Global Economic Situation
Climate Change: the Challenge for Finance Ministers
Financial Inclusion
Reforms in the Public and Financial Sectors
Millennium Development Goals
Managing Infrastructure Development
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Increasing tourism flows can bring many positive economic consequences to host countries, particularly in terms of income and employment opportunities, state revenues, diversification of economy and foreign exchange earnings.”
On behalf of all the people of Guyana – welcome to our country. We are delighted to host this year’s Commonwealth Finance Ministers’ Meeting and invite all our visitors from overseas to enjoy our country’s unique beauty and legendary hospitality.

This Finance Ministers’ Meeting takes place at a time of major change for the Commonwealth and for our planet.

International terrorism, threats to energy security and the global dangers from climate change present challenges which were barely known about just ten years ago.

Future generations will judge us by our response in the face of these challenges – did we allow them to overwhelm us, or did we apply our collective abilities to solve them and create a better world?

At moments of great change, the timeless principles which underpin our Commonwealth are needed more than ever. These principles – respect for democracy, the rule of law, good governance, human rights, gender equity and sustainable development – can provide the foundation from which we can devise modern solutions for modern problems.

Yet success is not pre-determined. No matter how solid the foundation, successfully addressing our generation’s challenges will require innovation, collective will and long-term perseverance. For just as the challenges we face are unlike those we faced in the past, our responses must be greater than those we have ever deployed before.

The fact that Finance Ministers are meeting to discuss climate change is proof of this profound change in the nature of our global development. In the past, the issue of climate change was the preserve of scientists and environmental campaigners. It was seen as a fringe issue with limited impact on the world at large, and certainly not something which would engage the sustained attention of Finance Ministers and Heads of Government.

This is no longer the case.

Climate change is the greatest long-term challenge faced by our world. On current trends, average global temperatures will rise by two to three degrees relative to pre-industrial levels within the next fifty years. One sixth of the world’s population will be threatened by melting glaciers; hundreds of millions will be at risk of starving; diseases such as malaria and dengue fever will spread to new parts of the world; hundreds of millions of people will become displaced; and eco-systems upon which so much of the world’s agriculture and medicine depend will be placed at major risk. The Amazon rainforest, the edge of which is just one hundred kilometres from our capital, presents a striking physical manifestation of what we stand to lose if we do not act.

It is clear that this is not simply an environmental issue but one of profound human consequence, the likes of which has never been seen in the history of the world.

Yet just as the potential devastation is profoundly human, so too is the potential solution. With the right leadership and global collective action, we can act to prevent the worst extremes of climate change. This means addressing the continued short-comings in the international framework for dealing with climate change – every day that we fail to do so increases the probability that the consequences of climate change will be of catastrophic proportions.

The Kyoto Protocol represented important progress in the fight against climate change, but as it stands, its measures are grossly inadequate. As Governments of 30 per cent of humanity, we must seek to influence the wider international community to build on Kyoto, and work at the UNFCCC’s upcoming Meeting in Bali and elsewhere to identify workable solutions to create larger markets and better regulation for carbon, support the development of clean technologies, encourage behavioural change by individuals and businesses across the world, help developing countries cope with the impact of climate change, and prevent deforestation of the world’s tropical forests.

As Finance Ministers sit in Georgetown with the vast Amazon less than two hour’s drive away, action to prevent deforestation takes on a special significance.
Tropical deforestation contributes 18 per cent of global greenhouse gas emissions — about the same as the United States, the equivalent of India and China combined, and greater than the cumulative total of emissions from aviation since aviation began until at least 2025. Almost all the world’s tropical forest lies within developing countries, and much within the Commonwealth.

I propose that one practical outcome from our Finance Ministers’ Meeting can be a declaration of intent that the Commonwealth will act to support international action to address the issue of tropical deforestation.

The science is clear — slowing down the rate of deforestation will immediately contribute to a slowdown in the growth of carbon emissions. The economics are equally sound — last year’s ground-breaking Stern Review described avoiding deforestation as a “highly cost-effective way of reducing greenhouse gas emissions”. McKinsey & Co identified avoiding deforestation as the largest and most cost-effective measure that could be taken to immediately combat climate change.

However, despite clear science and sound economics, nothing will happen unless these are joined by global political will to identify solutions that will protect and restore tropical forest. These solutions must avoid creating perverse incentives where countries which are already causing major deforestation are rewarded for slowing this down, but countries which are acting to protect standing forest receive no value. Aside from the injustice in implementing such solutions, they would simply not work as they would result in cross-border economic leakages amongst the countries of the Amazon and other rain-forest areas.

Instead, solutions must create incentives both for preservation and restoration. They need to be national and supra-national in scope — project-based solutions will not create the necessary impact. And above all, they need to take into account the needs of people, both those who live in the forest, and those of the country in which the forest is found. This last point is particularly important given that most of the countries where tropical rainforest is found are those with the most pressing social and economic development needs.

Guyana is prepared to lead, and to implement innovative policies to deploy our rainforest — which is larger than England — as a global asset in the fight against climate change. Our record in sustainable management of the rainforest is already well-established. Over many years, we have pursued pioneering environmental policies with Conservation International and other global organisations to protect the forest without sacrificing the developmental needs of our people. In 1989, the people of Guyana gave one million acres of forest at Iwokrama to the peoples of the Commonwealth and the world, and since then, Iwokrama has been a global beacon in efforts to sustainably manage the forest. But we are prepared to act on a far greater scale, and will welcome proposals to balance our national development with globally relevant action to combat climate change.

To conclude — combating climate change has rightly become one of the defining challenges of our age. As the largest gathering of Finance Ministers ever to substantively address this issue, I am confident that those assembled in Georgetown this week will elevate the quality of the climate change debate yet further. Most of all, I am hopeful that at the end of three days, we will see the start of a solution that will benefit not just the people of our Commonwealth, but the whole of human-kind.

Once more, welcome to Guyana — I wish you an enjoyable and successful stay.

Bharrat Jagdeo
President of the Republic of Guyana
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As the former UN Secretary-General Kofi Annan has said, “good governance is the single most important factor in eradicating poverty and promoting development.” It is now acknowledged that there are critical linkages between good governance and positive development outcomes, such as reduced poverty and peace and stability. The Commonwealth has itself long voiced this view. As early as 1971, Commonwealth Heads of Government in the Singapore Declaration agreed on Commonwealth principles which emphasised the important role of governance in the development process, and subsequently, in the landmark Harare Declaration (1991) as well as in the Aso Rock Declaration (2003), they reaffirmed their commitment to democracy, good governance, sustainable development, human rights and gender equality. It will also be recalled that Heads of Government in 2002, at the Coolum Summit, recognised the links between democracy and good governance on the one hand, and poverty, development and conflict on the other, and established a high-level Expert Group on Democracy and Development which produced a seminal and insightful report, *Making democracy work for pro-poor development* (2003).

**What is good governance?**

An important perspective on governance is that it encompasses both processes and institutions, and not only the state as a key actor, but the private sector and civil society as well. All the latter three play central roles in providing the conditions and structures necessary for improved governance. Among the key roles of the state is that of creating a stable political and legal environment conducive to sustained development. The private sector contributes through wealth and employment creation, while civil society institutions and organisations facilitate political and social interaction, including through mobilising groups and individuals to participate in economic, social and political activities.

This perspective points broadly to desired outcomes – but it is important to emphasise that good governance is as much about process as it is about outcomes: the two are inextricably linked.

**Governance and poverty reduction**

Does good governance contribute to poverty alleviation? The Commission for Africa asserted two years ago that governance and capacity building are at the core of all of Africa’s problems. This is an assessment that need not be confined in the developing world to Africa. Problems of poverty and governance are intertwined. It is clearly the case that when power is abused, or exercised in an improper manner, and if institutions are inefficient, those without access – the poor – are most likely to suffer. Ineffective or weak
governance compromises the delivery of services and benefits to those who need them most; the influence of organised and well-heeled interest groups biases policies, programmes and spending away from the poor. Not surprisingly, analysts have pointed to the vicious circle in which the poor are caught up. By definition lacking significant assets, the lack of property rights, poor security, and inadequate legal services that often attend weak governance further disadvantage the poor and inhibit them from securing their homes and other assets and from operating businesses. Thus poor governance both generates and reinforces poverty, and subverts efforts to reduce it; the corollary of course is that sustainable poverty reduction strategies require good governance.

It is both intuitively plausible and demonstrated empirically that the provision of external resources is affected by the quality of governance, although it will be readily recognised that in a complex world the reasons for resource flows, public and private, can vary. Regression analyses more than a decade old indicate that corruption is negatively linked to levels of investment as well as to economic growth, the latter being retarded by factors such as excessive rent seeking, loss of tax revenue, unproductive and wasteful expenditure and poor quality infrastructure and services. The Commonwealth’s own engagement in anti-corruption programmes in its member states is predicated on the premise that corruption is deleterious to development, hurts the poor disproportionately by diverting funds intended for development, undermines the ability of governments to provide basic services, and helps to perpetuate inequality and injustice. The Secretariat’s programmes aim ultimately to ensure that governance institutions serve citizens transparently, efficiently and in a cost-effective manner.

In regard to aid flows, arguably no aspect of development cooperation has been the subject of more concerted attention in recent years than the relationship between governance and aid effectiveness. Many countries in Africa will have to double their per capita income over the next decade if they are to meet the goal of halving poverty by 2015. The attainment of this, and other Millennium Development Goals (MDGs) demand a number of measures, including a significant scaling up of aid – even beyond the levels committed to at the Gleneagles Summit – as well as increased private investment, both domestic and external, and the implementation of the policy reforms that are at the heart of improved governance. The United States Millennium Challenge Account, the United Kingdom’s Governance and Transparency Fund, the EU/AU Strategy for Africa, and the African Union-NEPAD Peer Review Mechanism are some of the initiatives which reflect this new and concerted focus on governance and development.

A pillar of the emerging policy framework at the international level is of course the 2005 Paris Declaration on Aid Effectiveness – to be reviewed in 2008 – which introduces principles essential to genuine partnership between donors and recipients, such as country ownership, mutual accountability, and harmonisation and alignment of aid efforts among them. The changing relationship between donor and recipient, as reflected in the Paris principles, is as of now a work in progress, but one that augurs well for both governance and development. And given the undeniable linkage between the two, in the medium to long term this must necessarily augur well also for poverty alleviation.

The task before the international community, and no less the developing countries themselves, is a very challenging one. According to the World Bank’s Worldwide Governance Indicators (WGI) Project, which tracks governance indicators for 212 countries and territories for six dimensions of governance, 38 of 46 countries in Africa are both poorer than the global average and score lower than the global average on the basis of the project’s governance indicators. Those indicators are: voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of corruption. Whether there will be broad-based success in achieving the MDGs or not – and this is the leading development challenge of our times – will be decided in Africa. For this reason the relationship between governance and development is of immense relevance, particularly to that continent.

What is the Commonwealth doing?

The considerable variation in the kind and quality of the governance arrangements across countries means that there is no one-size-fits-all approach to the processes and institutions that will be plausible and beneficial to countries under all circumstances. At the Commonwealth, we consider a strong and vibrant democracy to be crucial for development, and we hold democracy and development to be mutually reinforcing. For the Commonwealth therefore, good governance is to be identified with democratic forms, with the rule of law, and with institutions anchored in public participation, accountability and transparency. On this basis also, integral to good governance are processes, relationships,
and institutions which make it possible for citizens and groups “to articulate their interests, exercise their rights and obligations, and mediate their differences”. The Commonwealth Expert Group on Democracy and Development, referred to earlier, emphasised that the scope of democracy must be widened beyond elections, so that democratic institutions and processes facilitate, protect and reinforce the full range of human rights – which include political and civil rights, social and economic rights, gender rights, and group rights.

The Commonwealth is thus committed to and actively promotes “democratic processes and institutions which reflect national circumstances, the rule of law, the independence of the judiciary, (and) just and honest government.” (1991 Harare Declaration). Among Commonwealth programmes aimed at promoting good governance are Good Offices for Peace, Democracy and Consensus Building, Rule of Law, Human Rights, Public Sector Development, and Capacity Building and Institutional Development.

It should be emphasised that, while falling outside strict definitions of development modalities, conflict resolution and consensus-building mechanisms are essential to peace and stability, to good governance, and to development. As with the relationship between governance and poverty, governance, peace and stability are interrelated issues, constituting a virtuous circle in which each element reinforces the others. Peace and stability are dependent on good governance: poor governance breeds disillusionment, grievances and conflict.

The Commonwealth has long provided advice and technical assistance on governance and related matters to its developing member states through programmes and activities such as those cited earlier. Election observation, for example, is one of the many ways in which the Commonwealth encourages adherence to democratic process. The Commonwealth has observed more than forty-five elections in more than thirty countries and has assisted governments in implementing the recommendations of observer groups in regard to elections and the electoral process. In recent years, the Commonwealth has observed elections in a number of countries including Guyana, Lesotho, Nigeria, Solomon Islands, Uganda and most recently Sierra Leone.

Over the years, the Commonwealth has been active also in assisting member states in strengthening institutions that uphold democratic principles and processes, such as the judiciary, the parliament, the civil service, election management bodies, offices of the ombudsman, regulatory bodies, as well as strengthening the other social partners, the private sector – including through the promotion of public/private partnerships – and civil society. Another practical example of this is initiatives in legislative drafting, training of the judiciary and court management, undertaken in Africa, the Pacific and in the Caribbean. Such initiatives are designed to ensure that citizens rights are enshrined in legislation and can be fully protected.

Election observation is one of the many ways in which the Commonwealth encourages adherence to democratic process.

The Good Offices role – political intervention of the Commonwealth Secretary-General or a personal envoy at the highest political level – has helped resolve or prevent conflicts in a number of countries. While it is recognised that there is much more work to be done, we consider that on balance these efforts at strengthening governance are yielding significant improvements, although, across countries, the progress is uneven. Furthermore, in some noteworthy cases, this is beginning to pay dividends in the area of economic growth and development. Of the 18 Commonwealth members in Africa, 13 achieved growth rates in 2006 of five per cent or more. Nine of these countries were in sub Saharan Africa. While one must note that these growth rates lag the average performance of developing countries, and the specific circumstance of a commodity boom must be taken into account, it is evident that the quality of political and economic governance has been improving in some countries and that growth rates have trended upwards – though not yet by enough to ensure that the MDGs are met, or to reduce the absolute number of those living in poverty. A major developmental challenge remains, but how this challenge can be met is increasingly clear.

