CHAPTER IV – OPERATIONALIZING THE MILLENNIUM DEVELOPMENT COMPACT: AN ENHANCED STRATEGY FOR MEETING THE MDGs

The sections above have emphasized the basic dynamics of poverty reduction, the general conditions in which poverty reduction fails, and the core principles that need to drive poverty reduction policies – all with a focus on identifying the centrality of the MDGs and how the MDGs can be achieved. This section outlines an operational framework at the, country and international level, through which developing country governments, working closely with development partners, could develop and implement long-term strategies to achieve the Goals.

The basic principle underlying the MDGs is to create a goal-oriented international partnership that can help the poorest countries break out of poverty traps. As already suggested in this report, this includes two novelties compared to current international development practice. First, it implies that development processes and policies need to be <u>targeted</u> to achieving the MDGs. Second, it implies <u>partnership</u> in the international community, with improved developing country policies and institutions being matched by coordinated increases in donor assistance, improved rules of international trade, and more active engagement of the international scientific community.

The international system has not yet organized itself to work systematically towards achieving the MDGs through joint efforts by rich and poor countries as well as the international organizations. As a result, there is little goal orientation in the critical international agreements that guide development assistance. In fact most international organizations and bilateral donors do not systematically align their work with the Goals. As one example, the IMF Executive Board receives no systematic information on progress or lack of progress towards the MDGs in low-income countries that have an IMF Poverty Reduction Growth Facility (PRGF).[15] Nor does the IMF staff conduct an analysis of how the country's budget framework should be altered to achieve the MDGs.

There is also little international partnership to date in support of the MDGs. While there is considerable rhetorical attention to the MDGs and specific commitments have been made at several recent international conferences (including Doha, Monterrey and Johannesburg), the actual processes within countries and at the international level are not aligned with the goal of achieving the MDGs. Donor assistance has only slightly increased in the past two years, and is poorly targeted and coordinated to support the MDGs.

Based on the two core principles of goal-orientation and international partnership, we now turn to the Task Force's main operational recommendations. We propose a country-level planning framework that would systematically enable all countries to achieve the MDGs, provided minimum standards of good governance relative to the country's per capita level of GDP are in place. While the precise operational details will differ from country to country and likely evolve over time, the following lays out a core set of guidelines through which the multilateral institutions, developed country governments, developing country governments and civil society could be aligned to ensure all countries reach the Goals.

[15] There has, however, recently been an indication that in early 2004 IMF staff reports will begin to include standardized country-specific MDG evaluations.

1. Country-level processes to roll-out national MDG strategies

This report has already established the need for MDG planning and progress to take place at the country level. The Monterrey consensus outlines how developing countries that commit to good governance and poverty reduction will receive increased support from donor governments in order to achieve the MDGs. To actually achieve the Goals, developing country governments need to follow a two-stage planning process.

Needs Assessments: First, each low-income country should conduct a needs assessment that compares its current situation with MDG targets and identifies the combination of public investments that would enable the country to achieve the MDGs by 2015. This needs assessment will identify the particular obstacles faced in each country that are preventing faster economic development and greater progress towards poverty reduction, covering each of the six policy clusters outlined earlier in this report.

As a first approximation of what a national MDG needs assessment would look like, the Millennium Project has recently worked with local partners to conduct such MDG evaluations for five countries: Bangladesh, Cambodia, Ghana, Tanzania and Uganda.[16] In each of these countries, the Project and local research partner built upon international best practices to identify, in as much detail as possible, the input targets that would be needed for each country to achieve the MDGs by 2015. These estimates cover hundreds of *interventions*, defined as goods, services and infrastructure that need to be provided to meet the Goals. Examples include the provision and operation of rural medical clinics, medicines, sanitation services, textbooks, and school uniforms; the training and employment of skilled professionals; and the construction and maintenance of physical infrastructure. Note that a needs assessment is *not* the same as a policy plan of institutional design, but instead forms a basis for designing policy.

Crucially, a needs assessment provides a framework for scaling up activities over the full MDG time horizon, from 2004 through 2015. The estimates also include local unit costs to assess the financial resources needed to achieve the Goals. In addition to estimating the total needs for meeting the MDGs, the country case studies develop a simple financing strategy, which explores the extent to which domestic resource mobilization towards meeting the MDGs can be increased.

Building Policies Around Needs Assessments: Second, each country needs to develop a long-term (10-12 year) policy plan for achieving the MDGs. Policies identified in this stage will need to be developed through domestic consultative processes and will need to build upon the results of the MDG needs assessment to identify the mechanisms for delivering necessary goods and services. In many instances this stage will require countries to align their long-range policy plans much more concretely with the MDGs than is currently the case. Next each country needs to construct its medium term (3-5 year) poverty reduction strategy (PRS) and, where appropriate, its Poverty Reduction Strategy Paper (PRSP) based on the long term MDG plan. Both the long-term and short-term plans will then need to be periodically reviewed and revised as countries learn from their scale-up experiences and fine-tune policies towards the MDGs.

Note that this does *not* suggest creating new poverty reduction processes. It does imply formulating and revising the content of current approaches based on needs assessments. For

[16] The Millennium Project Working Paper, "Millennium Development Goals Needs Assessments: Country Case Studies of Bangladesh, Cambodia, Ghana, Tanzania and Uganda." January 17, 2004 version is available online at http://www.unmillenniumproject.org/documents/mp_ccspaper_jan1704.pdf.

instance, PRSs are typically three-year financing frameworks, so they need to be built into the national 10-12 year financing plan for MDG achievement. Likewise national budgets need to be built in line with the MDG achievement.

It is crucial to note that current PRSs are not formulated in this manner. Instead, governments in low-income countries are advised by the Bretton Woods institutions to prepare PRSPs on the basis of existing development assistance availability. If existing development assistance flows are insufficient to achieve the MDGs, as is the case in most countries, then the developing country governments are encouraged to be "more realistic" in their targets. That is, they are encouraged to "accelerate *progress towards* the MDGs" rather than to *achieve* the MDGs.[17] Thus the current PRSP process does support progress, but that progress is only directional rather than truly goal-oriented. The difference between the current process and the Millennium Project's recommendations are presented schematically in Box IV.1. This box illustrates the the lack sufficient goal-orientation in current PRSs. It also highlights a deeper point – that current processes do not encourage countries stuck in a poverty trap to make the large scale public sector investments necessary to break free of the poverty trap and to achieve the MDGs.

In summary, the PRSP process needs to be streamlined with long-term national MDG plans if low-income countries are going to achieve the Goals. Beginning in 2004, low-income countries preparing or revising their PRSPs should be invited by their development partners to prepare them based on a rigorous MDG needs assessment. The PRSPs should identify priorities in three areas: domestic policy reforms, increased public investments, and reforms in international trade. The PRSPs should be built on a 12-year horizon, through to 2015, even though the financing commitments from donors and international agencies will be much shorter. Only the 12-year horizon will allow appropriate planning by both the countries themselves and by donors to allow for the gradual and long-term scaling up of human resources, infrastructure and other key sets of interventions.

Having established the need to construct national needs assessments and policy frameworks consistent with the MDGs, the next question is one of organizational design. What should be the process for developing national MDG plans? Recommendations to this end are outlined below.

A. National Governments

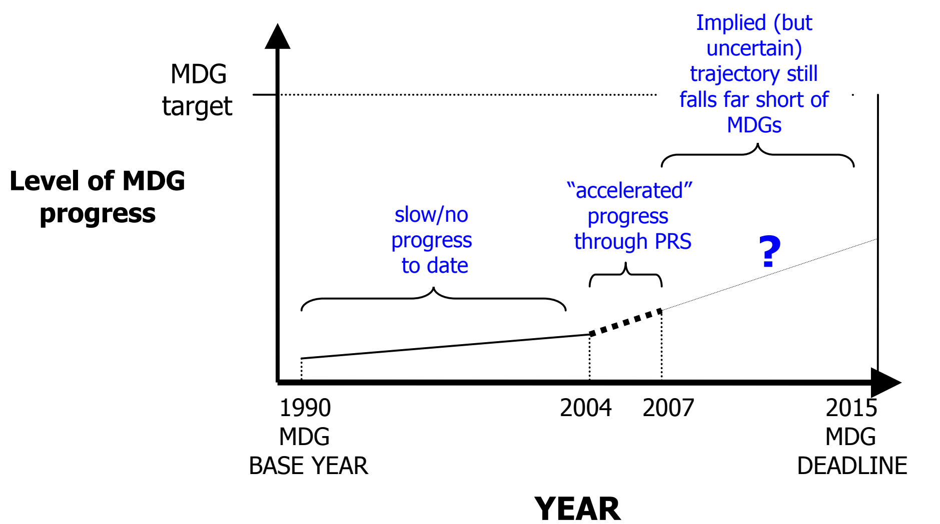
National governments need to lead the planning process. They need to develop and own their needs assessments and policy plans since they are the entity best suited to identifying and addressing local needs. We recommend that governments construct national teams responsible for overall MDG planning coordination. These teams should include senior technical officials from all key ministries – critically not just representatives from the ministries of finance and planning. Specific plans to achieve each of the MDGs must be put forward by sector specialists and then synthesized by the individual(s) commissioned with overall coordination. National MDG planning teams will be crucial for overcoming the common problem of ministries "not talking to each other," resulting in governments not placing adequate emphasis on social and environmental sectors.

[17] The language of "accelerating progress towards the MDGs" rather than "achieving the MDGs" is used, for instance, in the recent World Bank staff paper for the Development Committee, entitled "Supporting Sound Policies with Adequate and Appropriate Financing," September 13, 2003. Paper available online at http://siteresources.worldbank.org/DEVCOMMINT/Resources/Fall-2003/DC2003-0016(E)-Financing.pdf.

