVs), credit lines and direct investment in companies'. The business score is calculated as the normalised ratio between private flows mobilised between 2012 and 2015 and the total average ODA over the period (extracted from DAC5). DAC members who do not report to the survey are given an automatic red card, as are members with very low reported scores (less than 2% of ODA). The 2015 DAC Survey on mobilisation is available at: https://public.tableau.com/views/Mobilisation3/Dashboard1?:embed=y&:display_count=yes&:showTabs=y&:toolbar=no?&:showVizHome=no.

China: China score is calculated as the normalised average of the ratio between total net disbursement to the countries participating in the OBOR initiative and total net disbursements to all developing countries (DAC2a) for the period 2013–2015. A higher share implies greater competition with China and, therefore, lower resilience.

Annex 2. Climate finance flows in 2013–2014 (\$ billion)



		2013 (US \$ billion face value)	2014 (US \$ billion face value)	Sources of data and relevant chapter in the technical report
Flows to developing countries 2013–2014 average total Public: US \$41 billion Private: US \$2 billion renewables US \$24 billion FDI US \$14.8 billion mobilised	UNFCCC funds ^a	0.6	0.8	Chapter 2.2.1 Fund financial reports, climate funds update
	Multilateral climate funds (including UNFCCC funds)	1.9	2.5	Chapter 2.2.2 Fund financial reports, climate funds update
	Climate-specific finance through bilateral, regional and other channels	23.1	23.9	Chapter 2.2.3 CTF table 7(b)
	Of which grants and concessional loans	11.7	12.4	Chapter 2.2.3 CTF table 7(b)
	MDB climate finance attributed to developed countries (own resources only) ^b	14.9	16.6	Chapter 2.2.5 MDB climate finance reporting
	Renewable energy projects ^c	1.8	2.1	Chapter 2.2.9 CPI landscape of climate finance, BNEF
	FDI in greenfield alternative and renewable energy	26.4	21.6	Chapter 2.2.9 CPI landscape of climate finance, FDI Intelligence
	Mobilised private financed	12.8	16.7	Chapter 2.2.9 OECD CPI report 2015
Global total flows (inclusive of flows to developing countries above) 2013–2014 average total US \$714 billion	Public and private investment excluding renewables (CPI)	95–102	102–112	Chapter 2.4.1 CPI landscape of climate finance
	Public and private investment for renewables (CPI)	244	285	Chapter 2.4.2 BNEF, CPI landscape of climate finance
	Private energy efficiency	334	337	Chapter 2.4.3 IEA energy efficiency market report
	Private sustainable transport	Not available	Not available	Chapter 2.4.4
	Private climate-relevant land use	5	5	Chapter 2.4.5 CPI land-use studies
	Private adaptation	1.5	1.5	Chapter 2.4.6
	Domestic climate-related public investment	192	192	Chapter 2.4.7 CPEIRs (UNDP, World Bank, ODI), GFLAC climate finance studies, BURs

Abbreviations: BNEF = Bloomberg New Energy Finance, BUR = biennial update report, CPEIRs = Climate Public Expenditure and Institutional Reviews, CPI = Climate Policy Initiative, CTF = common tabular format, FDI = foreign direct investment, GFLAC = Climate Finance Group for Latin America and the Caribbean, IEA = International Energy Agency, MDB = multilateral development bank, ODI = Overseas Development Institute, OECD = Organisation for Economic Co-operation and Development, UNDP = United Nations Development Programme.

^a Includes commitments approved during 2013 and 2014. Almost all contributions are contributed by Annex II Parties. The values do not reflect pledges to the Green Climate Fund amounting to US \$10.2 billion by the end of 2014.

^b From Annex II Parties to non-Annex I Parties. Values are derived by excluding climate finance to Annex I Parties from the total climate finance provided by MDBs from their own resources to arrive at climate finance provided to non-Annex I Parties, and by attributing 85% of this to Annex II Parties.

^c From Annex II Parties to non-Annex I Parties.

^d From Annex II Parties as well as the Czech Republic, Poland, Slovakia and Slovenia.



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Cover photo: Eleven year old Willberforce runs in a puddle along an unpaved road near his home in Northern Uganda where he lives with his parents and six siblings.

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