Another dimension of governance: the private sector

It is necessary to highlight the key role that successful partnership with the private sector can play in taking both the good governance and development agendas forward. The private sector is quite appropriately a key driver of sustainable growth in many Commonwealth developing countries, especially through the activities of small and medium-sized enterprises (SMEs). The development of SMEs is also a key prerequisite for the emergence of a middle stratum which is important for
entrepreneurship, human capital formation, domestic market expansion and thus to long-term social and political stability. There is clear convergence of interest between the public and private sectors in promoting good governance, given the evident nexus between governance and development and the deleterious impact on development of waste, inefficiency, corruption and general ineffectiveness. It must be said, however, that while governments interested in promoting development are duty bound to provide a conducive and facilitatory legal and regulatory environment for businesses and entrepreneurs, domestic and foreign, the private sector, even if only incipient, must be expected to adhere to acceptable standards of probity and to itself exercise social responsibility.

It is evident that the quality of political and economic governance has been improving in some countries and that growth rates have trended upwards.

The Commonwealth Secretariat, consistent with the view that the imperative of good governance extends beyond the public sector has, through advisory services and training, sought to strengthen best practices within public and private entities, including SMEs and cooperatives. Given the composition of the Commonwealth, of particular relevance in this regard is the fact that high standards of corporate governance by a few role model enterprises in small states can have rapid demonstration effect in these markets, boosting confidence for local and foreign investors alike. Needless to say – and regrettably – the reverse is also true.

The Commonwealth contributes to promoting good governance – and by extension to poverty reduction and the promotion of peace and stability – through various channels.

Firstly, through policy advice and technical assistance delivered primarily under its public sector development and capacity building programmes, the Commonwealth has assisted its member countries by enhancing their capacity to design and implement sound economic and social policies, build and maintain effective public sector institutions (including legal and regulatory machinery), and improve accountability. Secondly, through its good offices, rule of law and democracy programmes, the Commonwealth has assisted member states in strengthening democratic institutions and culture, especially through mediation and conflict resolution, assistance to election management bodies, and the promotion and protection of civil, political and human rights.

The primacy of good governance for sustainable poverty reduction and for peace and stability is unassailable. Putting in place and consolidating the institutions, structures and processes that make for good governance demands constant and concerted commitment from governments and indeed from all social partners. The assistance of development partners is particularly crucial. The Commonwealth will continue to provide and increase its assistance in this area to member states, and in particular to the least developed among them. By so doing it will fulfil its commitment to democracy and development. The 2002 Commonwealth Expert Group on Democracy and Development was prescient when it stated “Given the conflicts and tensions in the world today, and the seriousness of many of the divides between countries, religions and ethnic groups, reducing poverty and improving governance are more important than ever. They are directly needed for peace and stability and are essential steps for the world to move towards greater international equality and justice.”

Mr Ransford Smith was appointed Deputy Secretary-General (Economic) of the Commonwealth in August 2006. A career diplomat of nearly 30 years standing in the Jamaican Public and Foreign Service, Mr Smith previously served as Permanent Secretary to the Ministry of Commerce and Technology, and also Permanent Secretary to the Ministry of Industry and Investment. Mr Smith was formerly the Permanent Representative of Jamaica to the Office of the United Nations and its specialised agencies in Geneva, Rome and Vienna. Mr Smith was also Ambassador of Jamaica to the World Trade Organisation (WTO), and served as non-resident Ambassador to a number of European countries.

The Commonwealth is an association of 53 independent states consulting and cooperating in the common interests of their peoples and in the promotion of international understanding and world peace. The Commonwealth Secretariat, established in 1965, is its main intergovernmental agency, facilitating consultation and co-operation among member governments and countries.

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Prospects for WTO and EPA negotiations

The World Trade Organization (WTO)'s Doha Development Round of multilateral trade negotiations, which was to be concluded by the end of 2004, is still ongoing. The three key issues of market access, domestic support, and export subsidies in the area of agriculture, as well as those critical areas of concern relating to market access for non-agricultural goods, have been frustrating the timely completion of the round. These issues remain intractable because they involve fundamental national interests. The Uruguay Round negotiations took eight years to complete. It was always optimistic to assume that 20 years later, when there are more countries involved and more issues on the table, a new 21st century round could be negotiated in less than eight years.

After another failure of the G4 (US, EU, Brazil and India) to make any real progress in resolving knotty WTO issues during their meeting in Potsdam in June, and the muted but somewhat cautious reactions to the draft texts released by the Agriculture and Non-Agriculture Market Access (NAMA) Chairs on July 17th, the prospects are not good for concluding the WTO’s Doha Development Round during 2007. Meanwhile, the negotiations between the European Union and six African, Caribbean and Pacific (ACP) regional groupings for economic partnership agreements (EPAs), are struggling erratically towards their agreed deadline of 31st December, 2007.

The WTO’s Doha Development Round
Concessions in agriculture necessary

In the negotiations, the real concern on the part of many countries, developed and developing alike, is that unless the US and the EU are prepared to make significant concessions in agriculture, the successful completion of the Doha Development Round will remain an elusive dream.

Agriculture is a major contributor to national incomes for many developing countries. However, in developed countries, the implementation of market-distorting measures enables resources to be diverted away from other sectors into agricultural production, thus increasing the world supply of commodities and depressing world prices. The use of trade-distorting subsidies by the major developed countries adversely affects developing nations, particularly those that depend on one or two commodities, by limiting the prices received for their agricultural products. Cotton, produced in the United States under highly subsidised rates and exported at relatively low prices, is a case in point. The cotton-producing countries in Africa have been suffering severely as a result of this situation. It should not be allowed to continue.

Domestic support, export subsidies, and restrictions on market access are inimical to free or fair trade. Their use by both developed and large developing countries significantly distorts world agricultural trade. This is the major reason for the stalemate in the current multilateral trade negotiations in Geneva.

Non-agricultural market access and services

In the areas of non-agricultural market access and services we are witnessing the same tactical approach by developed countries. They are insisting that developing countries, with the exception of the LDCs, make drastic and time-bound reductions in their customs tariffs in order to facilitate greater access to their markets for the exports of developed countries.

With respect to services, some developed countries are demanding that all countries make substantial and wide-ranging market access offers. These more advanced countries seem determined to capitalise on their
advantages regardless of the consequences for countries which are less advanced. In taking this hard line approach, developed countries are showing little or no regard for the provisions of the General Agreement on Trade in Services (GATS), which speak to special and differential treatment for developing countries. The inability of the G4 to reach agreement in this area reflects the differing perspectives of the developed and developing countries. While the US and EU saw a need for modalities in NAMA to create new market access opportunities, Brazil and India were of the view that any successful result would depend on substantial reduction in domestic support and market access for products of export interest to developing countries.

Agriculture and NAMA Chairs issue draft texts

In mid-July 2007, the Agriculture and NAMA Chairs issued their draft modalities texts on Agriculture and Non-Agriculture Market Access. Although WTO Director General Pascal Lamy opined that the texts constitute a fair and reasonable basis for reaching ambitious, balanced and development-oriented agreements, reactions from WTO members have been less positive.

Some developing countries have been particularly critical of the NAMA text, commenting on its severe imbalance. The African Group and the ACP were particularly disappointed, and have signalled that this text cannot form the basis for discussion on modalities. Small Vulnerable Economies (SVEs) have also expressed their disappointment with the extremely large tariff cuts that were proposed for them by the NAMA Chair. In the case of Barbados, for example, the numbers proposed would result in a 70 per cent reduction in bound tariffs on non-agricultural products.

These more advanced countries seem determined to capitalise on their advantages regardless of the consequences for countries which are less advanced.

Although the Agriculture draft modalities text was perceived as having taken into account some of the concerns of developing countries, including the need for enhanced flexibilities for SVEs, some groups of developing countries expressed the view that the agriculture text should be seen as a ‘working document’ rather than the basis for discussions on modalities. These countries pointed to the absence of elaboration on some key issues of concern to developing countries. The idea that all special products will be subject to some reduction is one of those interpretations which is opposed by a number of developing country groupings. In addition, the Agriculture text did not truly address tariff escalation or the special safeguard mechanism.

Special and differential treatment for developing countries

Both the Doha Ministerial Declaration and the WTO General Council's Decision speak to the issue of special and differential treatment for developing countries. The latter specifically addresses rural development, food security and/or livelihood needs of developing countries. Essentially, these countries are not required to make the same level of commitments as their developed counterparts in respect of market access, domestic support, and export subsidies. In addition, developing countries will have the flexibility to designate, ‘for more flexible treatment’, an appropriate number of products as ‘special products’, based on criteria of food security, livelihood needs, and rural development. A Special Safeguard Mechanism (SSM) is also to be established for use by developing countries.

A number of developed countries have repeatedly questioned the granting of special and differential treatment.

Despite such explicit provisions, a number of developed countries have repeatedly questioned the granting of special and differential treatment and have sought to delay or even abandon tangible delivery of the concessions to developing countries. It is clear that if certain WTO members continue to deny developing countries the special and differential treatment to which they have a realistic expectation, there is little or no chance of a successful outcome to the Doha Development Round.

However, the WTO negotiations experienced at least one positive development in July when the Committee on Subsidies and Countervailing Measures adopted a recommendation to extend the transition period for the elimination of export subsidy programmes of 19 developing countries for an additional eight years ending in 2015. This success was due in large measure to the unstinting efforts of developing countries who took the lead in this area. There are a number of conditions attached to the extension, but this decision allows the beneficiary countries to continue to promote various export subsidies in order to attract investment, create employment and expand export capacity.

Economic partnership agreements

There is one other set of major international trade negotiations involving most of the member countries of the Commonwealth. The European Union (EU) and the countries of the African, Caribbean, and Pacific (ACP) Group are negotiating regional Economic Partnership Agreements.

The ACP-EU Partnership, established by the Cotonou Agreement, is centered on the objective of promoting...
the sustainable development of ACP countries and eradicating poverty; and the EPAs are intended to foster the realisation of this objective. It was agreed that the negotiations should adopt an asymmetrical approach.

The EPAs are scheduled to enter into force from January 1, 2008, but progress in the negotiations has been very uneven across the ACP, with some regions reporting solid if unspectacular progress, whereas others have been experiencing major difficulties.

It is important, therefore, to consider the major issues which have not yet been resolved. Before proceeding to do so, however, we should note that there have been some areas of agreement, notably with respect to the scope and structure of the agreements, the need for asymmetry, length of transition periods, treatment of sanitary and phyto-sanitary measures (SPS) as well as technical barriers to trade issues, and the establishment of EPA Councils to oversee implementation of the agreements. Some of the major areas of divergence include:

**Differences on scope of regional integration processes**
The level of ambition with respect to the pace and scope of regional integration in the ACP is an area of long-standing divergence between the EC and the ACP in all of the regional EPA negotiations. Although both sides concur that one of the key objectives of an EPA is to strengthen the regional integration processes in the ACP, there continue to be significant differences as to how and at what speed this should be undertaken.

For the Caribbean, rum, sugar, rice and bananas constitute one of the unresolved aspects of the negotiations.

Throughout the negotiations ACP representatives have been obliged to battle against the Commission’s persistent attempts to push regions to accept common commitments. For example, there is the question as to whether all countries in the Caribbean should proceed from one common starting point, irrespective of their actual level of involvement in the regional integration exercise or their existing obligations under other agreements.

**The sequencing of trade related assistance and market access commitments**
The level of technical and financial assistance that would be made available to ACP countries to permit them to develop a real and sustained capacity to benefit from the EPA is another area of concern. We are dealing with two unequal partners, with vastly different resource endowments and size of economies. In such circumstances, fairness and equity can only be achieved if positive steps are taken to help redress the existing imbalance.

The logical sequencing of the EPA implementation underlines the need for supply-side constraints and trade capacity shortcomings to be addressed before the ACP regions undertake any further trade liberalisation. Caribbean countries have decided to pursue an EPA negotiating strategy of balancing regional trade objectives with EU development co-operation commitments, combining liberalisation with support measures in areas such as trade capacity building, regulatory reform, fiscal adjustment and competitiveness improvement.

**Market access and rate of tariff liberalisation**
The market access issues are some of the most difficult in the EPA negotiations. All regions are struggling to make meaningful progress. The CARIFORUM-EC
A definite role for the Commonwealth

There continues to be a definite role that the Commonwealth can play in both the EPA and WTO negotiations. Technically, the Commonwealth Secretariat should continue to provide serious and objective analyses of a number of the issues confronting its members, particularly the small developing countries. It also should convene timely meetings of its members to discuss and arrive at positions on the outstanding thorny issues in the negotiations. Politically, the Secretary General ought to continue to speak out, on behalf of the Commonwealth, on those aspects of the negotiations that directly touch and concern us greatly. Despite differences in size and levels of economic development, there exists a common bond among Commonwealth states that compels us to promote and defend each other’s interests.

negotiations may be used as an example where some progress has been made; but significant differences remain on critical issues.

As the negotiations have progressed, there is a convergence of views on a lengthy transition period for some products; development cooperation support to strengthen the region’s capacity to satisfy the EU’s SPS and TBT requirements; and on an overall asymmetrical approach to the negotiations.

Nevertheless, there continues to be considerable difficulty in reaching an agreement with the EC in terms of an approach to take into consideration CARIFORUM’s multi-faceted economic space. Therefore, the construction of tariff schedules and compilation of exclusions lists remain a major challenge.

The construction of tariff schedules and compilation of exclusions lists remain a major challenge.

Implications of not completing the negotiations before the end of 2007

In the event that the EPA negotiations cannot be concluded within the prescribed timeframe, and in the absence of any new trading arrangement, a legal void would be created on 1st January, 2008. The GATT Article 1 waiver covering the Cotonou trading arrangements would have expired. This situation would be prejudicial to the interests of ACP exporters and investors who would find themselves operating in an uncertain environment. ACP preferential access arrangements would be unprotected in the WTO, and thus subject to challenge.

If another waiver were requested, it is not clear what conditionalities would be attached and what impact they might have on ACP countries. Furthermore, Commission officials have stated repeatedly that there is no EU interest in seeking an extension of the current waiver. Other options, such as GSP Plus, also come into consideration, but they would not provide an equivalent market access. Key commodity exports to Europe, including sugar, rum, bananas, rice and beef, could suffer even greater damage than has already been the case.

Conclusion

Although there are difficulties in some key areas, most notably with respect to the pace and scope of the regional integration processes, the realisation of the development dimension of the EPAs, and the structuring of market access for goods, both the ACP and the EU are making an effort to complete the negotiations on time. In the case of the ACP, the clear assumption underlining this approach is that their interests will be satisfactorily addressed in the negotiations during the coming months. Failure to make meaningful progress in the areas mentioned above would raise serious doubts about the likelihood of EPAs coming into effect on 1st January 2008.