Box IV.1: Poverty reduction planning today vs. MDG-based poverty reduction planning

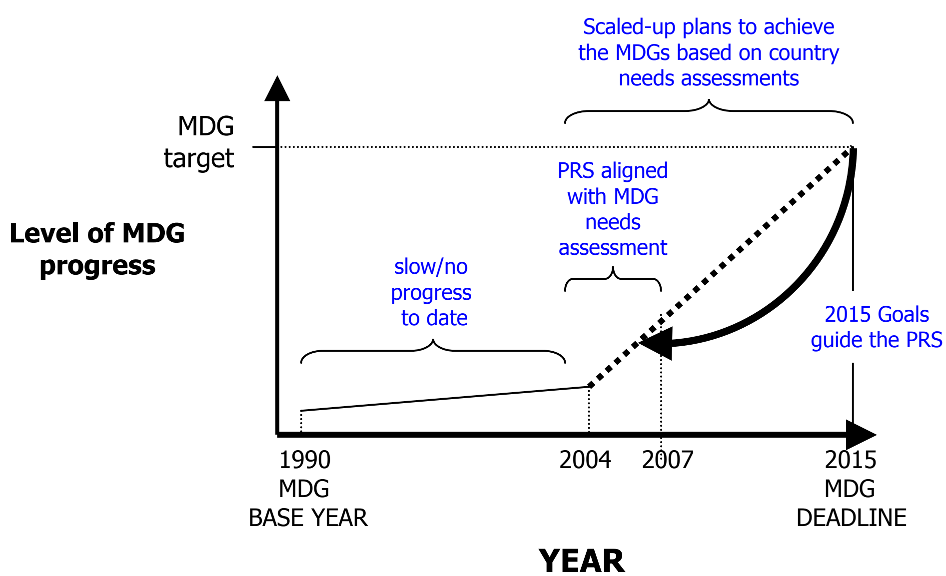
I. <u>Today:</u> Poverty reduction planning in Priority countries

This diagram captures how current poverty reduction strategies in "Priority" countries relate to the MDGs. Movement up the vertical axis represents progress towards the Goals while the horizontal axis represents the progression of time. The left side of the graph shows how the country has so far experienced slow progress toward the MDGs. A short-term PRS supports a slight acceleration in progress, but the implied trajectory is uncertain and far short of the MDGs.



II. <u>Starting in 2004:</u> MDG-based poverty reduction planning

This graph shows how country-level planning needs to work in order to achieve the MDGs. Countries that have made slow progress since 1990 need to draft 2015-based plans for scale-up to achieve the MDGs. The 2015-based plans need to guide the shorter-term PRS and resource allocations.



B. UN Country Teams

UN Country Teams must play a crucial role in assisting national governments as they develop their MDG plans. The poorest countries rely heavily on the UN specialized agencies and the Bretton Woods institutions for technical assistance. The UN agencies provide vital support in almost every sector. Within most low-income countries, the resident representatives of all agencies now meet regularly as UN Country Teams to discuss the development challenges facing the country. These Country Teams report to the UN Development Group, which was established in 1997 by the UN Secretary-General as the overall mechanism for coordination between development-oriented UN agencies.

However, the UNDG is not yet structured to take on this added responsibility. Its key limitation is the lack of operational engagement between the specialized agencies (e.g., FAO, UNDP, UNFPA, UNICEF, WFP and others) and the international financial institutions (i.e., the IMF, the World Bank, and the regional development banks) that set the budgetary and financing priorities for developing countries. While UNDG-World Bank cooperation is increasing, this disconnect is greatest between the IMF and the specialized UN agencies. The IMF works with low-income countries to set their budget framework, including levels of public investments and social outlays. In order to fulfill its responsibility of fiscal stewardship, the IMF needs to have a clear understanding of the levels of public spending needed in key sectors in order for a country to achieve the MDGs. In theory, IMF staff determine this information through consultations with the national government and with the relevant specialized UN agencies. In practice, though, this is not done. *The staff papers sent to the IMF Executive Board for approval do not offer any systematic assessment on the compatibility of a country's macroeconomic framework with progress towards achieving the MDGs.*

Starting in 2004, when a country's budget framework is not compatible with meeting the MDGs, the IMF and the national government should work together to explain how the budget framework can be made consistent with achieving the MDGs. This may require a country to re-orient its own domestic expenditures towards MDG priorities. It may also require increased tax collection. In addition, for the poorest countries, the solution will typically require significantly greater official development assistance to finance increased public sector outlays in MDG-related areas. Increased development assistance might take the form of deeper debt reduction or increased development assistance or both. Opportunities for increased foreign investment and remittance income should also be explored. These increases in ODA are entirely in line with the Monterrey Consensus established between developed and developing countries in 2002. Indeed the Monterrey Consensus states explicitly that, for the poorest countries, there is no realistic prospect of closing the financing gap through private flows.

In the future, the IMF, the World Bank and specialized UN agencies should work much more closely together to assess the development needs of each low-income country and to support a macroeconomic framework that will realistically achieve the MDGs. A promising example of this kind of coordination was provided by the "United Nations/World Bank Joint Iraq Needs Assessment" published in October 2003.[18] The Iraq Needs Assessment involved a process in which the IMF, the World Bank and the specialized UN agencies cooperated closely to determine a public investment and financial framework for economic recovery and development in Iraq. The needs assessment offered a specialized analysis in twelve sectors, which were then aggregated

[18] Available online at http://www.iq.undp.org/UN-WB-IraqNeeds.pdf.

into an overall financing framework that formed the basis of a donors' meeting in October 2003. The assignments for preparing the sector analyses were as described in Table IV.1, with lead agency and cooperating agencies listed by sector.

Table IV.1: Sectoral Assignments for 2003 UN/World Bank Joint Iraq Needs Assessment

Sector	Lead Agency	Cooperating Agencies
Agriculture	FAO	WB, WFP, UNEP
Education	WB	UNICEF, UNDP, UNESCO, UNOPS, UNHCR, UNEP, UNIFEM, UNOCHI
Electricity	UNDP	WB
Financial Sector	WB	
Governance	UNDP	UNCHR, UN/OPI, UNESCO
Health	WHO	UNICEF, WB, UNIDO
Water and sanitation	UNICEF	WB, UNIDO
Mine Action	UNMAS	UNOPS, UNICEF, UNDP, UNEP, WHO, WFP
Employment	UNDP	UNHCR, UN-HABITAT, ILO, UNEP
Housing	UN-HABITAT	WB
Investment	WB	IFC, UNIDO
State Enterprises	WB	IFC
Transport and Telecoms	WB	UNDP, ITU

The needs assessment document laid out a four-year strategy (2004-2007) for meeting specific sectoral and aggregate objectives in Iraq. Specifically, the report called for $35 billion in donor financing over 4 years, or roughly $364 per Iraqi per year. Notably, this figure is approximately 10 times greater than the per capita aid flows to well-governed low-income countries in Africa. It is also 40-50 times higher than the incremental ODA needs calculated by the WB country studies (REF) for Tanzania and Uganda by 2015.

C. Country-Level Donors Committees

In most low-income countries, a committee of bilateral donors exists and is typically organized by the UNDP or the World Bank. The committee of donors is well positioned to support the MDGs, but few have yet played that role. To do so, two things will be needed: much greater ODA flows for the poorest countries, as outlined above, and much better harmonization of aid flows to support the MDGs.

Box IV.2 outlines many of the structural flaws in current ODA development mechanisms that stand in addition to the overall insufficiency of flows. The weaknesses in the current ODA mechanisms reflect the same fundamental problem as that outlined for PRSs. Since international development cooperation is not goal-directed, ODA is not allocated on the basis of a rigorous calibration of needs. Rather, donor governments tend to haphazardly pursue political goals or are swayed by domestic lobbying.

In the future, the donor community should be reorganized to support an MDG-based PRS. Donor assistance should be formulated in light of a rigorous MDG needs assessment. ODA should then be pooled by donors to support national-scale programs in MDG-related areas. This can pursued through Sector-Wide Approaches (SWAps), in which donors pool their money to provide budgetary support to a particular sector like education or health. It can also be pursued through global funds such as the Global Fund to Fight AIDS, TB, and Malaria or the Global Environmental Facility, in which donors pool their money in a multilateral fund that is then accessed to support country-scale programs.

D. Country-Level Trade Committees

In the current international development framework, there is no real venue for low-income countries to seek redress for international systemic barriers such as protectionism in rich-country markets. As part of their repeated commitments to the Millennium Development Goals, the rich countries pledged to support international trade policy reforms in support of economic development. Specifically, Goal 8 commits all countries to "develop further an open, rule-based, predictable, non-discriminatory trading and financial system." This goal should be pursued not only in the context of the Doha trade round, which amplifies the commitment of Goal 8, but also through new institutional mechanisms. [19] We propose that the WTO establish a committee of trade ambassadors in Geneva for each low-income country, charged with identifying specific trade policy reforms in the rich countries to further the development goals of the country in question.

E. Human Right Institutions[20]

As part of the Universal Declaration of Human Rights (1948), and the subsequent Convenant on Economic, Social, and Cultural Rights (1966), governments throughout the world have recognized human rights to adequate food, health, education, decent work, adequate housing, and other basic human needs. Thus, the MDGs can and should be defended not only on the basis of the needs of the poor, but also on their explicit *rights*. These rights can and should be mobilized at the level of the nation and the international community. Specific institutions and legislation designed to protect human rights can be deployed in support of the MDGs.

F. Mobilizing Science and Technology

One of the reasons why many of the poorest countries fail to break out of poverty is the lack of readily available technologies to remove key barriers to development. The poorest countries are often in ecological settings that are distinct from those of the rich countries: the crops are different; the climate and soils pose specific challenges; the plant and animal pests are distinct; and the human disease burdens are also specific to the local environment. For this reason, technological advances in the rich countries are often not immediately transferable to local conditions. In some circumstances, completely new basic research is required to develop solutions adapted to the needs of developing countries.

Consider some examples from the African context:

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[19] The Doha declaration declares, "The majority of WTO members are developing countries. We seek to place their needs and interests at the heart of the Work Programme adopted in this Declaration. Recalling the Preamble to the Marrakesh Agreement, we shall continue to make positive efforts designed to ensure that developing countries, and especially the least-developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development. In this context, enhanced market access, balanced rules, and well targeted, sustainably financed technical assistance and capacity-building programmes have important roles to play.

[20] This human rights component will be an area of significant focus in the Task Force's final report, with key contributions from Task Force member Philip Alston.

Agricultural technologies. Africa, for example, was unable to utilize the high-yield seed varieties of the Asian Green Revolution because of distinctive ecological conditions in most of sub-Saharan Africa (e.g. rain-fed agriculture, vulnerability to periodic drought, low soil fertility, tropical food crops such as sorghum, millet, and cassava). Advanced agricultural research is needed on soil management, tilling systems, water management for agriculture, inter-cropping strategies, germplasms, pest resistance, nutritional supplementation, etc. to increase agricultural productivity in tropical Sub-Saharan Africa.

Health technologies. Africa is uniquely burdened by malaria due to a combination of the high prevalence of *plasmodium falciparum*, the most lethal type of the parasite, highly competent mosquito vectors (with an especially high propensity to bite humans), and high ambient temperatures. This killer disease, which accounts for a massive share of under-5 mortality and countries' overall health burden, is under-researched by the international scientific community, whose attention is heavily focused on the diseases of the high-income countries.

Climate forecasting and adaptation. Much of Africa is vulnerable to drought conditions, especially in the sub-humid tropics close to the equator (e.g. the Sahel). These drought conditions, in turn, are linked to global climate dynamics, including El Niño, and longer-term trends in sea surface temperatures. In addition, tropical Africa is likely to be especially affected by anthropogenic climate change resulting in higher average temperatures and greater variability in precipitation. Thus there is an urgent need for site-specific research on climate trends and options for adaptation to long-term climate change (e.g. through changes in growing season or alternative water-management systems)

Biodiversity preservation. Africa is home to remarkable biodiversity, much of which is currently under extreme stress and even risk of extinction because of massive habitat change under pressures of Africa's growing population. Ecologists and economists need to work together under Africa's specific, indeed unique, ecological conditions, to design strategies for conservation management.

Yet focusing on science and technology is essential not just to solve local problems but also to develop the core processes for technological learning and advancement that underpin economic growth. The Millennium Project Task Force 10 on Science, Technology and Innovation has identified policy and institutional mechanisms for promoting the use, adoption and development of science and technology. Its framework emphasizes the need for low-income countries to focus on building human capabilities through science education, strengthening science advisory mechanisms, and spurring technological entrepreneurship to foster technological learning.

Such specific emphases on the overarching need for improved policies and institutions for science and technology are almost never incorporated into poverty reduction strategies. While new solutions are urgently needed, the range of existing technologies is typically taken as given for purposes of the PRS. As a result, international agencies and bilateral donors rarely decide to fund research projects as part of their assistance efforts to countries. While there have recently been several important initiatives to increase funding for neglected problems of low-income countries, such as disease control and agriculture, these efforts are still very modest in scale. These initiatives for science and technology need to be a systematic focus of a PRS and, where appropriate, PRSP.

G. Private sector engagement

The international business sector can support the MDGs through three forms of participation: (1) core business activities related to the MDGs (e.g. provision of drugs and other technologies at cost to low-income countries); (2) social investments and philanthropic activities; and (3) engagement in advocacy on behalf of the MDGs.[21] The UN Country Team in each country can take the lead in identifying business participants – both domestic and international – for MDG business commissions. The UN can be assisted in this endeavor through various apex organizations, including the International Chamber of Commerce and the World Economic Forum. Members of the UN Global Compact should be encouraged to join these national-level councils.

Meanwhile, the local private sector can also play a key role in national PRS processes. Although most of the PRS in low-income countries will need to focus on the public sector outlays required to create the conditions for sustained private sector growth, private firms should still be involved in the country-level PRS consultations. In particular, local firms should be transparently involved with discussions regarding the promotion of specific industries and reform of domestic economic governance structures. Transparency in these discussions will be of paramount importance, since it will be crucial that politically well-connected firms are not able to profit unjustly through policy change. This will be particularly crucial if private firms are allowed to compete for public-financed service delivery contracts.

H. Civil society engagement

One significant area of policy progress over the past decade has been the growing influence of local, national and global civil society organizations and networks in driving policy change. The successes of the debt relief campaign stand as a leading example of civil society's potential to stimulate constructive change. Non-governmental organizations, community organizations, professional organizations and other civil society groups are regularly called upon to help design and implement PRSs. Their participation is also considered vital to the efforts of the GFATM.

These new approaches reflect the three key roles of civil society in PRSs: as participants in the design of strategies, as service providers through community organizations and national NGOs, and as watchdogs to ensure government fulfillment of commitments. In many countries these roles are taking root only gradually, with governments continuing to dominate decision-making and implementation. By insisting on transparent processes to develop national strategies for the MDGs, bilateral and multilateral development institutions can help civil society play an increasingly constructive role in national policy-making and implementation.

I. Overall Coordination of the International Agencies

Achieving the MDGs in the low-income countries will require an intensified program of global partnership and coordination lasting at least a decade. Many stakeholders have a key role to play: the low-income-country governments; NGOs; other institutions of civil society within the countries and at the international level; bilateral donors; the UN specialized agencies; and the Bretton Woods institutions. This enormous range of actors diminishes the responsibility that any

[21] See *Business and the Millennium Goals: A Framework for Action*, produced by the Prince of Wales International Business Leaders Forum and the United Nations Development Programme, 2003.

single actor has in meeting the MDGs. There is little accountability when cooperation must be so complex and maintained for many years.

It is therefore especially important that all of the relevant actors be subject to some degree of cooperation and review. The natural locus for international cooperation is the United Nations Development Group (UNDG), which is charged by the Secretary General with system-wide coordination in support of development goals. The UNDG could take responsibility for the oversight of the interconnected processes of international agencies that operate at the country level, and could issue annual reports to the Secretary-General and the General Assembly on the progress of each country. These reviews would stress the mutual responsibility of all actors in achieving success in the MDGs, and would aim to hold each of the key actors responsible for their particular contributions to the process.

2. International Processes to Support National MDG Strategies

A. Official Development Assistance

The year 2002 was a landmark in official development assistance (ODA) policy, with donor countries pledging both to significantly increase the amount of development assistance they offer and to improve they way they deliver it in order to make aid more effective in helping to achieve the MDGs. Donors recognized that the amount of ODA currently on offer is insufficient for low-income countries to achieve the MDGs, even in the context of strong policy environments in the recipient countries. At the same time, donors increasingly realized that some of the perceived ineffectiveness of foreign aid was due to their own practices, including poor allocation of ODA, significant amounts of "tied" aid, and overly burdensome and unnecessary requirements on recipient countries. While aid is not the *only* policy lever on which the developed countries must follow-through for low-income countries to achieve the MDGs, it is a *necessary* lever.

i. International Declarations on Official Development Assistance

During 2002 the member countries of the United Nations twice committed to increasing all developed countries' ODA towards the target level of 0.7 percent of GNP. Member countries first made this pledge at the Financing for Development Conference in Monterrey in March, then again at the World Summit on Sustainable Development in September in Johannesburg. It is worth citing the explicit text of those commitments here, since many policy makers do not realize how specific these commitments were. First, paragraphs 41 and 42 of the Monterrey Consensus document state:

> We recognize that a substantial increase in ODA and other resources will be required if developing countries are to achieve the internationally agreed development goals, including those in the Millennium Declaration. To build support for ODA, we will cooperate to further improve policies and development strategies, both nationally and internationally, to enhance aid effectiveness. In that context, we urge developed countries that have not done so to make concrete efforts towards the target of 0.7 per cent of gross national product (GNP) as ODA to developing countries and 0.15 to 0.20 per cent of GNP of developed countries to least developed countries (UN 2002b).

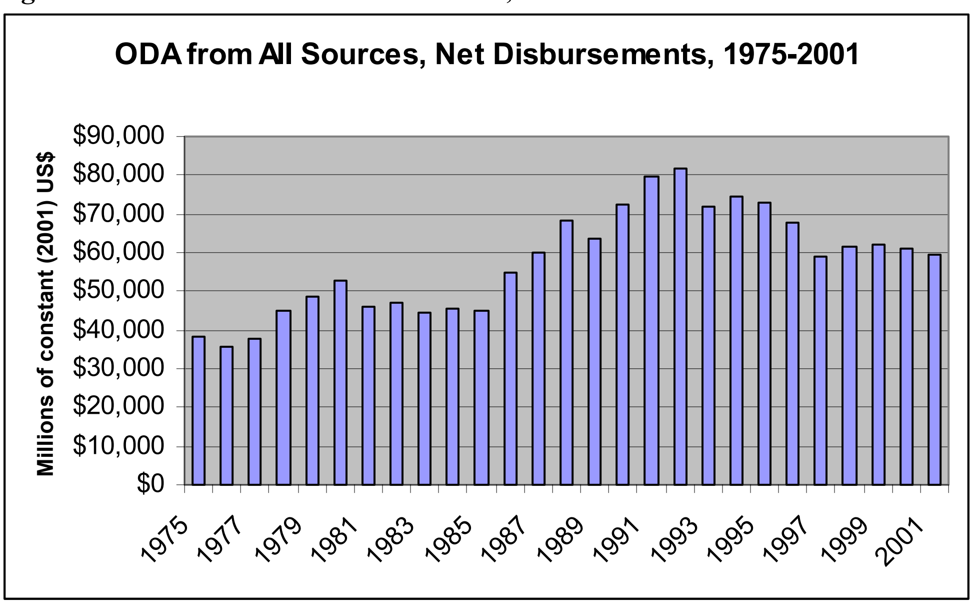
Similarly, paragraph 85 of Johannesburg Plan of Implementation asserts almost precisely the same commitment, ending with the same key sentence:

> *[We] urge the developed countries that have not done so to make concrete efforts towards the target of 0.7 percent of gross national product as official development assistance to developing countries* and 0.15 to 0.20 per cent of GNP of developed countries to least developed countries"[italics added] (UN 2002c).