In their 33 years of development cooperation since the first Lomé Convention, the ACP states and the EU have always been able to find common ground on difficult issues. This history of success suggests cautious optimism that a mutually agreeable solution will be found to what now seems to be an impossible challenge.

The same level of optimism cannot be felt for the successful conclusion of the Doha Development Round by the end of 2007.

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Reform of the international aid architecture

The international aid architecture may be defined as the world’s agencies, institutions and systems for managing the transfer of resources (finance and expertise) to, and development of relationships with, low-income countries. In recent years, the aid industry has been experiencing significant change. Aid volume has increased from about $60 billion a year in the 1990s to $106.5 billion in 2005. Though it declined to $103.9 bn in 2006, it is projected to increase to $130 billion by 2010 if the Gleneagles commitments are fulfilled. At the same time, the aid architecture is being characterised by a proliferation of agencies and special purpose vehicles. UNDP has estimated that there are now over 1,000 financing mechanisms. The author outlines the issues and principles for reform of the international aid architecture.

The key features of the aid system include a large number of agencies; a high proportion of bilateral aid (70 per cent), much of it tied, particularly technical assistance; and an expanding role for non-governmental organisations (NGOs). The official agencies comprise over 40 bilateral, 20 global and regional financing institutions, 15 UN agencies and a growing number of vertical global funds.

In the decade since 1993, donors members of the Development Assistance Committee (DAC) have accounted for around 95 per cent of all international aid. A recent trend has been the emergence of non-DAC, particularly Asian, donors. China has committed to provide US$10 billion in concessional loans and preferential export buyers’ credits within the next three years. India is increasing its provision to Africa to roughly ten times the level in 2004/05. In addition, Korea is aiming to reach US$1 billion Official Development Assistance (ODA) by 2010.

Structure of the aid system

Bilateral aid. This continues to constitute over 70 per cent of ODA. However, it is not well coordinated, involves high transaction costs; has no binding rules or norms, and delivers a large volume of tied and ineffective technical assistance.

The UN development system. This system has legitimacy. However, it lacks core funds, priorities have been driven by donors and it has struggled to organise effectively and to prioritise at country level. There are too many agencies operating with insufficient coherence and the UN still has to win the trust of big donors. A UN High Level Panel (HLP) reported in November 2006 with proposals to reform the organisation’s development system. The essence of the HLP’s vision is for the UN ‘to deliver as one’ in the areas of development, humanitarian assistance and the environment. The UN’s normative and analytic expertise, its operational and coordination capabilities and advocacy role must be brought together more effectively at the country, regional and global levels.

Bilateral aid is not well coordinated, involves high transaction costs; has no binding rules or norms, and delivers a large volume of tied and ineffective technical assistance.

Key recommendations for reform include:

• One UN for development at country level
• One UN for development at Headquarters
• Strengthen results-based funding, performance and accountability
• Enhance the UN’s role in humanitarian assistance
• Strengthen multilateral action to promote environmental sustainability
• Improve the UN’s delivery of gender equality and women’s empowerment
• Streamline co-ordination with other multilateral agencies, particularly the Bretton Woods Institutions (BWIs).
**World Bank.** The World Bank’s concessional arm, International Development Assistance (IDA), continues to dominate policy processes related to structural reforms. It has found it difficult to embrace ‘alignment’ and let go of non-selective conditionality. There are also issues related to flexibility and predictability. Much of the intellectual input into the discourse on development and the formulation of policies/conditionality come from the international financial institutions (IFIs). In fact, the IFIs act as gatekeepers for the bilaterals. **The Regional Development Banks (RDBs).** These experience concerns about effectiveness. Though they have greater legitimacy than the BWIs, the developing country voice is diluted through donor-driven replenishment processes. **The European Commission.** This institution has experienced criticism from both recipient countries and some member states, such as the UK, regarding effectiveness; problems of favouring middle-income countries; and its highly bureaucratic and time-consuming procedures which constrain disbursements.

**Systemic issues**

Overall allocation of aid is problematic. ‘Favourite country syndrome’ tends to over-aid some countries while under-aiding others. There are very different systems for countries on either side of the IDA definition of low income. There is no systematic framework that spans the low-income and lower middle-income countries.

Aid flows to individual countries are very volatile and unpredictable, particularly multilateral assistance. They also tend to be pro-cyclical thereby exacerbating the effects of shocks.

The Paris Declaration has set out specific targets for 2010 for 12 indicators related to ownership, harmonisation, alignment, managing for results and mutual accountability.

The aid system lacks flexibility. It is slow to pick up on new ideas. Strategies for dealing with single purpose funds and private philanthropy are unclear.

Low-income countries have very little voice within the system. They have no formal influence over bilateral policies and no effective voice over system-wide issues.

Humanitarian aid accounts for a growing share of ODA. There are even fewer agreed rules or norms and no Millennium Development Goal (MDG) to provide a unifying objective. Patterns of finance do not respond to need and the required co-ordination functions are seriously under-funded.

**Developing country priorities**

Any reform of aid architecture must take into account the concerns of developing countries. The draft final outcomes paper of the Monterrey Conference on Financing for Development contained some G77 proposals excluded from the final outcomes paper. Developing country priorities at Monterrey were:

- Enhanced voice in the international architecture and specifically in the BWIs and the new institutions for global financial stability
- Increase overall aid volume
- Policy coherence and trade policy of developed countries
- Official flows playing a clear counter-cyclical role
- Issues of harmonisation, reduced transaction costs and streamlined conditionality, and
- Lack of control over policy framework.

Partner countries tend to take the view that low disbursement ratios and aid cancellations were due, at least in part, to the fact that original project designs were donor driven and lacked realism.

**Paris Declaration on Aid Effectiveness**

There is no recognisable ‘architect’ for the aid system as a whole. So far, the main response has been to try and operationalise the concepts of ownership, harmonisation and alignment. This is reflected in the Paris Declaration on Aid Effectiveness (2005) which has been signed by 35 donor countries, 26 multilateral donors, 56 recipients and 14 civil society representatives. The Paris Declaration has set out specific targets for 2010 for 12 indicators related to ownership, harmonisation, alignment, managing for results and mutual accountability.

The implementation of the Paris Declaration will be challenging. The first DAC survey of its implementation was recently published and confirms that the cost of managing aid continues to be high for aid recipients. While the survey is a useful baseline tool, it also highlights a number of gaps in information, understanding and implementation.

For instance, in its assessment of alignment, the survey does not examine the causes of low disbursement ratios in many countries. There are frequent aid cancellations and a large part of committed aid remains unutilised. Donors tend to attribute this to weak governance. Partner countries tend to take the view that low disbursement ratios and aid cancellations were due, at least in part, to the fact that original project designs were donor driven and lacked realism and were inadequately informed by local knowledge of what works and what does not. Future surveys should seek to gain greater understanding of this dimension of alignment.

In addressing mutual accountability, it is also important to take account of the fact that in some instances, donors bypass the government entirely and prefer the NGO route of delivery. This is particularly so in fragile states.
which are largely not included in the 2005 Survey. The modalities for addressing the whole issue of NGO accountability in such instances need to be included in the guidelines for future surveys.

Almost all monitoring and evaluation of donor assistance continues to be by donors themselves despite the commitments to mutual accountability in the Paris Declaration.

Donors need to recognise the governance challenges many aid recipients face. In practice, governance constraints become at least as important for donors as meeting the resource needs of development programmes. It has been suggested that donors often do not recognise the inherently political role that they play in recipient countries and risk undermining the role of domestic politics. There is also need to manage expectations in donor countries about what aid can realistically achieve. Public opinion should be better informed about the difficulties and tensions inherent in aid giving, in order to ensure long-term public support for aid, even in the face of short-term challenges.

While the Paris Declaration has the potential to empower partner countries in their dealings with donors, even if it is implemented, it will not address the issue of how the overall structure of the aid system might be rationalised. Some aspects of the reform of the aid architecture are already on the agenda: governance reform of the BWIs to give developing countries greater voice; and the Report of the UN High Level Panel on System-Wide Coherence. However, there has not been a systematic and holistic approach to reform of the architecture of the aid industry. Recipient countries, in particular, have lacked the opportunity to express their views.

The aid system is too complicated as the international aid architecture has not developed in a planned way and has no central architect. There is little co-ordination of inputs and processes between the large donor agencies and no single approach to the objectives and outputs of aid programmes.

The principles for an effective aid system

The overall objective is to establish a system that will deliver the finances, policies and expertise to support sustainable growth, poverty reduction and help countries attain the MDGs. A UK Department for International Development (DfID) discussion paper (June 2003), Vision and Options for Change for the International Development Architecture, identified seven principles which should underpin such a system:

1) Improved accountability through effective voice and relevance for poor countries

A key issue is the balance between bilateral and multilateral aid. The case for multilateral aid is strong. There is also the issue of how one allocates additional resources across different multilaterals: IFIs tend to be more effective but lack legitimacy – the UN and European Union (EU) have greater legitimacy but have been less effective. There is a strong case for increasing multilateral aid, provided there is effective reform of these institutions.

2) Better balancing of co-ordination and competition

The current aid system is too muddled, with too many agencies offering the same products and services; often of varying and uncertain accessibility. However, concentrating the international aid system under the control of one or two board structures (and by extension, dominant board members) is risky. Hence it is necessary to balance the requirements for better co-ordination with the needs for competition and room to manoeuvre for beneficiaries. Many poor countries, faced with unpredictable aid flows, have expressed a preference for a portfolio of suppliers.

3) Medium-term predictability at country level

Volatility and unpredictability of aid flows at the country level is a major problem. Multilateral aid (both receipts and commitments) is considerably more volatile than bilateral aid. Volatility has been greater at the country rather than global level. This is probably explained by country level conditionalities, with aid being turned on and off. The case for greater predictability is extremely robust. This would enable countries to plan over a 5–10-year time horizon at least. It can be argued that an important determinant of the success of the East and South-east Asian countries was their capacity to take a strategic perspective over 10-15 years.

4) Flexibility, including the capacity to smooth shocks

An effective aid system needs the flexibility to respond to different country contexts and different emerging issues. The ownership/alignment agenda is not always working out on the ground: the aid system also needs to move fast enough to smooth the impact of shocks to ensure that the burden does not fall too much on domestic adjustment, which affects the poor and vulnerable disproportionately. The current phase of buoyant commodity prices has meant that the inadequacy of systemic capacity to provide countercyclical liquidity in the face of exogenous shocks has not been exposed.
5) Balancing need and performance to attain MDGs
Aid allocation is being increasingly driven by performance. IDA, the African and Asian Development Fund and the European Development Fund all use similar systems. It is important that aid allocation models give greater weight to poverty. There has been a call for a model with one-to-one weight for poverty and policy performance, compared with about 1 to 16 in the IDA model. Aid allocation models must also respond to country priorities rather than being based on a ‘one-size-fits-all’ view of a good policy environment. This is best done through a bottom-up process of aid allocation which factors in the MDGs.

It is important to have a common methodology for assessing need which permits a consistent approach across the whole spectrum of humanitarian aid, development aid for poor performers/failing states and financing for good performers.

6) Addressing market failures, strengthening institutions and promoting harmonisation and alignment
Many parts of the aid system continue to deliver supply-driven instruments and approaches. Insufficient emphasis is placed on understanding and addressing government and market failures in recipient countries. It is important that there is a strong focus on supporting the changing role of the state through institution building. This would increase the returns on aid programmes across the board.

The case for greater predictability is extremely robust. This would enable countries to plan over a 5-10-year time horizon at least.

Donors’ individual accountability and fiduciary systems and their continued insistence on having their own policy processes, rather than subordinating them to recipient country-driven political policy processes, impose heavy burdens and undermine ownership by limiting policy space. Despite improvements in government financial management and accounting systems and commitments made in the Paris Declaration, these are still being used too little by donors, reflecting agency rules or operational habits that should be changed.

7) Mainstreaming political analysis and engagement
Donor behaviour can weaken political legitimacy. The development system tends to be weak in understanding its political role and in analysing the potential threats and opportunities associated with political processes in recipient countries. Greater capacity on the part of donors to analyse political processes is essential to inform sound strategies for policy development.

The Commonwealth’s role
The Commonwealth Secretariat has been playing an important role in focusing on the issue of a holistic reform of the aid architecture. Jointly with the Organisation Internationale de la Francophonie, it has carried out a project which has been financed by DFID and facilitated by the Overseas Development Institute (ODI). The principal objective of this project has been to bring southern voices to bear on the debate.

Following three workshops in London, Dhaka and Yaoundé, a report was submitted to the Commonwealth Finance Ministers Meeting in Colombo (September, 2006) who deliberated upon the role of the association in the reform of the international aid architecture. In their Communiqué, Ministers requested the Secretariat “to establish a working group of senior officials to consider how best the Commonwealth can influence the continuing debate”. The Working Group met in Washington DC at the time of the IMF/World Bank Spring Meetings. The purpose of the meeting was to recommend specific ways in which Commonwealth countries can individually and collectively influence the international discussion on this subject. The Working Group agreed upon a number of priority actions for the Commonwealth as an advocate, service provider and network, which will be considered by the Commonwealth Finance Ministers Meeting in Georgetown in October, 2007.

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Africa’s economic opportunities

How can African governments accelerate economic growth? There are specific strategies that can be tailored to a country’s geographic characteristics, as proposed in the author’s book The Bottom Billion. Africa’s growth has recently accelerated. However, this is partly due to high prices for commodity exports. It is not possible yet to tell whether change will endure. The past has been dismal. On average over the period from 1960 to 2000 Africa’s growth was a mere 0.1 per cent per capita when population-weighted. Africa diverged from other developing regions: between 1980 and 2000 the annual rate of divergence was an astounding five per cent.

Growth opportunities are determined by geography. Because Africa is land-abundant yet low-income, natural resource endowments matter. However, these resources are unevenly distributed. Considerable parts of Africa are abundant in natural resources, but other parts are resource-scarce. The other feature of geography follows from the fact that Africa is enormous and divided into many countries: many of them are landlocked.

These distinctions create four categories: resource-rich and landlocked; resource-rich and coastal; resource-scarce and landlocked; and resource-scarce and coastal. However, the resource-rich coastal countries and the resource-rich landlocked countries can be combined.

The best-performing category globally has been the coastal, resource-scarce countries of which there are many Asian examples.

If the resources are valuable, being landlocked is not a disadvantage to their extraction. Conversely, the coastal countries are generally not in a position to take advantage of non-resource exports because of the apparent link between revenues from natural resources and the weakening of the industrial sector, known as Dutch disease. We thus have three categories which have sharply distinct growth performances. The best-performing category globally has been the coastal, resource-scarce countries of which there are many Asian examples. The worst-performing category globally has been the landlocked, resource-scarce countries. In between, the resource-rich countries have on average grown moderately.

Africa has followed this global pattern, with three differences. First, the largest difference between Africa and other regions was for countries that are resource-scarce and coastal. Since around 1980 the non-African economies have been outperforming their African counterparts by around five per cent per year. The second difference between Africa and other developing regions was in the category of countries that are resource-rich. This difference has persisted since the 1960s rather than exploding since 1980. Only in the category of landlocked and resource-scarce countries, which globally have been slow-growing, is the difference modest.

The implications of these differences in growth rates for the path of GDP per capita have been dramatic. Outside Africa countries have on average decisively broken out of poverty, rising above US$5,000 per capita, as long as they are not landlocked and resource-scarce. They are converging on the developed countries. By contrast, in Africa countries in all three categories have stayed resolutely stuck below US$2,000 per capita.

The African population is skewed towards the globally slow-growing category of landlocked, resource-scarce.

The third difference between Africa and the other regions is in the distribution of population between the categories. Outside Africa 88 per cent of the population lives in the coastal, resource-scarce countries, around 11 per cent in the resource-rich countries, and a mere one
per cent in the landlocked resource-scarce countries. In Africa the population is evenly spread between the three groups. Thus, the African population is skewed towards the globally slow-growing category of landlocked, resource-scarce, and away from the globally fast-growing category of coastal, resource-scarce. This accounts for around one per cent slower growth for Africa as a whole.

In Africa countries have stayed resolutely stuck below US$2,000 per capita.

However, the key importance of distinguishing between the categories is that their opportunities are different: growth strategies will not look alike. The opportunities characteristic of each category are detailed in the following sections.

**Landlocked and resource-scarce countries**

The most striking difference between Africa and other regions is in the proportion of the population in landlocked, resource-scarce countries. Outside Africa areas with these poor endowments seldom became countries: they became the hinterlands of countries that are more fortunately endowed.

Globally, there are examples of success among landlocked, resource-scarce countries, such as Switzerland. However, Switzerland has benefited from its neighbourhood. Being landlocked has not cut it off from international markets but placed it at the heart of a regional market. More generally, the most promising strategy for such countries has been to orient their economies towards trade with their neighbours. As the barriers to international trade have come down this has become easier, and outside Africa the growth rates of landlocked, resource-scarce countries have accelerated.

Developments such as e-trade and air-freight that do not disadvantage landlocked countries might offer a new route to global integration.

Growth spills over from neighbours. Globally on average, if neighbours grow at an additional one per cent, that raises the growth of the country itself by 0.4 percent. Outside Africa the landlocked, resource-scarce economies gain larger spillovers, at 0.7 per cent, not 0.4 per cent. They orient their economies towards making the most of these growth spillovers. By contrast, in Africa, the growth spillover for the landlocked, resource-scarce economies is a mere 0.2 per cent – implying that these countries are not orienting their economies towards their neighbours. To date this has not mattered. Until recently even the better-located African countries have failed to grow. There has been little growth to spill over.

Thus, the critical path for the landlocked, resource-scarce countries to succeed is first that their more fortunate neighbours need to harness their opportunities, and then that the sub-regional economies need to integrate. The integration agenda is partly a matter of practical trade policy such as the removal of road blocks. It is also a matter of infrastructure: roads need to be built and maintained.

Developments such as e-trade and air-freight that do not disadvantage landlocked countries might offer a new route to global integration. The landlocked countries should push these opportunities to the hilt. Being landlocked is not a choice, but being airlocked is largely a matter of airline regulation and competition policy. The policies that produced high-cost monopolies were mistaken. The twin pillars of e-trade are international telecoms and higher education. Policies that raise the cost of international telecoms, or make access unreliable, and the neglect of tertiary education, are costly for landlocked, resource-scarce countries.

The African population is skewed towards the globally slow-growing category of landlocked, resource-scarce.

Although these landlocked countries are the core of Africa’s poverty problem it is also important to focus on the other two opportunity categories. It is the inability of the African countries in these categories to harness opportunities that has been decisive.

**Resource-rich**

Resource-rich countries are increasingly important in Africa. Globally, high commodity prices are a mixed blessing for resource-exporting countries. In the past, when export prices have doubled, for the first five years growth has been significantly higher. By the fifth year this faster growth has cumulatively raised GDP by around seven per cent. However, from then on things have typically gone badly wrong. After a further decade, GDP is not seven per cent up but 25 per cent down. Three processes generate this long-term adverse effect: Dutch disease (see above) makes non-resource exports uncompetitive. For example, in Nigeria, oil exports led to the collapse of agricultural exports. Macroeconomic volatility is also damaging: since the discovery of oil, Nigeria has been among the most volatile economies in the world. But the most important problem is that poor governance leads to ineffective public spending.

Resource-rich societies inevitably have large public sectors. The resource rents should be taxed so that they accrue to the nation. Hence, however dysfunctional the
public sector has been, the ‘minimal state’ is not appropriate for resource-rich countries: the public sector must be made to work. Not only is effective public spending critical for its users; more basically, since the public sector is a large part of the economy, its own productivity growth is a key component of overall growth.

Effective public spending requires accountable government. Until recently, the conduct of the international resource extraction companies fuelled the opposite. Companies bribed their way into contracts, empowering the corrupt against the honest. The spread of democracy across much of resource-rich Africa might potentially provide an internal brake on such behaviour. Unfortunately, evidence suggests that globally, instead of democracy improving the way in which resource revenues are used, resource revenues undermine how democracy works. In the absence of natural resource rents democracies grow significantly faster than autocracies. In contrast, in the resource-rich countries autocracies outperform democracies. Making democracy conducive to economic growth in a resource-rich country is likely to be an uphill struggle. Globally, in resource-rich countries democracy tends to get corrupted into patronage politics. This process of corruption occurs because resource rents substitute for the checks and balances upon the use of power. With low taxation citizens are not provoked into scrutinising government and this weakens the checks and balances upon the use of power. This produces an unbalanced form of democracy in which electoral competition, which constrains how power is used, is not matched by checks and balances which constrain how power is achieved. Without strong checks and balances electoral competition drives political parties to resort to patronage: votes are bought instead of won.

Uniquely, in resource-rich societies checks and balances are significantly beneficial for growth, whereas the remaining aspects of democracy in isolation are detrimental. Thus, those resource-rich countries that are democratic need a rather distinctive type of democracy with strong checks and balances. Africa indeed has such a country: Botswana. Botswana has impressively strong checks and balances, notably rules for public spending. All public spending projects had to pass a dual hurdle of honesty and efficiency. Honesty has been maintained by rules of competitive tendering. Efficiency has been maintained by careful technical scrutiny of the rate of return on each proposed project, with the political support to block all projects that fail to meet a critical minimum return. Unfortunately, Botswana is exceptional.

Other resource-rich African countries are now democratic, but they are ‘instant democracies’. As demonstrated by Afghanistan and Iraq, it is possible to establish electoral competition in virtually any conditions, but it is far harder to establish effective checks and balances because nobody has the incentive to enforce them. Nigeria under President Shagari displayed the classic patronage politics of resource rents in the context of intense electoral competition without effective checks and balances. The regime of President Shagari, though democratic, failed to harness the previous Nigerian oil bonanza for sustained growth.

In summary, resource-rich countries need a form of democracy with unusually strong checks and balances, but typically get a form in which they are unusually weak. The leadership challenge is to counter the pressure for the erosion of checks and balances.

The savings decision out of resource revenues is also important. The central bank has a critical role in smoothing fluctuations in revenue to avoid peaks in expenditure. However, there is a distinction between medium-term revenue smoothing and ‘future generations’ funds. The latter are inappropriate for Africa.

Resource-rich countries need a form of democracy with unusually strong checks and balances, but typically get a form in which they are unusually weak.

The cluster effect

Before 1980 manufacturing and services were concentrated in the OECD economies, locked in partly by trade restrictions but mainly by economies of agglomeration. Economies of agglomeration are when many firms in the same activity are clustered in the same city, lowering their costs of production. For example, clusters create a large pool of skilled labour and many suppliers of inputs. Around 1980 a combination of trade liberalisation and the widening gap in labour costs between the OECD and developing countries began to make it profitable for industry to relocate to low-income countries. This process is explosive: as firms relocate clusters build up in the new location and make it progressively more competitive. Unfortunately for Africa, the chosen locations where these clusters became established were in Asia. Once Asia got ahead of Africa, the growth of these clusters made it progressively harder for Africa to break in. Currently, Africa has no significant advantage over Asia in terms of labour costs while having large disadvantages because it lacks comparable clusters.

To induce clusters to form in Africa the region needs privileged market access for its manufactures. While the US now provides such access through the African Growth and Opportunity Act (AGOA), there is no equivalent in the rest of the OECD. Europe’s scheme, Everything-but-Arms, is so badly designed that it has been ineffective. Africa needs a common OECD-wide scheme that would grant AGOA-type temporary access, enabling it to catch up with Asia.
In low-income countries there is a need to build up domestic capital: if spending can be managed well, productive absorption can be quite high. Further, Africa does not have the long stability of political institutions necessary to make the credible commitments involved in future generation funds. The most likely scenario for such a fund is that it is a transfer from a prudent minister of finance to an imprudent minister a few years later.

The essential aspect of government behaviour is that it should not actively inhibit the emergence of a new export sector by burdensome regulation, taxation, or predation.

Hence, the centrepiece of policy towards resource wealth is not the savings decision but the spending decision. Africa’s one remarkable success in managing resource wealth, Botswana, indeed focused on the rules for spending rather than rules for saving. Because Botswana is a landlocked desert it was not possible to spend all the revenues productively and so, under the spending rules, the balance was saved abroad. The savings decision was a by-product of the application of effective spending processes.

Where revenues are very substantial, some of it should be given directly to citizens. The most credible mechanism by which low-income countries can redistribute income directly to households is through the schooling system: children could receive bursaries as is already done through the Progresa system in Mexico. Studies have shown this to be highly effective both in increasing school attendance and in directly reducing poverty.

Breaking with the past depends upon more than high commodity prices. Governments need to develop genuine strategies for growth.

Resource-scarce and coastal

Resource-scarce, coastal economies form the category that globally has had the fastest growth, but in which African performance has been least encouraging. The only African country to succeed has been Mauritius, which has followed the Asian pattern in transforming itself from an impoverished sugar economy into an upper-middle income country.

Whereas in resource-rich countries the state has to be large, in the coastal, resource-scarce economies the state need not be central to rapid development. The core growth process in these economies is to break into global markets for some labour-intensive product.

This is fundamentally a matter for the private sector. The state may, as in parts of East Asia, actively help in this process, but it is by no means necessary. Indeed, the essential aspect of government behaviour is that it should not actively inhibit the emergence of a new export sector by burdensome regulation, taxation, or predation. The easiest way for the state to ‘do no harm’ is for it to be small, and concentrated upon essential public services. Thus, the ‘minimal state’ model may well sometimes be appropriate. The size of the state has too often been derived from ideology rather than from an analysis of opportunities.

Growth strategies needed

The countries of ‘the bottom billion’ need to sustain rapid growth so that they can catch up with the rest of mankind instead of continuing their divergence of the past forty years. Africa currently faces its best opportunity for growth since the commodity boom of the mid-1970s, but breaking with the past depends upon more than high commodity prices. Governments need to develop genuine strategies for growth and in turn, these must reflect the opportunities determined by geography. Despite the rhetoric of the Millennium Development Goals (MDGs), few African governments currently have such strategies.

Paul Collier is Professor of Economics and Director of the Centre for the Study of African Economies at Oxford University. His book, ‘The Bottom Billion: why the poorest countries are failing and what can be done about it’, was published in June.

The Centre for the Study of African Economies (CSAE) has been undertaking research on Africa for more than a decade, and has become one of the largest concentrations of academic economists and social scientists working on Africa outside the continent itself.

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Climate Change: the Challenge for Finance Ministers
The increasing emissions of greenhouse gases, of which carbon dioxide (CO₂) is the main contributing one, are already creating a variety of problems through climate change; further, it is highly likely that the devastating effects will magnify unless urgent action is taken. The greenhouse effect, produced naturally by gases present in the atmosphere and giving the earth the mild temperature needed for life, is being reinforced, resulting in a greater retention of the sun’s radiation, thus contributing to global warming.

Most developed nations have committed themselves to emission reductions targets by 2012 under the Kyoto Protocol. However, stipulated reductions are too modest and, even more importantly, the US, the world’s largest polluter, remains outside the agreement. It is high time now that global warming and climate change are taken up on an urgent basis, locally and globally, to fight one of the major scourges afflicting Mother Earth and her children today.

The most important challenge at the current juncture is to press for the ways and means to stall this horrendous journey towards humanity’s self-destruction and to persuade governments – and other relevant actors such as powerful corporate industrial interests – at different levels from local to global, to embark on a broadly agreed trajectory of sustainable development.

Impacts

Global warming effects have already started showing up with increasing intensity, and some of the most adverse consequences include change in species habitats and habits, acidification of oceans, loss of wetlands, bleaching of coral reefs, increases in allergy-inducing pollen, among others. Rapid and continued loss of biodiversity is taking place at an alarming rate, and the ecological footprint, which measures the extent of human demand on earth’s ecosystems, has tripled since 1961, showing that the planet’s resources are being used at a rate 25 per cent higher than their ability to regenerate (Living Planet Report, 2006).

The recently published Stern Review (UK Treasury, 2006) and the Climate Change 2007 report by the Intergovernmental Panel on Climate Change (IPCC) compile current knowledge about the future, and some of their critical findings demand serious actions regarding the way we treat our ecosystem.