It would be difficult to overstate the importance of these two commitments by the member states of the United Nations. These are the international community's firm commitment to a tremendous increase in ODA. Importantly, they were again reconfirmed by the leaders of the G8 countries at their 2003 annual meeting in Evian, France, where heads of government "Reaffirmed [their] commitment to address the challenge of global poverty and [their] support for the Millennium Development Goals and the Monterrey consensus" (G8 Summary 2003 Section 2).

While aid is not the *only* policy lever on which the developed countries must follow-through for low-income countries to achieve the MDGs, it is a *necessary* lever. As shown in Figure IV.1 below, current ODA levels are slightly more than $59 billion, or 0.23 percent of the rich country's total GNP of approximately $25 trillion per year. This $59 billion includes non-DAC bilateral aid, non-DAC ODA channeled through multilaterals, and ODA from the European Commission. An increase to 0.7 percent would be equivalent to $175 billion, or roughly an incremental $120 billion per year. If the rich countries continue to grow at a sustained real per capita rate of 2 percent per year, 0.7 percent would be equivalent to $215 billion in 2015, or an extra $165 billion over today's levels.

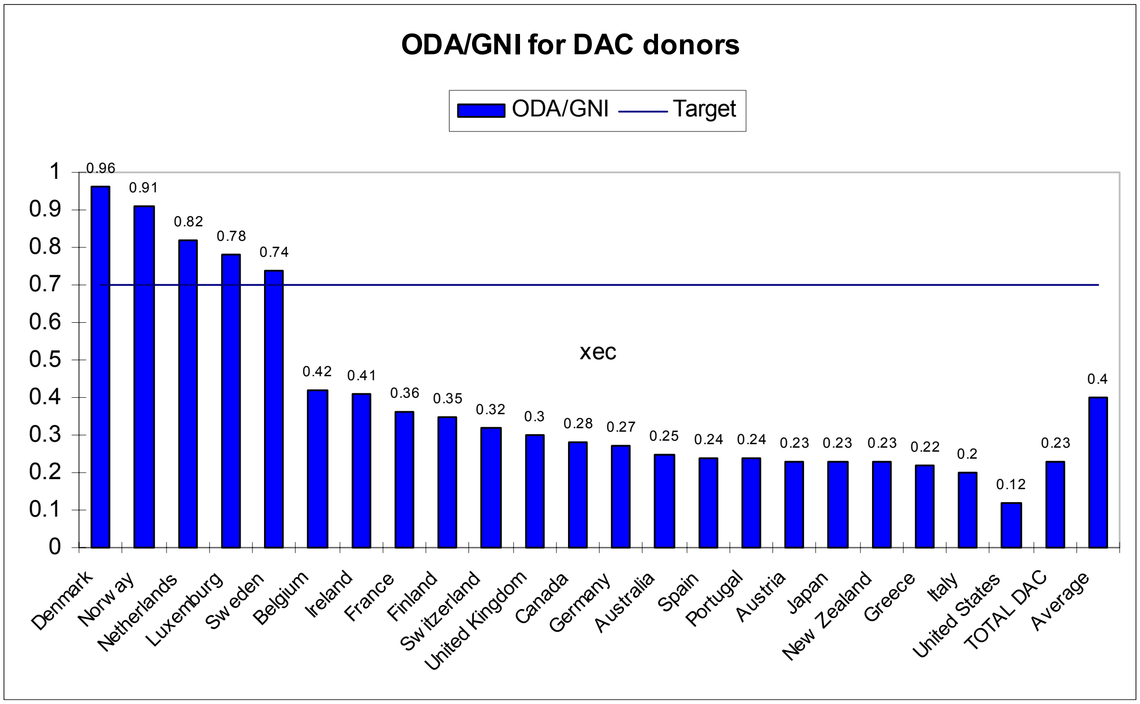
Figure IV.1: Net Disbursements of ODA, 1975-2001



Source: DAC Table 1.

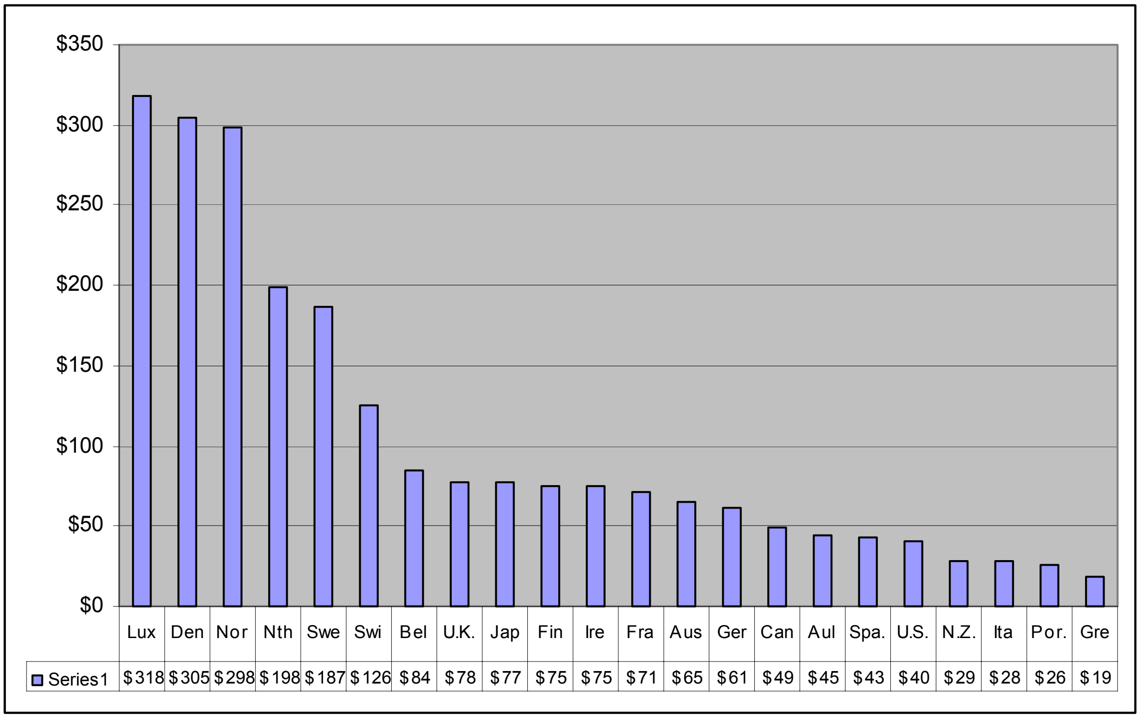
It is important to note that several countries have already achieved the 0.7 percent target, as shown in Figure IV.2 below. Denmark, Norway, Netherlands, Luxembourg and Sweden are the world leaders in development assistance. A majority of countries fall well below that level, with Belgium as the sixth highest as a percentage of national income at 0.42 percent. Importantly for absolute global levels of aid, the United States ranks last at 0.12 percent. As the world's largest economy by far – with more than one third of the rich world's annual income at $10 trillion per year – the United States is the largest ODA donor on an absolute scale, but its low proportionate ODA level needs to be overcome in order to achieve the MDGs. If the United States were to increase its ODA to only 0.4 percent of national income, that would be equivalent to an extra 30 billion dollars a year, or roughly a 50 percent increase in total global development assistance compared to today. Similarly Japan, as the world's second largest economy, at approximately $5 trillion per year, could provide major improvements in global development trends with even similarly small proportionate increases in ODA.

Figure IV.2: ODA as a percentage of gross national income (GNI), 2002.



Source: DAC Press Release, "OECD DAC Countries Begin Recovery in Development Aid: 5% Increase in 2002," dated 22 April, 2003. [http://www.oecd.org/dataoecd/43/56/2507734.pdf].

Figure IV.3. ODA per capita, by donor.



Source: DAC Table 1, and OECD Population Information Sheet (http://www.oecd.org/dataoecd/62/38/2698549.pdf).

ii. How Much ODA is Needed to Achieve the MDGs?

Increasing aid substantially towards the 0.7 percent goal is crucial as a clear and incontrovertible international commitment. But one needs to ask how analytically sound it is. The ODA originally target originally grew out of the Pearson Commission's recommendations in 1969, decades before the adoption of the MDGs (Commission on International Development 1969). Thus the questions arise: How does 0.7 percent relate to the achievement of the MDGs? Would it be enough to achieve the Goals?

To date, two prominent studies have assessed how much ODA is needed to achieve the MDGs. Both were published in advance of the March 2002 Financing for Development Conference in Monterrey. The Report of the High-Level Panel on Financing for Development (United Nations 2001), chaired by former President of Mexico (and current co-Coordinator of the Millennium Project Task Force on Trade) Ernesto Zedillo, estimated that approximately $50 billion in additional official development assistance (ODA) will be required each year to meet the MDGs.