Another aspect of climate change that is becoming increasingly clear is its potential as a major source of local national and global conflicts. Disputes over water resources, food production and land use, exacerbated by changing rainfall patterns, may erupt as the effects worsen and constraints over scarce resources increase. Christian Aid’s May 2007 report Humantide: the Real Migration Crisis warns of significant increases in forced migrations comparable to those during the world wars, as climate change will undoubtedly exacerbate conflicts over scarce resources. As many as one billion people are estimated to be forced to move their homes in less than half a century. Indeed, projections put Bangladesh’s loss of surface due to sea-level rise at around 20 per cent by the end of the century. In Christian Aid’s words, it will be the world’s most vulnerable communities who will have to “bear the brunt of the ‘future shock’” (The Climate of Poverty, 2006). A large majority of the potential victims are inhabitants of Commonwealth countries. In particular, Africa and Asia, because of their
geography, their housing of the largest numbers of vulnerable people, their multiple stresses and low adaptive capacities, will by and large be most affected. The Stern Review reports the following projections:

### Africa
- Over 200 million people may be exposed to water stress.
- Food production may decline in some areas by as much as 50 per cent by 2020.
- Over-fishing and rising water temperatures will decrease fisheries resources.
- By the end of 2100, up to 5–10 per cent of GDP per annum may be absorbed for adaptation to sea level rise.

### Asia
- The melting of glaciers in the Himalayas will bring about more flooding.
- Climate change effects, along with increasing populations and higher demands due to improving standards of living, will decrease fresh water availability, adversely affecting over one billion people.
- By the middle of the century, crop yields could decrease by 30 per cent in Central and South Asia.
- Floods and droughts will increase endemic morbidity and mortality due to diarrhoeal diseases, as well as the spread of cholera.

Table 1 presents a futuristic scenario of attainment of the Millennium Development Goals (MDGs), keeping in mind the impacts of climate change, and drawing largely on the information provided by the Stern Report.

### Adaptation and mitigation

Even if developed countries reduced their emissions to nil, global warming would still go on and sea levels will rise for several decades. This means that if we are to avoid the gravest consequences of climate change, developing countries will also have to play a role in mitigation. Mitigating the impact of global warming requires that countries produce fewer greenhouse emissions than the world’s sinks – namely, forests, soil and oceans – can absorb.

Key mitigation technologies and practices available now that are either already commercialised or will be in the next quarter may take the form of shifting from coal to gas, hydropower, solar, wind, geothermal or bioenergy sources as far as energy supply is concerned (IPCC, 2006). Shifts to relatively less polluting modes of transport (such as rail and public transport, increase in cycling and walking) are also helpful. Increased soil carbon storages and soil restoration techniques in agriculture, enhancing afforestation, reforestation, organic composting, water treatment, recycling and waste minimisation, etc, can be practised to check emissions.

However, the use of these technologies by developing countries is still very limited and will undoubtedly require that technology transfers occur. Nonetheless, it is apparent that the current carbon energy-based economy will need to be replaced. Arguably, the abandonment of fossil fuels altogether looks the most plausible way forward as dependence on ‘cleaner fossil fuels’ use may represent an obstacle for a transition into zero-carbon energy.

### Mitigation policies

Mitigation policies that can be beneficial are explained in Making the Kyoto Protocol Work by Anil Agarwal (Centre for Science and Environment, 2000). These include:
- Integrating climate change in broader development policies
- Regulations and standards on emission levels
- Taxes and charges setting a price for carbon
- Emissions tradable permits
- Financial incentives to stimulate diffusion of new technologies

### Table 1. Climate change and the MDGs

<table>
<thead>
<tr>
<th>MDG</th>
<th>Situation by 2100 with Climate Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Goal 1</strong>: Eradicate extreme and one poverty and hunger</td>
<td>At 3°C, around 150-550 million additional people around the globe are under the risk of hunger to three million die of malnutrition every year. An additional 145-220 million people would be living on less than US$2 a day by 2100.</td>
</tr>
<tr>
<td><strong>Goal 2</strong>: Achieve universal section of primary education</td>
<td>Climatic disasters can threaten educational infrastructure making it physically impossible for children to attend school. Schooling may become less affordable and accessible, especially for girls.</td>
</tr>
<tr>
<td><strong>Goal 3</strong>: Promote gender equality and empower women</td>
<td>Workloads and responsibilities of women such as collecting water, fuel and food will grow and become more time-consuming in light of greater resource scarcity.</td>
</tr>
<tr>
<td><strong>Goal 4</strong>: Reduce child mortality</td>
<td>An additional 165,000 to 250,000 child deaths are expected per year in South Asia and sub-Saharan Africa by 2100</td>
</tr>
<tr>
<td><strong>Goal 5</strong>: Improve maternal health</td>
<td>Severe malnutrition may increase the problems.</td>
</tr>
<tr>
<td><strong>Goal 6</strong>: Combat HIV/AIDS, malaria and other diseases</td>
<td>Even at 1°C, 300,000 people may die every year due to climate related diseases like malaria.</td>
</tr>
<tr>
<td><strong>Goal 7</strong>: Ensure environmental rising sustainability</td>
<td>Addition of another two to three billion people to the developing world’s population because of sea level and desertification in the next few decades. Add to this the natural growth in population in the developing world by another two to three billion by 2050, and the future seems catastrophic.</td>
</tr>
<tr>
<td><strong>Goal 8</strong>: Develop a Global Partnership for Development</td>
<td>Increased competition and conflicts over resources may lead to growing distrust among nations, a problem already rampant in many regions of the world. This will obviously diminish further the prospects of sustainable use of resources.</td>
</tr>
</tbody>
</table>
• Voluntary agreements, and  
• Research, Development and Demonstration (RD&D).

The Kyoto Protocol, established by the United Nations Framework Convention on Climate Change (UNFCCC) and adopted by most developed countries, includes the stimulation of a set of national policies, the creation of an international carbon market and the establishment of the Clean Development Mechanism (CDM). It has been proposed in some quarters that border tax adjustments be imposed on products originating from non-signatory developed countries as a way to enforce emission curbing. However, this measure seems to be less feasible politically. Reducing emissions involves substantial changes in the current model of economic development and a change in the global economic order.

Responsibilities

It is no secret that since the early stages of industrial revolution, developed countries have increasingly been leading the world in terms of greenhouse gas emissions. Indeed, not only do developed countries bear responsibility for most of the historical emission but also they present much higher current per capita emission figures – along with some Middle East oil producers and former so-called communist states. Four countries, however, reveal extraordinarily shocking trends in terms of per capita emission, namely the United Arab Emirates, the US, Australia and Canada, in decreasing order. In fact, a US citizen accounts for as much emissions as two Germans, or six Chinese, or 12 Brazilians, or almost 17 Indians.

The UNFCCC has acknowledged that responsibility and mitigation efforts should be assumed and paid for, respectively, on a per capita emissions basis. Nevertheless, the moment to take measures and establish emission caps for the period 2008-2012 through the Kyoto Protocol, the US backed out of the agreement, challenging the equitable approach that had previously been almost unanimously agreed upon.

Rapidly growing developing economies obviously need to confront their own moral responsibilities and work with the developed world to find solutions consistent with a just global socio-economic order. What is crucial is collective but differential responsibility on a global scale. This should be the guiding principle and Commonwealth countries should strive towards the realisation of this principle.

A policy perspective

It should be clear from the preceding discussion that in order for the global community to address the pressing issues of climate change regarding adaptation and mitigation, mainstreaming sustainable development should be a priority on the national and global agenda.

At the international level, developing countries must seek that developed countries abide by the widely accepted principle of per capita emissions rights, which is consistent with the principle of equity and fairness. This is where robust alliances and partnerships between civil society organisations in the North and the South are absolutely critical. Together they should press for the establishment of a Disaster Relief Fund to address the issues relating to mitigation and adaptation costs; such a fund ought to be under the administration of the UN. The developing countries, and not only donors from the advanced countries, should be able to participate in the processes related to the management of that fund.

Finally, another key element could be the inclusion of a ninth Millennium Development Goal (in the current list of eight major MDGs) related to adaptation and mitigation of global climate change. This would harmonise the mutually enhancing synergies between sustainable development and climate change combat.

The very brief menu of policy measures suggested here largely pertains to the domain of government action. However, it is worth emphasising that such measures hardly have a chance without active participation of civil society organisations. This would be particularly so in the context of several developing countries with low levels of literacy, awareness etc. Furthermore, the nature of the problems is such that the stakeholders from grass roots to the higher echelons of society and economy have to take ownership of the challenges and the concomitant responsibilities.

The unmitigated accumulation of greenhouse gases in the atmosphere poses ever-greater risks, and the policy challenge is to find the most cost-effective, efficient and equitable way to reduce these risks. It is worth re-emphasising that the problem is not going to be solved without international collective action: there is no laissez-faire solution. As Albert Einstein observed, ‘today’s problems cannot be solved if we still think the way we thought when we created them’.

Praveen Jha is on the faculty of Centre for Economic Studies and Planning, Jawaharlal Nehru University, New Delhi, India. His major areas of interest include labour and agriculture with special focus on the developing countries. His other areas of interest include resource economics, history of economic thought and macroeconomics of developing countries.

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International energy security: the agenda for the Commonwealth

Energy is on the policy agenda for every Commonwealth government. For some, such as Trinidad and Nigeria, the issue is the orderly development of oil and gas resources in a volatile market. For others, including India, the primary challenge is to secure supplies as import requirements increase. For all there is the looming question of climate change and the associated dislocation to economic and social life. The common factor is that energy is no longer taken for granted. There is a sense of insecurity for producers and consumers alike. The insecurity runs across the Commonwealth member states and well beyond. What can we do to restore the lost sense of security in the years ahead?

Why is energy a topic of such live attention in the media and increasingly a matter of concern to citizens across the world?

The first answer to that question is the growth in demand. Worldwide energy demand has risen by 20 per cent just since the turn of the century. That is in just six years. The growth in demand is driven by two fundamental forces – population growth and prosperity. At a guess it will take you an hour to read four or five articles in this book. In that short time the world’s population will rise by almost 10,000. That means over 200,000 new global citizens every single day.

Linked to that is the spread of prosperity. As Fareed Zacharia pointed out recently in Newsweek, who would have imagined on September 12th, 2001, that the following five years would be one of the strongest periods of economic growth across the world in the whole of the last 200 years?

The growth in energy demand has been strongest in Asia. In India energy demand has risen by 65 per cent in the last 15 years, even though per capita consumption is still less than a tenth of the OECD average. Chinese demand is up by almost 60 per cent since the turn of the century.

Particular countries have grown particularly rapidly. Chinese GDP is up by more than 50 per cent in just six years. In that time energy demand rose by 70 per cent. India too has enjoyed rapid growth and energy demand there in the last decade is up by 30 per cent. As people emerge from poverty they start to use commercial energy, and the best estimate is that across the developing world there are 150 to 200 million new consumers of commercial energy every year.

The authoritative forecast of the International Energy Agency is that energy demand will continue to grow by over two per cent a year over the next decade and beyond. If that doesn’t sound like much, consider that it means that the total annual consumption of France is added to the demand total every year.

Supply challenges

The second challenge concerns supply. Most of the growing demand for energy has been met, and will continue to be met, by hydrocarbons. At the moment 80 per cent of daily supply comes from oil, gas and coal. But supply is also about trade. For the poor in Africa or Asia energy is local. But the most dramatic change in the world economy since the Second World War has been the growth of trade – and energy trade has been at the heart of that.

Now there are four major regions in the world which are dependent on energy imports – the US, Europe, Japan and China. India is well on the way to joining the list. All will need to import more as time progresses.

As well as the growth in demand the reason for the increased import requirement is that indigenous...
production is beginning to fall. In the North Sea, for instance, the production of oil and gas is now declining by over 10 per cent a year. The same is true in other mature provinces around the world.

Within a decade two-thirds of all the oil the world uses every day will be traded before it is consumed and the supply to meet that requirement will principally be met from just three exporting regions: West Africa – which means Nigeria and Angola; Russia; and the five states around the Persian Gulf – Abu Dhabi, Kuwait, Saudi Arabia, Iran and Iraq. Those countries will account for almost 80 per cent of total oil trade within the next decade.

A similar position applies for natural gas. Many developed economies including the UK and the US are no longer self-sufficient and again supply is concentrated. Although supplies from Trinidad, Australia and Nigeria are important, 60 per cent of remaining identified gas reserves lie in just three countries – Russia, Iran and Qatar.

These more advanced countries seem determined to capitalise on their advantages regardless of the consequences for countries which are less advanced.

Concentration is one part of the problem. The other factor we have to be aware of is the nature of control over the resources. In an open market demand would stimulate supply. But energy is rather different. Up to three quarters of all the identified reserves of oil and gas are under state control. That means that decisions to invest in new production and infrastructure could be, and in fact are being, dictated by national priorities rather than market circumstances.

Climate

Then there is the issue of climate change. As we use and burn hydrocarbons we produce waste including emissions of carbon, some of which go into the atmosphere. The concentration of carbon in the earth’s atmosphere continues to grow.

We know that the annual carbon dioxide concentration growth rate was larger during the last ten years – with an average addition of 1.9 ppm per year – than it has been at any time since the beginning of continuous direct atmospheric measurements. We know from the report of Working Group 1 of the Assessment report published by the Intergovernmental Panel on Climate Change (IPCC) in February that 11 of the last 12 years rank among the 12 warmest years in the instrumental record of global surface temperature – that is since 1850. Of the 24 warmest years, 23 have occurred since 1980.

We know that sea levels rose by an average of 3.1 mm per year over the period from 1993 to 2003 – almost twice the historic average rate of increase. The IPCC estimate is that there will be a further sea rise of 0.5 m between 2001 and 2100. But that may be an underestimate, because of the melting of the ice cap of Greenland and the Arctic regions. We know that the extent of arctic ice has declined by some 2.7 per cent each decade since the 1970s.

We know that the number of wildfires, the average wind speed and the frequency of cyclones have all increased in the last two decades.

Every one of those points is a matter of measured fact

No one can predict the future with comparable accuracy but as the evidence mounts the direction of change is clear. The climate is changing, and will continue to change. The change will not be uniform. Some places will get warmer, some wetter. Some will be severely affected and estimates of averaged global changes can be misleading. The changes have begun and will continue and as well as a general tendency to get warmer, the climate looks set to be much more volatile, with weather conditions more extreme and less predictable. For Commonwealth countries in Africa and the Indian subcontinent, where most of the population depend on reasonably stable weather conditions, the prospect of unpredictable and often extreme climatic variations is extremely worrying. For the smaller island states the longer-term but inexorable rise in sea levels raises different but more fundamental challenges.

Responses

So those are the challenges – demand growth, supply concentration and the impact of climate change. How do we start to construct a response and move back to a position of greater security? How can we make what the UK foreign secretary David Miliband described in a speech in Cambridge earlier this year as a transition to a low carbon economy which is comparable in scale and scope to the transition which the developed world made to the industrial revolution over 200 years ago?

First we must be realistic and avoid the myths which tend to make a difficult situation seem worse. The first myth is that energy supplies are about to be exhausted. Oil and gas are not running out – there is no great physical shortage and these sources will provide most of the world’s energy supply for the next several decades.