Meanwhile, a World Bank study used two different approaches to estimate resource requirements for achieving the MDGs (Devarajan *et al*. 2002). The first approach estimated the cost of meeting MDG Target 1, which calls for halving income poverty by 2015, while the second assesses the costs of achieving the health, education and environment MDGs. According to the authors, both methods will lead to similar results since halving poverty will lead to the achievement of many of the other Goals, while investments in health, education and the environment will help achieve Target 1. The study estimated that an additional $40-60 billion in ODA is needed each year to meet the goals in 2015, although it did not include a detailed assessment of how these resources would translate into country-level investments.

Since these studies take a very high-level approach to calculating the need for additional aid, the Millennium Project has initiated a "needs assessment" approach to the MDGs by working with local partners in a series of country case studies – Bangladesh, Cambodia, Ghana, Tanzania and Uganda – to calculate, in considerable detail, the public investments required to achieve the MDGs in those countries. While the country-level results are preliminary and the methodology for aggregating to the global level is still being refined (see www.unmillenniumproject.org for the current draft), the early results suggest that achieving the MDGs will require *at least* a doubling of aid *(that is, to at least 0.46 percent of donor GNP)* but less than the international target of 0.7 percent of GNP. The necessary increase could be on the lower end to the extent that donors improve the quality of aid, for example by reducing the portion of aid that is "tied" to purchases in the donor country, or by improving the harmonization of donor administrative requirements, as discussed below. In other words, the ODA needed to achieve the MDGs is likely entirely within the realm of current international commitments. No new ODA commitments need to be made to achieve the MDGs; current commitments merely need to be followed through upon.

iii. Improving the Quality of Aid

For substantially higher levels of ODA to be used productively in accelerating low-income countries' progress towards the MDGs, there will also need to be changes in the ways in which donors provide their assistance. As the World Bank has outlined, to achieve the MDGs donor assistance needs to follow four guiding principles:

1. A larger share of ODA should be allocated to those recipient countries with better governance and with greater needs.
2. ODA levels need to be coherently aligned with national MDG-based strategies
3. Overall donor assistance needs to be harmonized and coordinated across donors
4. ODA needs to be disbursed in a predictable and timely manner
5. ODA financing mechanisms need to be reconfigured to focus on cash outlays, to support recurrent costs, and to be "untied."

Aid Allocation

In general, donors do not allocate aid very efficiently towards countries that need it the most or can use it most effectively. Significant amounts of aid budgets go to middle-income countries, where poverty is not as acute as in the low-income countries. Similarly, some donors provide substantial amounts of aid to countries with relatively poor governance, little commitment to implementing effective development strategies, and a weak record of using aid effectively. Several donors have begun to take steps in recent years to improve aid allocation, but more steps in this direction are necessary in order to make the most progress as possible towards the MDGs from any level of total aid.

Making ODA more effective will depend on the commitment of both recipient country governments and donor governments to ensure development cooperation is successful. One frequently-discussed component of this is recipient country's quality of governance and hence ability to apply increased aid to the MDGs in an effective manner. One often-overlooked aspect of such discussions is that quality of governance tends to increase with economic development, since richer countries can afford better public institutions. Quality institutions definitely are an important factor in reducing poverty, but they are far from the only factor. Thus, when assessing countries' governance levels, a more important question than "How good are there public institutions?" is "How good are there public institutions relative to their level of GNI per capita?"

Many poor countries have weak governance on a global scale but extremely competent governance for their level of economic development. These countries require tremendous support in bolstering their investments to achieve the MDGs.

MDG coherence in donor assistance
The first principle guiding donor assistance should be the achievement of the MDGs. As already described, achieving the Goals will require developing countries to develop rigorous scale-up plans through 2015 that will guide medium-term and short-term policy frameworks. At the core of the Monterrey Consensus lies the idea that developing countries must take this responsibility to develop and implement sound plans to achieve the Goals and they will receive the necessary donor support to finance these strategies. Thus, to achieve MDG policy coherence, donors need to coordinate their assistance to support long-term national MDG plans and, in turn, shorter-term PRSs. This implies donors pursuing developing countries' MDG policy and program priorities, rather than donors pursuing programs and projects driven by their own individual priorities.

Coordination and harmonization of donor assistance
Closely linked to the notion of coordinating donor activities to ensure coherence in the context of national MDG plans, in order to improve efficiency, aid delivery needs to harmonize institutional requirements and operational procedures and practices across donors. There are currently 23 members of the DAC. Asking low-income countries with scarce human resources to prepare separate funding proposals, monitoring plans, procurement strategies, and evaluation procedures for each donor results in at least an order of magnitude of extra and unnecessary administrative resources being allocated to donor requirements. These developing country resources will be much better utilized in drafting and leading plans and policies to achieve the MDGs. Harmonization practice has varied in the extent to which recipient countries' systems are used as the basis for common donor procedures and practices. Here the tension lies between reaping the benefits from harmonizing around the countries' own processes on the one hand and maintaining fiduciary standards acceptable to various donors.

Perhaps the best way of achieving improvements in both policy coherence and efficiency is to shift donor assistance to direct support for public budgets rather than for projects and programs, at least for those recipient countries with the appropriate institutional mechanisms in place to support such a change. A leading example of this is embodied in the recent application of sector-wide approaches (SWAps) to development financing. While the details have differed by country and sector, the core principle has been for donors to pool their resources into contributions to government budgets – health budgets have been at the fore of this development. While progress in developing SWAps has been significant, country-specific details still vary to reflect compromises between recipient governments' benefits of harmonized procedures and individual donors' desires to be associated with particular project components. Moreover, budget support and SWAps may not be appropriate in countries with weak budget systems, little fiduciary oversight, and poor governance, where there is less confidence that funds provided to the budget will be used as pledged.

Predictability and timeliness of financing
The issues of predictability and timeliness of financing are extremely important for recipient countries. First, donor assistance should be provided in a manner linked to recipient countries' budget cycles rather than donor countries' programming cycles. This would help countries plan ahead within the context of a medium-term expenditure framework. Second, these commitments should be made over a period consistent with the MDGs, *i.e.*, through to 2015. While mid-course adjustments and reviews will undoubtedly be necessary, in order to pursue a true MDG strategy the recipient countries will need to know that their development partners share an equal, long-term commitment to achieving the MDGs. Third, the sustained policy and governance reforms required to make fast progress towards the MDGs are necessarily long-term in nature. Governments can only make the proper reforms and investments if they have a reasonable degree of confidence in the resource levels that will be available. This implies that they require confidence in the stability and trajectory of external assistance and the conditions under which the resource inflows are scheduled to materialize. Moreover, upfront commitments from donors that link to recipient countries' policy performance will allow countries greater confidence in the delivery of aid over an extended period of time and help create a virtuous circle through which recipient country governments can initiate and sustain improvements in their public policies and institutions.

Reconfiguring financing mechanisms
Three major issues require attention if donor financing mechanisms are to be reconfigured in alignment with the MDGs. First, a greater share of aid needs to be provided in the form of grants (rather than loans) and direct cash outlays. Particularly for highly-indebted countries with good policies and governance but a high degree of susceptibility to shocks, a greater share of aid needs to be provided in the form of grants. Redirecting assistance towards grants will help address concerns that higher aid flows intended to assist low-income countries make faster progress towards the MDG targets might increase the risk of debt distress in the future.[22]

Second, financing plans, particularly those designed to support long-term national MDG plans, must include recurrent as well as capital costs. Historically, donor programs have helped to finance capital expenditures and then aspired for projects and programs to meet tests of "sustainability" and local commitment by supporting the recurrent costs locally. This is not a very useful approach since in many sectors operating costs account for a very large share – if not a majority – of total outlays (e.g. education, health, water and sanitation, etc.).

Reflecting the lack of emphasis on this issue, the World Bank does not even keep data for the recurrent unit costs of projects supported throughout its decades of assistance for large scale project and government assistance. However, an increasing number of donor organizations are beginning to realize the need to focus on recurrent costs as well as the fact that the poorest countries simply cannot afford to pay these costs. For example, medical professionals are integral to a functioning health system but they are typically too expensive for a government to afford at anywhere near a scale required to achieve the MDGs. Training and employing health professionals needs to form a central component of any national MDG plan, and will require external assistance in order to succeed. Thus the traditional notion of "project sustainability" needs to be abandoned in the poorest countries. To get out of the poverty trap described in chapter II of this report, the poorest countries are going to require sustained external assistance in order to

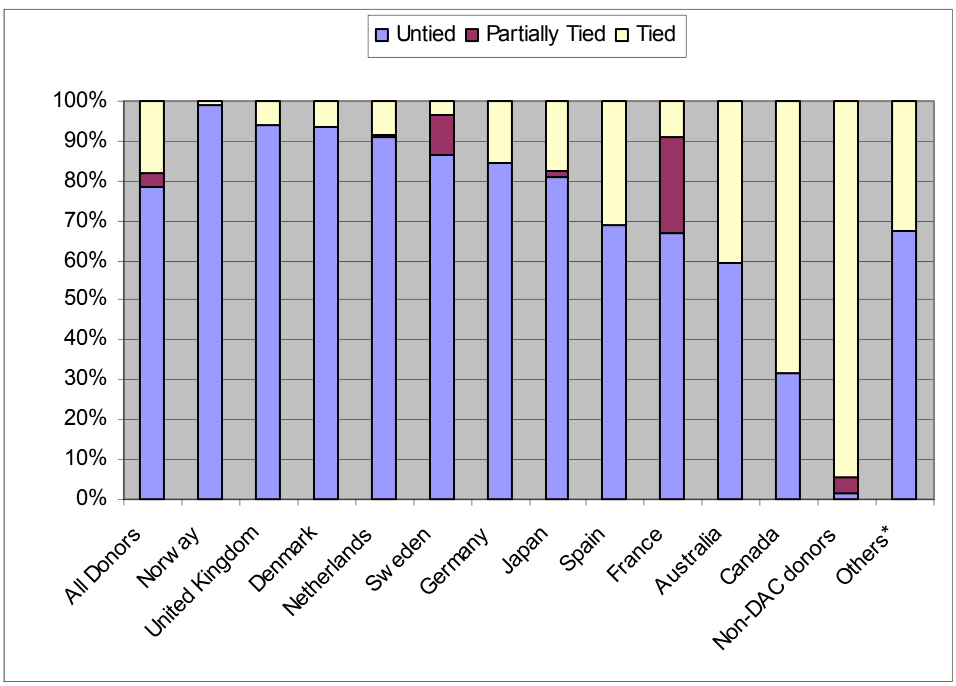
[22] Of course, the necessary shift towards grants raises other issues to be addressed, including the implied substantial increases in development assistance and the long-term viability of the concessional lending affiliates of the multilateral development banks.

develop a public sector sufficient to support the conditions for sustained economic growth and the achievement of the MDGs.

Third, a large proportion of aid, particularly bilateral aid, is still "tied," *i.e.*, goods and services must be purchased from the donor country (fully tied aid) or a limited group of countries (partially tied aid). For example, with tied aid a recipient organization may be compelled to import its office furniture from the donor country at vastly higher cost, thus wasting scarce resources. Most empirical estimates suggest that tied aid raises the costs of goods and services by 20-25%, which significantly undermines the effectiveness of existing aid.

As Figure IV.4 outlines, the variance of tying differs significantly by country. While over 90 percent of ODA from Denmark, the Netherlands and the United Kingdom is untied, almost two-thirds of Canadian bilateral aid is tied. According to the U.S. Congressional Research Service, approximately 70 percent of USAID's outlays were tied in 2000/01 (Tarnoff and Nowles 2001). Despite some donor countries lack of progress is this area, the overall movement to untying aid is positive particularly for the poorest countries. Following the agreement at the High-Level Meeting of the OECD Development Assistance Committee (DAC), all DAC members agreed to untie aid to the Least Developed Countries. As of January 2002, three-quarters of all bilateral aid to LDCs is untied, so increasing this proportion must remain an important policy priority for donor countries. Likewise the untying of aid remains a significant priority for aid to non-LDC low-income countries – such as Cote d'Ivoire, India and Kenya – and for middle-income countries.

Figure IV.4. Tying Status of ODA, by Donor, 2001.



Note that this table excludes the United States, whose ODA tying status is not reported to the OECD DAC. However, Congressional Research Services estimated that 70 percent of US aid was tied in 2000/2001.
Sources: DAC Table 7; Curt Tarnoff and Larry Nowles, "Foreign Aid: An Introductory Overview of U.S. Programs and Policies," Congressional Research Service Report 98-916F, April 2001.

Finally, a core debate in development policy concerns the role of broad horizontal and targeted vertical funding mechanisms. The Task Force has not yet taken a position in this debate, but discusses the relative merits of each in Box IV.2.

Box IV.2: Funding Mechanisms to Achieve the MDGs: Vertical versus Horizontal

Much debate in development circles has recently focused on the relative advantages and disadvantages of vertical and horizontal funds as donor financing mechanisms. "Vertical funds" are those that focus on a particular issue or a small number of related issues, typically financing programs and projects encompassing all aspects of the issue. These funds have a long history, starting with the United Nations Children's Fund (UNICEF), which was established in December 1946. There are many other examples, including the UN Population Fund, the World Food Program, the Global Environment Facility, the Global Alliance for Vaccines and Immunizations, and the recently founded Global Fund to Fight AIDS, TB and Malaria (GFATM). Horizontal funds provide financing for a wide range of interlocking issues across a broad spectrum of development challenges. Most of the major donor agencies operate as horizontal funds, including the World Bank, regional development banks, UN Development Programme, and the major bilateral donors. Some donor mechanisms are meanwhile a combination of horizontal and vertical, such as the World Health Organization.

Vertical Funds

There are several advantages to vertical funds. First, they help draw public attention to specific problems (e.g., specific MDGs). UNICEF has increased awareness of the particular problems facing children through various campaigns over the years, in particular when it was awarded the Nobel Peace Prize in 1965. More recently, GFATM has focussed world attention on HIV/AIDS, TB, and malaria. The more diffuse mandates of horizontal funds make it more difficult for them to draw attention to specific problems, since by design they are drawing attention simultaneously to a wide range of issues. Second, vertical funds can help mobilize donor resources because of their focus on a narrow set of issues. Individuals, foundations, and government budget officials tend to be more willing to provide financing if they have a clear idea what it will be used for. For example, it is often easier to get potential donors excited about providing financing for HIV/AIDS, children's health, or famine victims than for broad health or agricultural systems. In this vein, one could consider the possibility of organizing new vertical funds focussed on one or more of the MDGs as a way of generating more funding and greater attention on that specific goal.

Third, vertical funds can often maintain a sharper focus on specific goals. They can specialize their activities and develop advanced expertise and high skill levels in specific areas. This specialization and expertise can help improve the full range of donor activities including program design, implementation, monitoring, and evaluation. There is an analogy here with private firms that specialize in producing niche products or services. By contrast, horizontal funds take a broader approach with less focused goals, and their broad mandate can lead to continued expansion into new areas. Generally speaking, horizontal funds require staff with more generalized knowledge across several areas, rather than high-level expertise in one area. Of course, horizontal funds can include many staff with high level expertise in particular areas, in addition to generalists (as with the World Bank).

Box IV.2 (continued)

Horizontal Funds
Meanwhile, horizontal funds offer clear advantages of their own. First, they typically take a more integrated approach, recognizing the interrelationships across issues. They are better placed to fund programs and projects that cut across issues, for example such as the impact of women's education on health. Vertical funds tend to miss out on these inter-linkages, and partly as a result, tend to expand their focus over time. UNICEF started by focusing on food, clothing, and health for children, and over the years has added education (including teacher training), gender, child labor, armed conflict, and other issues. In other words, horizontal funds are better placed to consider the linkages between and complementarities across the MDGs.

Second, horizontal funds can finance broader sector strategies or multi-sector development strategies. Vertical funds can plug into one aspect of a broader development strategy, but are less helpful on designing the broader strategy itself. Thus, a horizontal fund would be better placed to finance, for instance, a complete MDG-focused PRSP. Third, horizontal funds tend to put more focus on broader institutional capacity building issues. For example, the World Bank is more likely to focus on sector-wide health capacity issues than a narrower vertical fund, and is better placed for an even broader focus such as on the entire public finance system. While vertical funds can also build capacity in their particular areas of interest, they tend to have less focus on broader capacity issues. For example, UNICEF historically has focused on particular children's health issues, but less so on broader health systems. Similarly, there is some concern that GFATM's focus on AIDS, tuberculosis, and malaria may lead to less attention being given to broader health systems.

Fourth, horizontal funds can provide financing for lower-profile (but still important) issues that may fall through the cracks of vertical funds. Deworming tablets or training for budget officials may not attract the attention of a vertical fund, but can easily be covered by horizontal funds. Similarly, while the MDGs each represent important issues, they are by no means complete recipes for development. They say little explicitly, for example, about energy, infrastructure or private sector growth . Vertical funds focused on specific MDGs would run the danger of missing out on or under-emphasizing some of these other issues. Fifth, in terms of additionality and fungibility, horizontal funds are better placed to assess whether donor funds are truly additional, or whether increased funding in one area comes at the expense of another. For example, it is possible that while GFATM provides additional funding for HIV/AIDS, TB, and malaria, this funding may come at the expense of other health issues or funding for other non-health development issues. In principle, horizontal funds could be more efficient by avoiding overlapping programs and duplication of effort and by easing communication across activities.

Horizontal and Vertical support for National MDG plans
Notably, both horizontal and vertical approaches can be consistent with the increases in pooled funds and budget support that this report has outlined as necessary for low-income countries to achieve the MDGs. For example, a vertical fund that is large in scale and narrow in scope (like GFATM) can provide a common pool mechanism to which many donors can contribute. Some (or all) of these funds could be provided as budget support. Horizontal funds can provide a vehicle for pooling and budget support across a broader range of activities. However, vertical funds may be more difficult to link to a recipient country's budget than horizontal funds, because it may be harder to balance their country-specific allocations with the amounts that emerge from a recipient country's budget process.

Box IV.2 (continued)

The Task Force intends to consider the issues of horizontal and vertical funds in more detail as part of its work plan in 2004.

Source: Steve Radelet (2003), Task Force Background Note

Macroeconomic Frameworks for Expanded Public Investment[23]

In order to accommodate the higher aid inflows required to achieve the MDGs, recipient countries will need to develop their macroeconomic planning frameworks accordingly. Many low-income countries have faced severely binding resource constraints for many years so formulating, executing and monitoring spending plans involving relatively large amounts of resources will pose a new set of challenges. These challenges will need to be surmounted through active collaboration between recipient country governments and the IMF, since the latter typically provides the international community's professional review of national macroeconomic frameworks before endorsing inflows of financial assistance.

The macroeconomic framework underpinning a country's PRS must address two key issues. First, it should account for the uncertainties associated with a country's vulnerability to exogenous shocks, which could undermine the success of its overall poverty reduction effort; and second, it must provide a practical basis for the formulation and execution of government policies. Even modest assumptions regarding growth, budget revenues and exports can have adverse consequences when countries are forced by circumstances to adjust mid-stream by reducing expenditure, incurring new debt or resorting to inflationary sources of financing.

External shocks are a particularly significant issue for low-income countries, since they are usually more vulnerable to them and economically harder hit by them than richer economies. This is because these countries often depend, as outlined in Chapter II, on a narrow commodity-based production and export structure; they rely heavily on the agricultural sector for creating output and employment with a greater percentage of their populations living in marginal areas; and they generally have low domestic savings and weak risk management capability. Exposure to shocks can seriously undermine a country's ability to implement its MDG strategy if its macroeconomic framework does not account adequately for the likelihood such shocks will occur.