To date some one trillion barrels (bbl) of oil have been produced. But another 1.3 trillion of proven, identified reserves remain to be produced. And there are at least another one trillion bbl of conventional resources still to be found. That is on the best authoritative estimates produced by the US Geological Service. For natural gas the figures are even larger. 80 per cent of total resources still remain to be produced. Even these figures do not tell the whole story – there are for instance huge volumes of heavy oil supplies, not least in Canada.
Climate Change: the Challenge for Finance Ministers

‘Stabilization wedges’

An important piece of work by Professor Robert Socolow at Princeton University has identified what he has called ‘stabilization wedges’ (Science 305) – possible steps, all within the scope of known technology, which could contribute to improving the diversity of energy supply and keeping emissions down. There are 15 wedges in total, but to mention a few: One could increase the fuel economy of two billion cars from an average of 30 miles per gallon (mpg) to 60 mpg. One could replace 1,400 large-scale coal-fired power stations with natural gas fuelled stations. The carbon from coal could be extracted and stored at 800 large-scale coal plants. All the cutting and burning of forests could be halted – since deforestation causes 20 per cent of world’s annual CO₂ emissions. The output from nuclear power could be doubled.

Of the 15 wedges, seven would need to be pursued progressively from now on to 2050 to eliminate the risk of increasing carbon concentration. They are all known technologies, which are moving rapidly in response to investment. In the case of power stations the change is potentially made easier by the fact that so many new stations are being built, each of which could be designed in an emissions-friendly fashion.

Some of the wedges may be politically unacceptable in some places, but there is enough in the mix to make stabilisation of the level of carbon concentration in the atmosphere feasible.

So there is no physical shortage. Oil will peak one day but not because it runs out. It will peak as the use of stones or wood peaked at the end of the stone age – because people begin to use something else.

Then there is a second myth, which is that if we want to solve the energy challenges we should just use less energy. Like many myths this is built on a kernel of truth – the extremely legitimate belief that we can use energy more efficiently. There are great potential efficiency gains that we can and should realise.

But using energy more efficiently doesn’t mean that the world as a whole will use less. The plain fact is that we live in a world of 6.5 billion people. There will be eight billion by 2020 or thereabouts, and they will need more energy. It would be impractical and immoral to deny India and the other developing countries of the world the right to grow and to improve living standards.

Energy demand will grow and the challenge is to change the ways in which energy is produced and used and the impact of its consumption to reduce the risks and the costs. And that can be done.

And that brings into focus the third myth – fatalism. The feeling that energy security in general and climate change in particular is just too big and too global a problem for us to be able to do anything. That may be a common perception but, as the theologians remind us, despair is the ultimate blasphemy and there is absolutely no excuse for any despair in respect of energy security and climate change because we can see much of the way forward.

Science and engineering are not static. There is great potential across a whole range of different technologies. It is possible that we will see a great breakthrough in the science of alternative fuels. At the moment they make only 20 per cent of world’s annual CO₂ emissions. The output from nuclear power could be doubled.

There are possible advances in material science and in the storage of energy – in battery technology. That too could transform the energy system. And there are possible advances in other sciences such as biology which could for instance transform the potential for biofuels, carbon sequestration and the reuse of waste.

The overall point is that we are dealing with the art of the possible. There is no cause for despair and fatalism. There are solutions available already and more in prospect. But the problems are still real and the process of change is not automatic. If we want to restore energy security three fundamental steps are necessary:

• First: carbon must be priced and the market mechanism employed to encourage the development and takeover of the existing alternatives, as well as the research needed to provide further choices. Without a carbon price, emissions will continue to rise and so will the costs of taking action, as Sir Nicholas Stern has pointed out so clearly in his report to the UK Prime Minister.

• Secondly: we need a trading system which ensures that the necessary reduction in emissions is achieved at the lowest practical cost, and in a manner which recognises the imperative of continued economic development.

• And thirdly: we need a programme now to enable countries across the world – including many Commonwealth member states – to adapt to the changes in climate and weather conditions which are already under way. That issue, which is on the agenda of the Guyana meeting, is one on which the Commonwealth can take a substantial step forward to the benefit not only of its members but of the international community as a whole.

Nick Butler is Director of the Cambridge Centre for Energy Studies.

The Cambridge Centre for Energy Studies has been established to analyse the key issues of international energy security. Its approach is multidisciplinary and will draw on skills from across Cambridge and beyond. The Centre’s initial projects will focus on security of supply from Russia, on the development of international mechanisms to manage the reduction of greenhouse gas emissions, the use of energy in cities, and the role of state oil and gas companies in the international energy market.

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Insurers and the trillion dollar gamble

The insurance and reinsurance sectors, parts of the largest global industry with over US$3.7 trillion in premiums collected annually, were one of the earliest business areas to wake to the economic and social threats presented by climate change. By the mid 1980s, some of the most forward-thinking leaders in the industry had asked their research departments to analyse the potential impacts of climate change to their businesses. In this article the author weighs the implications of the latest initiatives.

When the world’s governments meet again in Bali in December for the latest round of international climate change negotiations, the insurance sector will be present once more. The industry’s understanding of climate change has moved on in a dramatic way since the 1980s. The Bali gathering, convened by the parties to the United Nations Framework Convention on Climate Change (UNFCCC), comes at the end of a year when both the political and economic concerns surrounding the impact of climate change have again heightened considerably.

While much research and analytical work remains for insurers to deepen their knowledge of the vastly complex interactions governing climate change, the challenge for the sector is shifting. In both the OECD constituencies, the emerging economies and the developing world, a growing focus is being placed on the types of insurance products and services needed to serve a world that will have to adapt to the uncertainties of more volatile weather patterns, the impact of extreme events and the economic and social challenges that climate change will bring. Critically, some of the poorest and most vulnerable communities in the world, where insurance cover of any kind is often non-existent, will face the greatest economic burden. An effective response, in order to ‘insure the uninsurable’, will demand public and private sector collaboration that yields true innovation in terms of delivering an affordable, accessible and rapid insurance response, to enable vulnerable communities to face the impacts of climate change with some degree of confidence that they can survive the crisis and rebuild broken lives.

A group of the world’s leading insurance companies joined with the United Nations Environment Programme (UNEP) in 1995 as part of a unique public–private partnership called UNEP Finance Initiative. UNEP FI brings together 170 financial service companies from the insurance, banking and investment sectors. Insurance and reinsurance companies such as Allianz, Aviva, AXA, Insurance Australia Group, Munich Re and Swiss Re have led UNEP FI’s work in climate change. In 2002, UNEP FI delivered a major study exploring the threats and opportunities to the global financial services sector from climate change. The group predicted the likelihood of US$150 billion losses a year to the global economy from extreme weather events and natural disasters within a decade. The annual loss figure was reached just three years later in 2005.

The UNEP FI group presented their latest report, Adaptation and Vulnerability to Climate Change: The Role of the Finance Sector, to governments meeting for the 2006 UNFCCC negotiations at UNEP headquarters in Nairobi. The thrust of the report was that “new kinds of insurance and financing are urgently needed in developing countries to assist them in adapting to current and future climate change”. The study warned also that losses from extreme weather events linked to climate change are doubling every 12 years and that within 40 years the world could witness a year in which losses from droughts, storm surges, hurricanes and floods hit one trillion US dollars.

When the report was released Achim Steiner, UN Under-Secretary General and Executive Director of UNEP, commented: “Adaptation to climate change is a wide-ranging issue which is already touching on every facet of economic and development life. The finance, insurance and re-insurance industry is skilled in the management of risk. In the past, this creativity has been largely confined to covering people and populations in developed countries.
“However, the reality of climate change is spawning new ideas which are now beginning to emerge. These make it possible to bring instruments to people and communities who have in the past been denied access to the formal insurance and finance markets. They also offer the UN and donors fresh and potentially lower cost avenues by which they can nip a climate-linked crisis in the bud before it develops into a full-scale and much more costly disaster,” he added.

Importantly, the UNEP FI study presented to governments at the Nairobi climate meeting called for closer public-private efforts to forge a ‘triple dividend’ (See diagram) of advantages in which the sustainable development, disaster management and climate change communities seek to work together to engineer a more effective response to the climate peril. Often the fragmentation and ‘silo mentality’ that exists among the three communities precludes certain pathways of innovation. In the report the UNEP FI members state:

“Forward-looking policy can reduce the effects of climate change by anticipating the future regime of sea level rise and weather, in order to capitalise on opportunities and minimise harm. Conventionally, this means identifying the planning horizons for key impact areas and sectors, developing plans and planning capability, selecting the best options and implementing them well. It also entails contingency planning to deal with impacts and responding effectively to climatic disasters. A fundamental new dimension is emerging: the need to integrate adaptation policies with policies for sustainable economic development and disaster management, to achieve a ‘triple dividend’ from scarce resources.”

Now, as part of UNEP FI’s response to the need to push innovation in the development and rollout of new insurance products and services to serve both climate change and the broader sustainability agenda, UNEP FI in 2006 created an Insurance Working Group (IWG) to compliment the work of its Climate Change working group. UNEP FI’s IWG is a strategic alliance of seventeen leading insurers from fourteen countries who are committed to advancing the principle of sustainability as an integral part of their corporate responsibility. In May 2007, in its inaugural report,
client education and having mechanisms for collecting premiums and paying claims. Thus, financial literacy and education of risk management techniques are key to the development of microinsurance.

**A wind of change with weather derivatives**

One innovation that has been identified by the Climate Change Working Group of UNEP FI is the use of simple weather derivatives to extend microinsurance into crop insurance for poor farmers.

Microinsurance can support most of the UN Millennium Development Goals by delivering products such as weather derivatives for farmers and health insurance for families. The solvency of such schemes could be underpinned by natural catastrophe pools, public-private partnerships and alternative risk transfer (ART) products such as catastrophe bonds. In this respect and building on the working of its fellow Climate Change working group, the UNEP FI’s IWG is undertaking a study that will link these innovative insurance products and mechanisms with the twofold aim of propelling sustainable development and optimising business opportunities.

More innovative insurance schemes are emerging as a result of extreme weather events and the need for immediate access to funds. This year, the Caribbean Catastrophe Risk Insurance Facility (CCRIF) was established. The facility acts as a backstop against natural catastrophes, particularly hurricanes and earthquakes, and offers participating governments from the Caribbean with immediate access to funds in the event of a major disaster. The facility is funded by the World Bank and donor countries (e.g. Canada and the UK) and is insured with UNEP FI member Munich Re, Paris Re and the Hiscox Syndicate at Lloyd’s. It is the first regional disaster insurance facility in the world.

**Financial services acting together**

As well as the action taken by individual companies or newly evolving public-private partnerships, the financial services sector and capital market actors are working together to forge new commitments and new ways of business in response to climate change and other sustainability challenges and opportunities.

Since 2003 the range of new activities and initiatives from the finance sector have been staggering. Just two major developments highlight the point.

Ahead of the 2007 gathering of the leaders of the G8 countries, a group of UNEP FI institutions, including insurance and reinsurance companies, released a forward-looking statement to be presented at the Bali meeting, challenging governments, policymakers and the sector itself to work directly together to craft more effective policies to climate change, to garner better responses from capital market and financial sector players.

At the same time, some of the world’s largest investors have backed a set of Principles for Responsible Investment (PRI) launched by former UN Secretary-General Kofi Annan in April 2006. Just a year after launch, some 230 institutional investors – from 30 countries and representing US$10 trillion in assets, approaching 20 per cent of global capital market value – have backed the PRI, an initiative of UNEP FI and the UN Global Compact. The PRI is a strong signal from the world’s biggest investors, including pensions funds, special government reserves and foundations, that environmental and social issues, such as climate change, as well as the manner in which our companies and markets are governed, is fundamental to creating stable, vibrant and thriving communities upon which vibrant and effective markets will be based.

These two examples highlight a stark choice for financial services sector companies grappling to understand complex challenges such as climate change for their future business. Companies can decide either to be defined as institutions seeking to provide innovative financing, investment and insurance solutions to some of the most pressing challenges and most promising commercial opportunities for future decades; or they can maintain ‘business as usual’ and be defined by the grime and pollution of the industrial past. UNEP FI and its 170 member companies have engaged, quite categorically, with the forward-looking agenda.
Community based adaptation in Bangladesh: sharing lessons within the Commonwealth

Global warming and climate change are evolving fast. The signs of their advent are clear and loud, the science is beyond any doubt. Within the Commonwealth, millions of people are vulnerable and the number of such potential victims is phenomenal. Past development gains and present efforts are threatened and sustainability questioned. Communities, especially in the front line, are the most vulnerable. For them, community based adaptation (CBA) can play a vital role in building resilience to climate change. In this article, thoughts on the community approach to adaptation to climate change in Bangladesh are shared in the interest of others in the Commonwealth.

Sharing experiences among countries, the lessons from practice or plans for the future, offers opportunities to explore how communities can engage and participate in decision-making processes and promote collective leadership, ownership and responsibility. These are in fact some of the essential ingredients to build resilience.

Bangladesh, one of the countries thought to be most vulnerable, is in desperate need of adaptation. The country is located in South Asia and covers one of the largest deltas in the world, second to the Amazon, and formed by multiple river systems, in particular the Ganges, the Brahmaputra and the Meghna rivers. The land, 80 per cent of which is unconsolidated flood plain, has also tertiary hills areas in the north-east and south-east (12 per cent), and Pleistocene terrace areas in the north-west and central zones. The total land area is 147,570 square kilometres, and bounded by 4,685 kilometres of land, river and sea lines. A network of 230 rivers with their tributaries and distributaries criss-cross the country, and therefore the country is virtually a conglomerate of islands. The population was 144.2 million in 2005 with per capita Gross Domestic Product (GDP) of US$447 per annum (2005-2006). The average population density of about 980 people per square kilometre is a nightmare for planners and population scientists.

Development challenges
Bangladesh has the highest rural population density in the world. Most live along the vulnerable flood plain and coastal belt, where poverty is strikingly prevalent.

The Bangladesh economy is predominantly based on agriculture, contributing about 22 per cent of GDP. This sector also accounts for the majority of employment (over 51 per cent), which is again strongly characterised by seasonal variation. In some places, human miseries, a phenomenon locally known as monga, in areas of north-western part of the country, are caused by the unequal seasonal distribution of employment. Diversity of agro-economic features is another interesting aspect. Now a gradual but slow transition to industrialisation is evolving. Increasing demand for land for urban and alternate economic activities is having a telling affect on the availability of land for agriculture. Per capita availability of net cultivable area is estimated to reduce to less than half of its present value in the course of the next 40-50 years. This will put strain on future land use pattern. The problem of food security will become a point of major concern. The problem will be compounded further by the declining global output of grain production, mainly due to the competition from bio-fuel crops. The vertical expansion of the agriculture system of Bangladesh will thus assume new and complex challenges.