Given these risks, the macroeconomic projections underpinning a country's development strategy must be based on a consistent and attainable set of macroeconomic assumptions, an explicit analysis of the sources of and obstacles to a country's economic growth, and an assessment of the major downside risks and uncertainties arising from external shocks and slippages in policy implementation. The government and the IMF need to work together to conduct the relevant sensitivity analysis and alternative scenario analysis. However, beyond analysis, the countries most at risk of external shocks also need contingency plans for assistance from donor countries in order to help balance the risk. With a very modest amount of their own resources, the rich countries could help to share this risk and lessen the persistent burden of shocks on the poorest countries.

While it might seem a small or obvious point for donors to provide additional risk-absorption support to the poorest countries, it is important to note that donor governments are a frequent

[23] Portions of this section draw upon a background note contributed to the Task Force by the International Monetary Fund.

source of risk for low-income countries. For instance, macroeconomic frameworks underpinning national PRSs have often assumed that sufficient concessional foreign assistance would be forthcoming to finance the spending required to achieve countries' poverty reduction goals, but then donors have frequently either not provided the requisite assistance or failed to follow-through on aid commitments.

Add to these risks the administrative challenges of developing the human resources and managerial systems required to accommodate higher spending and aid flows, and the practical challenges of expenditure framework planning can be considerable. Moreover, expenditure frameworks have not always been consistent with those on which annual budgets, and thus donor support, are based, and which generally reflect more conservative assumptions regarding expected aid flows, growth, and other key macroeconomic variables. This combination of complications is amplified when a time horizon and ambition is aligned with the MDG targets for 2015. Fortunately, the MDGs provide a common reference point around which low-income countries and international agencies can begin to implement coherence.

Partially to address the challenges of macroeconomic planning for the MDGs, the Development Committee of the IMF and World Bank recently proposed to support countries requesting the development of "alternative scenarios to reach the MDGs,"[24] suggesting one in which sufficient resources are available to meet the MDGs and another in which countries must continue under current resource constraints. Although such a two-scenario approach still falls far short of coherent planning to achieve the MDGs, it clearly represents a step forward in recognizing and making explicit the key resource constraints faced by many low-income countries.

In developing an explicit MDG-based macroeconomic planning scenario, the substantial increase in aid inflows required for many countries to achieve the MDGs raises a number of issues to be considered carefully. First are the structural macroeconomic issues. Governments should not spend what they don't have – especially through domestic credit expansion. The increases need to be financed through increases in ODA rather than domestic credit expansion. The increases in ODA will need to be focused on grants more than loans. Even concessional loans will probably prove to be prohibitive, given the scale of ODA needed relative to GDP. This will require a change in the financing rules for IDA and some other multilateral creditors. Countries will need to have exchange rat systems compatible with these increased inflows. The specific details for each country needs to be discussed and determined with technical advice from the IMF.

Closely related, governments and the IMF will need to assess carefully the impact of the aid inflows on fiscal and external debt sustainability, as well as the implications of the higher aggregate spending on the medium-term fiscal outlook and the recurrent cost implications of such spending within the context of a multi-year public expenditure framework. Debt cancellation will need to be deepened in most cases in order to meet the MDGs. Looking forward, countries must also maintain their efforts to mobilize domestic revenue and foster domestic savings and investment in order to support long-term economic growth.

Third, in many low-income countries the needed aid flows will be large relative to GNP, so they need to be highly predictable. Slippage of a few percent of aid could also be several percent of GNP, and hence a major macroeconomic factor. Donors will have to be much more careful and cognizant of the possibility that they themselves could become a destabilizing factor. Second, the

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[24] See Paragraph 11, Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries, "Development Committee Communique," September 22, 2003.

increased aid flows could and probably will, have at least a small Dutch disease effect of real exchange rate appreciation. This will be manageable, according to recent IMF internal assessments of the issue, but still needs to be taken into account. The aid flows will be a form a positive "shock" (as desired) in particular sectors with large salary components of expenditures, such as health care and construction, where real wages for skilled workers are likely to soar. This is to be expected and even desired (to stop brain drain), but it must be anticipated economically and politically.

Fourth, the administrative capacity within the government to maintain the quality and efficiency of any additional aid-financed spending must be enhanced in pace with the increased aid flows. This will require a long-term administrative scale-up program. Countries will also need to develop their ability to monitor and evaluate the results of higher spending on services. In many cases donors will need to provide targeted assistance to partner countries to overcome and constraints in administrative capacity.

Monitoring and Evaluation

Central to the discussions above is the notion of monitoring and evaluation (M&E) in the aid process. There are many reasons why donors and recipients should design strong M&E systems. Foremost are fiduciary and financial requirements to make sure funds are spent where intended. Governments and taxpayers in donor countries have a reasonable desire to ensure their contributions are not being stolen. A second reason is to modify and strengthen programs to ensure progress towards intended goals. Effective M&E can help detect design or implementation problems at an early stage and allow for mid-course corrections. It can likewise help to pinpoint administrative bottlenecks, whether lack of physical infrastructure, trained personnel, or administrative services. Third, M&E can provide incentives for success. Well-designed M&E programs can be the objective basis for rewarding programs that show strong results and penalizing those with weak results. It can also help to inform the broader publics in both donor and recipient countries about where aid works and where it does not. The general skepticism that prevails about the effectiveness of foreign aid can only be countered with clear evidence about the circumstances in which aid can be effective and where it is not.

Unfortunately, many donors frequently discuss the role of strong M&E programs as critical to performance-based financing, but typically these programs are weak and ineffective. Most M&E efforts focus on financial and fiduciary monitoring aimed at ensuring funds are spent where they were supposed to be spent, with a minimum of theft and misappropriation. Much less effort is directed to ensuring the substantive results of aid-financed programs in order to reallocate funds towards their most effective use. Nor is much systematic effort used to learn what kinds of programs work best and which do not at all.

If the world's developing countries are going to achieve the MDGs and donors are going to follow-through on their commitments to give sufficient aid to ensure those achievements, M&E will be critical. The necessary scale-up of aid levels and reform of aid composition will undoubtedly require ongoing organizational learning in order to ensure consistent improvements in aid effectiveness. Donor and recipient governments will need to focus on four core dimensions of M&E as they design specific policies and programs to achieve the MDGs: fiscal accountability; institutional strengthening, substantive goal-orientation, and benchmarking progress.

- To ensure fiscal accountability, donors and recipients need to ensure that resources are spent where they were supposed to be spent, that programs remain within budget, that regulations on procurement and payment are followed, and that funds are not stolen. This is the traditional focus of M&E.

- To strengthen institutions, M&E needs to focus on administrative systems, such as reducing the time to close accounts at the end of the month, removing ineffective bureaucratic procedures, and enhancing bureaucratic skills levels. Donors and recipients should specify precise goals in these areas during the program design phase. These institutional goals have historically been underemphasized by donors, at least in terms of specifying concrete targets and measuring progress against them, although that has changed to some extent in recent years.

- To ensure progress towards substantive goals in, for instance, health, education or other sectors, programs needs to establish specific targets for key outputs. For example, the provision of bed nets could be an intermediate target for the overall goal of reducing malaria incidence.

- Across the three areas above, benchmarks for progress are required. An important question is who should set the benchmarks? Traditionally donors have set the goals, but recently donors have moved towards a more consultative process in program design. A cooperative approach to setting benchmarks between donors and recipients is necessary in order to ensure their fully shared understanding and ownership. To monitor progress effectively, it is essential that implementers gather relevant baseline data at the outset of every project and program, and that the progress be monitored continuously throughout. In too many aid projects, monitoring and evaluation begin only two years into the project, for a “mid-term” review. A serious commitment to benchmarking progress requires committed resources – time, staff and money – from the outset of a project.

The most serious technical difficulty in M&E is attribution of a particular project or activity to observed outcomes. Even when a specific outcome has occurred, it is often difficult to assess the contribution of a particular organization, group of organizations, or even a particular strategy. This is because the outcomes generally result from the interplay of many variables. The longer the time horizon, the more likely that other variables have influenced the outcome, either negative of positive. For example, a program aimed at increasing agricultural productivity could be very successful, but may be interpreted as a failure if other factors (such as drought, pests or disease) intervene to reduce productivity. On the flipside, a particular activity could be judged to be a success when it really was not, if other factors helped to achieve the specific goals. Randomized or controlled trials are more successful at correctly attributing the role of specific activities to outcomes, and should be conducted more thoroughly, but this procedure cannot be used for all M&E activities.

iv. ODA for Countries with Weak Governance or Conflict

The countries with weak governance or in conflict roughly correspond to those that the World Bank refers to as Low Income Countries Under Stress (LICUS) and the OECD calls "Difficult Partnerships." Some of these countries are failed states, others are failing, while still others could be considered weak or fragile. These countries must be dealt with on a careful, case-by-case basis, as the circumstances on the ground can vary widely. Some countries are in a downward cycle, where the political and economic situation appears destined to get worse before it gets better. Others are struggling to end conflict; still others are emerging from conflict and are beginning to show progress. Some countries are not faced with conflict, but are mired with poor governance, high levels of corruption, and governments with little interest in political or economic development. In these countries, bilateral aid will be heavily influenced by strategic and security considerations. For example, the United States has expressed strong concern about "failed states" as part of the war on terrorism and has allocated substantial sums to weak states that are its allies in the war.

Foreign aid to poorly governed countries should be tightly focused on humanitarian relief and providing basic services to the poor. Donors should focus on a very limited set of high priority activities with the potential for quick results that can be demonstrated to policymakers and the general public in order to help consolidate the process of further reform (World Bank, 2001). Donors should play a much stronger role in setting priorities and designing activities here than in countries with strong governance, where principles of country ownership can be put into practice. Program aid and budget support, by and large, is out of the question, and in some countries, no aid should be provided at all. In these instances where governments are very weak, significant amounts of aid should be directed at civil society groups and NGOs. The World Bank (2001) and Collier (2002) have suggested establishing Independent Service Providers (which Collier likens to an expenditure-side version of an Independent Revenue Board) to oversee the delivery of basic services. Working in these countries is much riskier than other places. As a result, programs in poorly governed states require very careful monitoring, regular re-appraisal, flexible responses as initiatives begin to work or fail, and a higher tolerance for failure than when working in other countries.

Within this set of countries, aid has the most potential to be effective in post-conflict situations. Collier and Hoeffler (2002) find that, under a poverty-efficient allocation of aid, about twice as much aid should be allocated to post-conflict countries as to similar non-conflict countries, since post-conflict countries are starting from a lower economic base, have the potential for rapid catch-up growth, and have a greater capacity to deploy aid quickly. Mozambique, for example, has received large amounts of aid in the decade since its civil war has ended, which (along with policy reforms and institutional changes) has led to very a high rate of economic growth. The World Bank (2003d) also argues for significant aid to post-conflict countries, not just because the economic rates of return are potentially higher, but as a way of reducing the risk of a country slipping back into conflict. It warns against the typical donor pattern of providing significant aid in the first year or two when the country is very visible on the international agenda, followed by a sharp decline in aid. It argues instead for a slower ramping up of aid as peace is solidified, augmented by other international measures of support, especially peacekeeping forces. Aid flows should build to a peak four to five years after the conflict and gradually diminish thereafter.

One of the most difficult questions for donors working in poorly governed countries is when to continue providing some aid and when to stop. Since aid tends to be least effective in these countries, continuing with disbursements may have a high opportunity costs because the same aid could be used more productively elsewhere. Moreover, aid flows, if not directed carefully, can help sustain bad governments. However, there may be significant costs from entirely disengaging, including a greater risk of further destabilization and violence, or a deterioration of health and education systems (OECD 2001). It is probably true, as the OECD argues, that it is important for the international community – not all donors, but perhaps some – to maintain dialogue even with the most difficult governments.

B. The International Trade System

How should the international trading and financial system contribute to poor countries achieving the MDGs? In broad terms this means the realization of an open, rules based predictable and non-discriminatory trading and financial system which takes into account the needs of poor countries. In the trading system this ranges from systemic changes to ensure the "development" component of the Doha Development Round, to specific initiatives such as provision of drugs for poor countries under the pharmaceutical agreement in TRIPS. It would also include addressing the special needs of the least developed countries including tariff and quota free access to exports.

Ever since the failure of the 1999 Seattle WTO meeting, there has been a great deal of concern regarding how the multilateral trading system should contribute to development and equity. The agreement to launch the Doha Development Round in November 2001 to address the development concerns of developing countries was a promising beginning, but since then missed deadlines and lack of agreement at the Cancun WTO Ministerial Meeting in September 2003, signaled that there are fundamental problems afoot. There is now great pessimism that the Round can be completed by the January 2005 deadline.

The crucial question is how can the trading system serve the needs of the poorest countries so that they can meet the MDGs? Whilst developing countries also have to play a role, the key to all successful outcomes of past multilateral rounds has been the political will of the developed countries to deliver on broken promises and play a leadership role in addressing the inequities of the international trading system. The key issues of the trade negotiations are as follows:

i. Special and Differential Treatment

A so-far elusive goal is that of a credible framework for special and differential (S&D) treatment, implementation of past commitments, and how to best integrate least developed countries into the trading system. The Doha Development Agenda (DDA) also promised to deliver on "capacity building". S&D is a key pillar to achieving "development" in the agenda, and a key debate has always been "special" for whom and how "different". It has been argued that the current S&D system which is not based on a clear definition of "who" gets the special treatment, requires non reciprocity and without clear graduation criteria, has not been effective.

The WTO does not have a definition for developing countries or for "graduation" from that status. It is based on self-declaration. The only definition comes with the least developed country definition and some policies or leeway being allowed for countries with per capita income of less than $1000. However within the general definition of developing countries you have the whole range of rapidly growing middle income countries and the poorest developing countries. This makes it harder to focus S&D for the needs of the poorest countries and confining it to the current definition of least developed countries also leads to the exclusion of a number of the poorest developing countries.

The current framework of S&D on the one hand leads to developed countries giving limited and minimum preferences in the case of market access for goods, often using complicated rules of origin to reduce market access. This has affected for instance duty free access to EU by African countries. The fear of being overridden by competition from the richer and rapidly growing economies and the lack of clarity as to how long the preferences should be given leads to that outcome. On the other hand, developing countries receiving the preferences have no incentive to "develop" or graduate, and there is no counterbalance between exporting and import competing interests as there is no commitment that they have to make to also begin to undertake reforms.

How could S&D be made more effective to deal with the poorest developing countries? One suggestion is for developed countries to liberalize all trade and allow access for developing countries by a set deadline, say 2015 and not deal with ineffective preferential access (Hoekman et al 2003). Another suggestion is to design S&D framework for the needs of the poorest countries. This will require establishing a clear and non-arbitrary criteria defining which countries will benefit from S&D (e.g. per capital GNI and absolute size measure). Messerlin (2003) has suggested cutoff point which is already being used in the WTO of $1000 per capita combined with absolute size of not larger than 2 percent of total GNI of all donors. Based on 2000 data, this would include 74 poorest countries including the 49 Least Developed Countries (mostly in Sub-Sahara Africa), plus some other countries in Central and South East Asia, the Caucuses, the Middle East and elsewhere. These countries share many serious development problems such as being land locked. Using this criteria also excludes the competitive and large countries such as India and China, so that developed countries would be more willing to give concession.

Commitments from the beneficiaries will also be important and should include some form of reciprocity since full reciprocity would probably be unviable for the poorest countries (many of whom still rely on tariff revenues for government revenues). The poorest countries also need to begin the process of trade reforms as a means for development and having such commitments, even if limited, can also provide the tool for governments to counter powerful domestic vested interests. For instance in the case of market access for goods, commitments could be in the form of binding to a maximum tariff, adopting a more uniform tariff structure, and commitment to ban non tariff barriers.

ii. Goods Market Access

Agricultural goods: a successful outcome in agriculture will be the benchmark for trade success because of its potentially great impact on poverty. Three major outcomes are important in this regard: elimination (not just reduction) of export subsidies; phase out of other government subsidies to farmers in developed countries on products which are important for developing country exports; and reduction of agriculture tariffs. The decision rests on the two major countries, the European Union and the U.S. Current progress remains unsatisfactory, with no real commitment to eliminate, only to reduce and ability to still have acceptable domestic support (de minimus provisions) and non trade distorting subsidies (with no clear indication how it will be capped).

Developing countries will also need some flexibility to address food security and rural development. This could include extra financial and technical assistance for structural adjustments in the rural sector for poor countries. But they should be able to justify what "special products" are, and what their national plans are to support the development of such products and eventually integrate them into the international trading system.

Non-agricultural goods: the issue here, among others, is how to reduce tariffs for manufactured products using a formula and over a specific period of time. For developing countries this has to do with the speed and depth of tariff reduction, the removal of tariff peaks and escalation in developed country markets. There is also the specter of non-tariff barriers rising, in the absence of any agreement to discipline its use such as with regard to anti dumping, as tariffs fall, which can negate improved market access. The recent case of US tariffs on steel and in particular zeroing in on a number of Chinese products such as textiles and electronics, are particularly worrying.

Contingent Protection has in fact been biased against small and poor countries, who have initiated 12 percent of antidumping cases but have been the main target (62 percent of cases). In order to address the needs of poor countries as they become more competitive, is to increase the threshold that poorest countries exporting a product before initiating anti dumping case, and threshold reduced as the poor country “graduates”.

iii. Trade in Services
Liberalization in trade in services can yield potential gains, but developing countries will face difficulties in achieving across the board liberalization, because of difficulties in creating the institutional and regulatory set up and addressing non economic objectives such as universal provision. Therefore, the multilateral trading system can set up the framework, but full liberalization can only be achieved in the longer term. Some have suggested 2015 for developed countries and longer for developing countries with "opt in" option for the poorest developing countries (S&D). This allows the poorest countries which have limited regulatory capacity to not participate in the liberalization commitments initially, but to join the agreement later without having to renegotiate. This means they can focus on the few services of interest and their resources and energy to domestic regulatory reforms. Within this framework, developing countries can prioritize opening mode 3 that is allowing foreign companies to establish themselves to provide services (mode 3), and fight for a major issue that can be beneficial for developing countries, the movement of workers to provide services (mode 4). The latter can be a major source of foreign exchange revenues as well as human capital building.

iv. Accession to the WTO by Poor Countries
The current group of 49 LDCs account for 0.5 percent of world trade and unprocessed primary products accounted for approximately 62 percent of their exports. No LDC has been admitted since the establishment of the WTO in 1995 and stringent requirements are imposed on their accession. Therefore, the issue that arises is what kind of degree of flexibility can be given to LDCs in undertaking their commitments and obligations to become WTO members?

v. Not Broadening the Agenda
Implementation of the Uruguay Round agreement has not even been completed by developing countries, and to add new issues being introduced will stretch the already thin capacity of most developing countries and it is also questionable that WTO as an institution can cope with the broader mandate. As for the "Singapore issues" -- negotiations on investment, competition policy, government procurement and trade facilitation -- most developing countries have not agreed to start negotiations because of capacity, and a lack of understanding of these complex issues.

C. Other International System Topics to be Addressed by TF1

In preparation for its final report, the Task Force aims to address the following crucial topics: (1) regional development strategies; (2) migration and remittances; and (3) global public goods.