Climate challenges
Bangladesh is extremely vulnerable to climate change impacts because of its geographical location, high population density, high levels of poverty and the state of technological expertise and knowledge. The threat to climate sensitive sectors, particularly rural agriculture and fisheries, is enormous and complex. Consider that, if a part of the coastal area is permanently submerged due
to rise in sea level, people will move inland, the area of which will have decreased in size – thereby increasing the average population density to over 2,000 per square kilometre by the turn of the century or even before. Such a density has never been experienced anywhere else. The demographic nightmare will put severe stresses on life, employment, food, disease, nourishment, overall production system and practices, housing, access to water and above all poverty. It is estimated that in the event of a rise in sea level, over 30 million people will become environmental refugees permanently. The size of this vulnerable group is more than the total population of many countries of the world.

Adaptation as well as mitigation

Global negotiations on mitigation of emissions-induced climate change may possibly lead to some collective action on mitigation. Meanwhile, as the collective endeavours proceed, some of the changes will be irreversible for Bangladesh. The overall warming phenomenon will compound the issues and options in extraordinary proportions and in a rapidity not encountered ever before. The price of this experience, however interesting it could be for the scientists of the future, will be appalling for Bangladesh. Some early alarms are already too loud to ignore.

Recognising this realistic scenario, Bangladesh has formulated her National Adaptation Program of Action (NAPA), identifying a set of interventions of technical, administrative and management nature, which are focused on preparing the people to adapt to inevitable changes that are around the corner. Several of the identified fifteen priority areas of actions are community based. In addition, the Climate Change Cell of the government has commissioned research on adaptation to climate change in the health sector, crop insurance, and climate friendly crop varieties. Research to find options for community level adaptation continues. For example, Bangladesh Rice Research Institute (BRRI) has developed and released several rice varieties like BR 23, a late planting variety to facilitate cropping in low-lying land where floodwater recedes at a later time; the BR 40 and BR 41, which are saline (up to 7-8 Ds/m) tolerant varieties; and the BR 33 and BR 39, short duration varieties that enables harvesting of Boro (winter rice variety) crop in flash flood affected areas, which is envisaged to counter the effects of any late flood.

The tasks don't stop at agriculture; adaptation issues cut across other activities of human engagement. The mixture includes mainstreaming climate issues, planning and priority of normal and emergency development efforts, communication, health, especially the vector diseases, education, housing, flood protection and encroachment of salinity inland, nutrition including food security, access to potable as well as irrigation water, and other things. Bangladesh has to go ahead without waiting for an international consensus, especially as the life of the vast majority of its population is under imminent threat.

Above all the country needs ‘defence in depth’, materialised by rows and strips of green belt, including mangrove forest. These could add to the resilience. To us, afforestation of coastal areas is not only a defence against calamities; rather it improves tree canopy coverage and at the same time improves natural sinks of GHG. Bangladesh then can lead the way in mitigating emissions, not by default but by strategic choice. We must help others by pursuing a path of sustainable development.

Community based adaptation

Development projects and programmes in the natural resources management, livelihood diversification and enhancement including water, agriculture and fisheries, have so far introduced and practiced a number of adaptation initiatives engaging NGOs as well as formal and informal local organisations. The following salient practices are notable, especially as some of these are really innovative and cost-effective:

- Feasible and cost-effective flood resistant housing with reinforced concrete posts with footings, short reinforced concrete stumps and treated bamboo posts; treated jute stick woven mat partitions to increase durability; better bracing and fasteners for protection against high winds; plinths and floors made with a mixture of soil, cement and coarse aggregates; corrugated iron sheets as roofing material to reduce maintenance cost.
- Post-flood coping: the communities in Bangladesh cope as the flood recedes through taking activities like: mending houses and boats; draining floodwater from agricultural land; and cage aquaculture, a recently adopted strategy for fish culture in the waterlogged south-western coastal region.
- Mele (Cyperus Tagetiformus) is a moderate saline tolerant reed that can grow in high water levels. Depending on species variety, Mele can grow in saline, brackish and fresh water. This saline resilient reed is proving to be one of the best potential means of reducing vulnerability to floods and sea-level rise.
- Saline tolerant non-rice crops such as maize and grass as fodder are cultivated by communities in south-western Bangladesh to increase crop rotation, along with the retention of nitrogen and other nutrients in the soil for a longer time than usual.
- Small-scale homestead fish culture in pens in the floodplain, alongside the homestead during the time of flood.
- Choosing a rice variety (late transplanting cultivars) or bringing seedlings from other places selecting a quick growing low-cost non–rice minor crop, or skipping, if deemed appropriate, the entire cropping season.
- Cultivation on floating beds, called soil-less agriculture or hydroponics, is an indigenous practice in the south-western part of Bangladesh. Hydroponics is a traditional agricultural practice in some parts of the region where waterlogging is a regular phenomenon.
• Paddy-fish culture to adapt with the inundation and maximise productivity.
• Portable fuel-efficient earthen stoves for flood-affected communities in the south-western coastal region of Bangladesh.
• Raising ducks during the monsoon: when agricultural land is damaged, people of the south-western coastal region of Bangladesh resort to raising ducks in cages or common water bodies such as ponds.
• Priming chickpeas by soaking them overnight in water is practiced by the farmers of the dry areas in Bangladesh. This ensures better germination and crop yields.
• Rainwater collection is providing safe drinking water in arsenic-affected areas and during times of drought.

These examples provide a glimpse of the different options considered and practised by the people of Bangladesh in different locations facing and experiencing a number of climatic hazards and extremes. The examples also indicate the importance of local and traditional knowledge, as well as available local resources in identifying and pursuing community based adaptation.

In this respect, an important lesson from our experience is to focus on such factors as local physical context, human society, economy and livelihood, and vulnerability, as a starting point. The next step would be identifying local knowledge, capacity, how-to, resources to consider and plan community based adaptation options. This inclusive approach is a pre-condition to sustain the knowledge, process as well as results, towards building community resilience. Many of the good practices presented here are drawn from proven practices among communities for many years and were identified for adoption by community representatives for these interventions.

The role of the government

Bangladesh is pursuing Climate Risk Management and Adaptation through the Climate Change Cell of the Department of Environment under the Comprehensive Disaster Management Program (CDMP). In this respect the government is pursuing Community Risk Assessment and Participatory Action Planning for Risk Reduction and Adaptation. The process is currently piloted in seven districts representing hazard prone areas of Bangladesh. Also, an adaptation need prioritised in the Bangladesh National Adaptation Programmes of Action (NAPA, 2005), titled Community Based Adaptation to Climate Change through Coastal Aforestation in Bangladesh, has recently been approved by the Global Environment Facility (GEF) under the LDC Fund of the UNFCCC. Bangladesh, along with several countries, is also piloting community based adaptation through the GEF Small Grants Program. These clearly demonstrate the government’s recognition and commitment to integrate community based adaptation. We have to be proactive in our adaptation strategies. Reactive actions may result in adaptation at the cost of sustainability.

Conclusion

For countries and communities, the need and scope to adapt to the adverse impacts of climate change will be different and will depend on the types of hazards involved, the nature and extent of vulnerability, and capacity of the government and people to manage and reduce risks. Also, the degree to which national and local policies, institutions and processes are responsive to the needs of communities is of great importance in planning and managing vulnerability reduction and capacity building for resilience.

Adaptation to climate change at community level can be considered as spontaneous or planned actions, modification, changes in behaviours, attitudes and practices in the way people struggle to maintain or improve their well-being and security through formal and informal institutions.

It should be noted that each case where communities adapt successfully to address climatic risks provides useful lessons on how they engage and participate in assessing vulnerability, decide and plan to take actions, and implement those actions. For any community based adaptation approach to be successful, a core prerequisite is community participation. This is evident and demonstrated in leadership, ownership, and practice. Another important precondition is that the adaptation required at the community level is considered as a part of ongoing local development processes and actions, not as an isolated, ad-hoc or externally driven action.

It is imperative that adaptation potentials and capacity needs of communities be explored by different actors and stakeholder groups from Bangladesh. The need for bilateral and multi-lateral development partners can hardly be over-emphasised. The immortal song of George Harrison sung at the Concert for Bangladesh during our War of Liberation in 1971, “My friend came to me, sadness in his eyes … Bangladesh, Bangladesh …” needs to be sung again, possibly with some additional and stronger words.

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Climate change: charting a Caribbean response

Two significant developments may have triggered an explosion of interest and concern about the climate change problem – a boiling pot that has, until now, been building up pressure on the back burners of international agenda-setters. The first is the publication of the Stern Report; and the other the publication of the reports of Working Groups 1-3 for the Fourth Assessment Report (FAR) of the Intergovernmental Panel on Climate Change (IPCC). In addition the climate change issue was catapulted into public interest by the publication of Al Gore’s excellent exposition An inconvenient truth, which was later transformed into an Oscar-winning documentary.

Witness, too, the ground surge of activity in the US Congress and in states like California and New York; and the active role of a coalition of American city mayors to reduce their carbon footprint. They, of course, view this problem through the eyes of ‘stewards of the earth’. Witness also the constant reports of devastating floods, wildfires and storms from all corners of the earth and, surprisingly, a typhoon in the Arabian Gulf! All of these have collectively served to place climate change on the agenda of a much wider constituency. This increased visibility reached its zenith, recently, when the issue of climate change and global security was discussed at a special meeting of the United Nations Security Council.

The Stern Report was commissioned by the UK Government to assess the economics of moving to a low carbon global economy. It is the first comprehensive attempt to put monetary values to actions needed for countries to both reduce the level of their greenhouse gas (GHG) emissions (mitigation) and to decrease their vulnerability to the projected impacts of climate change (adaptation). The report calls for immediate action to deal with these issues, emphasises that any delay will incur significant increases in the costs of responding, and warns that action taken in next 10 or 20 years can have a profound effect on climate in the second half of this century and the next. The report observes that response will require, among other things, the promotion of adaptation – particularly for developing countries.

According to the IPCC Fourth Assessment Report, warming of the climate system is unequivocal, as is now evident from observations of increases in global average air and ocean temperatures, widespread melting of snow and ice and rising global mean sea level. For the next two decades a warming of about 0.2°C per decade is projected for a range of GHG emission scenarios.

The consequences of climate change for the CARICOM region

The interlocking effects of economy and ecology are particularly evident in the countries of the Caribbean region. Productive sectors for most of the countries in the region involve the direct exploitation of the countries’ natural resources and are concentrated along the coastlines. Degradation of the natural resources would greatly reduce the countries’ prospects for growth and development. Tourism development, for example, requires infrastructure which may cause the degradation of certain natural wealth. Similarly, land cultivation for agriculture sometimes encroaches on forested lands, and often requires the use of agrochemicals that can contaminate domestic water resources. At the same time, irrigation for agricultural land often depends on the protection of water catchment areas. The countries of the CARICOM are either small islands or have low-lying coastlines; most of
them are therefore particularly vulnerable to the hazards and problems facing small states.

In the Caribbean, more than half of the population lives within 1.5 km of the shoreline. In locations such as the north coast of Jamaica and the west and south coasts of Barbados, continuous corridors of development occupy practically all of the prime coastal lands. Other facilities such as fishing villages, government offices, hospitals and critical utilities are frequently located close to the shore. Changes in sea level and the characteristics of storm events are likely to have serious consequences for these settlements and infrastructure. Almost without exception international airports are sited on or within a few kilometres of the coast. Similarly, the main road arteries often parallel the coast. With projected sea level rise, much of this infrastructure would be at risk from flooding and physical damage, although the degree of risk will obviously vary from country to country. The threat from sea level rise to infrastructure is amplified with the passage of tropical cyclones (hurricanes). In the Caribbean, damage to coastal infrastructure from storm surge alone is often significant. In November 1999, surge damage in St Lucia, associated with Hurricane Lenny, exceeded US$6.0 million – although the storm was many kilometres offshore.

Many islands in the Caribbean are likely to experience increased water stress as a result of climate change and, in some instances, as in the case of the Bahamas, Antigua and Barbuda and Barbados, have begun to invest in the implementation of adaptation strategies, including desalination and rainwater harvesting, to offset current and projected water shortages.

Seawater warming and degradation of coastal habitats (mangroves, coral reefs) can lead to a decimation of the fish stocks, with dire consequences for livelihoods and the food security of the region, Changing weather patterns and soil and aquifer salinisation are further threats to the latter. In Guyana they are already exploring the development of salt tolerant varieties of rice to cope with both estuarine and soil salinisation.

Tourism is a major economic sector in many islands and the effects of climate change will be both direct and indirect. Sea level rise and increased ocean temperature are projected to accelerate beach erosion, cause degradation of coral reefs including bleaching, and degrade the overall asset value of the coast. Such impacts will in turn reduce the attractiveness of these destinations for coastal tourism. In addition more intense hurricanes will destroy tourism plant and infrastructure, creating insurmountable difficulties for the sector, especially in the pervading insurance environment in the region. Most insurance rates in the region are informed by conditions that prevail in southern USA as most of the insured risks are transferred to outside insurers through the reinsurance system. For many in the region these rates are unaffordable, leading to a situation where several properties and vital infrastructure are either under-insured or not insured at all. This exposure of vital tourism plant puts the sector at great risk and urgent steps need to be taken to address this.

The CARICOM Secretariat is working closely with the Caribbean Disaster Emergency Response Agency (CDEMA) on a comprehensive disaster management strategy that integrates the management of all natural and human induced hazards, including prevention, preparedness, mitigation, response, recovery and restoration. In addition, the recently established Caribbean Catastrophe Risk Insurance Facility under the coordination of the World Bank – to provide CARICOM member states with index-based insurance against government losses caused by natural disasters – is a welcome step in the right direction, but needs to be

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**Effects of climate change**

In the Working Group 11 report on Impacts and Adaptation, Chapter 16 is devoted to small islands. The report emphasises that small islands, whether located in the tropics or higher latitudes, have certain characteristics – such as limited size, proneness to natural hazards and external shocks – which make them especially vulnerable to the effects of climate change, sea level rise and extreme events. Sea level rise will exacerbate inundation, erosion and other coastal hazards, threatening vital infrastructure, settlements and facilities that are predominantly situated along the coast. Sea level rise will also impact negatively on coastal ecosystems such as coral reefs and mangrove forests, and commercial and artisanal fisheries which are based on those systems. We are already experiencing the adverse effects of some of these impacts.

- Elevated seawater temperatures have triggered widespread bleaching of coral reefs in the region and is believed to have contributed to the increased intensity of recent hurricanes.
- During the period 1970-2004 hurricanes have had a devastating effect on the Caribbean. Hurricane David hit Dominica in 1979 with winds exceeding 130mph, killing 42 people, damaging 95 per cent and destroying 12 per cent of buildings, destroying the country’s banana crop and 75 per cent of the forests. Similarly, hurricane Ivan wreaked havoc with the economy of Grenada with an estimated loss of 200 per cent of the country’s GDP. Nutmeg, Grenada’s most important agricultural crop, was devastated in a mere few hours by hurricane Ivan, and since the plant does not reach commercial production status under seven or eight years, Grenada will earn no foreign exchange from this source for almost a decade. Consequently, these countries’ Gross Domestic Product (GDP) declined, central government expenditures rose and fiscal deficit increased.
- The IMF has indicated that in the Eastern Caribbean the average annual damage from natural disasters over the 1970-2004 period was about 2.6 per cent of the GDP of those islands, compared to a worldwide average of 0.7 per cent.
- Recently Hurricane Dean made landfall on the Mexican coast North of Belize as a Category 5 hurricane. Although Belize did not suffer a direct hit from this storm it completely destroyed the country’s papaya crop inflicting damages to the extent of US$35 million to their export earnings. In addition to this there was widespread damage to housing with the consequent displacement of residents.
- With increasing frequency, countries in the region are facing situations in which scarce resources that were earmarked for development programmes have to be diverted to relief and reconstruction following disasters.
expanded and supplemented with other insurance instruments such as catastrophe bonds, parametric insurance and weather derivatives, to provide adequate protection to all levels of the regional population and especially for the poor and vulnerable sections of the community.

The Working Group report also emphasises the need for adaptation measures to be implemented in countries such as those in the region, but recognises that a lack of in-country adaptive capacity is a common constraint to adaptation and underlines the fact (also confirmed in the Stern report) that in most cases the costs of adapting and implementing adaptation options are prohibitive and will require financial resources that are generally not available to governments. The report recommends that to overcome this deficiency of human and financial resources, adaptive capacity in small states will need to be built up in four important areas: human resource development, institutional strengthening, research and systematic observation and public awareness and education. As pointed out later in this article, the CARICOM countries have for some time now embarked on bold moves to address capacity building in these key areas.

The Caribbean community response to climate change

Most of our efforts in the Caribbean, to date, have been directed at building national and regional capacity for adaptation to climate change. The region has been implementing a succession of projects: the Caribbean Planning for Adaptation to Climate Change (CPACC) project, the Mainstreaming of Adaptation to Climate Change (MACC) project, both funded by the Global Environment Facility (GEF) and the Adaptation to Climate Change in the Caribbean (ACCC) project which was funded by the Canadian International Development Agency (CIDA). All of these projects were designed to provide information on the future risks which the region will be exposed to as a result of climate change, the extent of the impacts of such risks on our human, institutional and socioeconomic systems, how these impacts could be reduced (adaptation), the costs of such actions and the eventual identification of the best options for implementation. Recently the region was successful in getting approval for another GEF funded project: the Special Project on Adaptation to Climate Change (SPACC). This project would advance the work in the region, in that it will support the identification and implementation of adaptation options in the three pilot countries of St Lucia, St Vincent and the Grenadines and Dominica. During the course of implementation of these projects capacity in several relevant areas for adaptation has been building up in the region. At the institutional level we have seen the establishment and functioning of a Regional Climate Change Center which became operational in January 2004.

The link between access and use of modern energy services and human development is very strong. The IPCC and the Stern reports have underscored the pivotal role of the energy sector in the transformation to a low carbon economy and the development process in emerging economies. Access and security of energy supply helps to promote better quality education, better quality health services, increased productivity, enhanced competitiveness and higher levels of economic growth. Many countries in the Caribbean Community are highly dependent on imported fossil fuels for energy supplies. In CARICOM these imports consume a significant percentage of foreign exchange earnings. In addition, the use of fossil fuels contributes directly to the degradation of the environment through pollution and increased emissions.

In the Caribbean Community, the potential to harness and develop renewable energy resources such as biomass, hydro, ocean, solar and wind, and for geothermal energy is vast. Some CARICOM member states have made innovative use of solar and wind power, agricultural by-products and hydro–power sources. In the area of renewable energy, several advances were made in 2006. The Caribbean Renewable Energy Development Programme (CREDP) financed by the GEF and executed by the CARICOM Secretariat, is a part of the Community’s Regional Energy Initiative, spearheaded the drafting of model National Energy Policy Frameworks in which there is a chapter on renewable energy for consideration by member states. In the area of renewable energy financing, the project has developed to address the high transaction costs and risk factors associated with the commercialisation of renewable energy, namely, the Caribbean Renewable Energy Technical Assistance Facility (CRETAF) which is now accepting applications for funding.

In addition, the CARICOM Secretariat has designed a Sustainable Energy Programme. This programme would address not only renewable energy, but also energy efficiency, energy conservation, biofuels, carbon finance, trade, development of an energy database for decision-making, and most importantly partnerships for resources mobilisation. The programme would also provide support for the implementation of the work of the CARICOM Task Force on Regional Energy Policy, as well as institutional support to CRETAF and CREF which will supersede CREDP after April 2008.

The CARICOM Task Force on Energy in 2006 prepared a Draft CARICOM Energy Policy which was presented to the Inter-Sessional Meeting of the Heads of Government in February 2007. Work continues on the policy document with a view to inclusion of a number of emerging issues. Further consideration of the Draft Policy will be facilitated at the Special Council for Trade and Economic Development (COTED) Meeting on Energy. The outcome of the Special COTED would be submitted to the Conference of Heads of Government which would among other things endorse the region’s approach to energy. However, actions on these initiatives are constrained by access to financial resources.

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Climate Change: the Challenge for Finance Ministers

Towards the future

The Kyoto Protocol, ratified in 2005, was the first global agreement to stipulate mandatory cuts of GHGs for developed countries. The protocol calls on countries which have ratified it to cut their GHG emissions by 5.8 per cent of their 1990 emissions and this between the years of 2008 and 2012. Even with the very modest requirement for compliance, the USA and Australia did not ratify the protocol. The global community is preparing to enter into negotiations for a successor treaty to Kyoto. Earlier this year the USA indicated that they would participate in the debate. China, India, Brazil and other large developing countries, with rapidly increasing GHG budgets, seem geared to agree to voluntary caps on their emissions. At the moment it does seem that a GHG emissions reduction regime that will result in about a 2°C rise in global temperatures will be agreed to. As a region, we need to be actively engaged in these negotiations. Our position should be defined by the fact that we are finding it increasingly difficult to cope with present day climate, much less with that in a world that is 2°C warmer. Moreover, whatever regime is agreed to we should also press for a significant increase of resources for adaptation. These should be the pillars of our strategy for the upcoming debate; aggressive mitigation by major polluters, with severe enforceable penalties for non-compliance and substantial funding to build adaptive capacity and to implement adaptation options, in developing countries, especially in the small island (developing) and low lying coastal states in the Caribbean.

At the same time the region should seize the opportunity, under the Kyoto Protocol, to continue to reform its energy sector, through the use of the Clean Development Mechanism (CDM), one of the enabling mechanisms under the protocol. Using the CDM the region can attract significant investments in activities in energy efficiency, renewable energy (solar, wind, geothermal), biomass (bagasse, rice husks, wood waste) landfill gas and biofuels. It is an opportunity, not only to green the region’s energy sector but, also, to provide for the more efficient production and use of energy and, ultimately, for our energy security. Ethanol, as a biofuel, offers promising prospects for the revival of the sugar cane industry in the region. Large producers like Cuba, Guyana, Belize and the Dominican Republic might target the ever expanding market for biofuels in the USA and Canada. Smaller producers can replace up to 20 per cent of their petrol consumption with ethanol in a blended fuel and save valuable foreign exchange, while providing local employment.

As we embark on global negotiations to agree on a post-Kyoto mitigation regime we in the Caribbean would expect developed countries to agree to an aggressive mitigation regime that would stabilise global greenhouse gas emissions at a level that will result in a less than 2°C rise in average global temperatures. To achieve this the recent G8 target of a reduction of 20 per cent by 2050 compared to 1990 levels, though commendable, offers no comfort for Caribbean states; the industrialised countries need to aspire to higher mitigation targets in that time period. Equally we expect all countries to be party to global mitigation initiatives and that countries with rapidly emerging economies will be supported to ensure that their development pathway is sustainable with a minimal carbon footprint. For Caribbean states, given the inevitability of climate change and its impacts on the region, adaptation is an imperative. One outcome of the ensuing negotiations must be a realisation of a significant increase in new resources available for adaptation.

Finally, the Commonwealth family of nations has a unique opportunity to take advantage of its diverse membership, reflecting every interest group in the climate change debate, to chart a course for an effective global response to the challenge we now face. The Commonwealth family with G8, Annex 1 and large developing countries, SIDS and LDCs among its membership, can take some bold collective measures to demonstrate to the rest of the world that, it is possible to forge new partnerships between all nations, rich and poor to meet the challenges of global climate change.

Edwin Wilberforce Carrington, a national of Trinidad and Tobago, is the current Secretary-General of the Caribbean Community. He has held that position since August 1992, making him the longest serving Secretary-General of the Caribbean Community. His distinguished career in Diplomacy and Development saw him serve as Deputy Secretary-General, and immediately thereafter, 1985-1990, as Secretary-General of the African, Caribbean and Pacific Group of States (ACP) – the only Caribbean national to have held that position to date. In acknowledgement of his outstanding service, Carrington Hall at the ACP Secretariat (Brussels) is named in his honour.

The objectives of the Caribbean Community (CARICOM), formerly the Caribbean Free Trade Association, are to improve standards of living and work; the full employment of labour and other factors of production; accelerated, coordinated and sustained economic development and convergence; expansion of trade and economic relations with third states; enhanced levels of international competitiveness; organisation for increased production and productivity; and achievement of a greater measure of economic leverage.

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Micro-finance initiatives successfully alleviate poverty...

Since its inception in 1983, the example of the Grameen Bank has been followed all over the world. Currently, thousands of micro-finance institutions (MFIs) – from Bangladesh to Bolivia and from Malawi to Bulgaria – provide small loans to over 60 million of the poorest people. As a result, many of these families have access to better nutrition and healthcare, and can send their children to school instead of being forced to use them as a source of labour.

Besides microcredit, other financial services are being rolled out by MFIs that can assist the poor in getting on the first rung on the ladder of development. A bank account and simple insurance products can help them reduce their exposure to theft, sickness, and death which are part of everyday life in many poor countries. For example, rainfall insurance for small-scale farmers has already proven its worth in India to cope with the consequences of drought or floods, and is being explored in Ethiopia, Malawi, Morocco, Nicaragua, Ukraine, and Peru.

...but only on a local scale

But more is needed. Despite its enormous success, the MFI industry currently reaches only a small fraction of the more than one billion of the poorest people on the planet and still struggles to become an economically viable, profit making operation. MFIs in Latin-America, Africa and the Middle-East are estimated to serve fewer than 10 per cent of the poor. Many donors still provide financial support to micro-finance institutions that are too small or poorly managed to survive otherwise.

This then raises the question: can the poor be better served through an expansion of the mainstream financial sector? Much evidence suggests it can.

The mainstream financial sector also reduces poverty...

A growing body of research and many real life examples show that the traditional financial sector can indeed substantially contribute to poverty reduction. Financial sector development has been shown to translate into significant economic growth and lower inequality, from which the poor also benefit. And besides providing the poor with credit and a bank account, the formal financial system offers payment services which make purchases and remittance flows – currently over US$125 billion – cheaper, easier, and safer. Again, the poor gain directly as exemplified by the price drop of transmitting US$100 from the US to Mexico from US$23 a few years ago to less than US$10 today.

Many case studies and more systematic research at the World Bank and elsewhere have also shown that access to financial services – most notably of private banks – is also associated with improvements in health, education, and gender equality, the main components of the Millennium Development Goals (MDGs), the eight development objectives supported by 189 nations. (For an overview, see: Claessens, Stijn and Erik Feijen (2006), Financial Development and the Millennium Development Goals, World Bank Working Paper 89, Washington, DC.)

However, although there has been substantial progress in several areas, overall the world did not perform well in terms of hunger, according to a recent report by the Food and Agriculture Organization. Since the early
1990s, there was only a reduction by three million in the number of hungry people, leaving more than 860 million malnourished people all over the world today.

Together, this suggests that, like microcredit, the financial sector at large can, as the Nobel committee has put it, create “economical and social development from below”.

...on a global scale

But how much does the financial sector matter for poverty and the other MDGs? The answer is – a lot! Using data from all over the world, studies show that increasing credit provided by private banks (as a percentage of gross domestic product) by one per cent reduces poverty and hunger rates by 0.22-2.45 per cent. Much of these gains in reducing poverty come through increases in agricultural productivity. Specifically, a better financial sector increases, for example, fertiliser use and the number of tractors per worker, resulting in increased crop and livestock production and general higher agricultural productivity.

In all, improving the financial sector translates into an impact on MDG-indicators equal to about 25 per cent of the impact of a higher gross domestic product per capita, a common measure of general economic welfare. This is an important comparison, since it is much cheaper to develop the financial sector than to improve general living standards: after all, financial sector development does not entail many real investments; rather, it mostly relies on a sound policy framework. Hence, focusing on the financial sector is not only effective, but also practical.

The path forward to a more inclusive financial sector

However, despite its great potential, many financial systems today do not provide sufficient access to financial services for the poor. A few measures stand out in how the poor can gain access to a broader variety of financial instruments and become part of the formal economy.

There are already signs of mainstreaming affordable microfinance services by commercial banks, as competitive forces, technology, and the use of existing networks motivate these banks to reach larger parts of the lower-income segments of the population. For example, under competitive pressure, the ICICI bank and the SHG Bank Linkage programme in India, and commercial banks in South Africa, have made it a priority to reach out to lower-income groups. Mobile technology has also already proved to be effective: banks in many developing and transition countries, including Bolivia, Brazil, China, and Ghana, have offered prepaid mobile phone cards that can facilitate payment services for low-income households. Often banks do not have the networks in place to reach the poor, but using the postal distribution network, four big retail banks in South Africa along with the post office’s Postbank, launched the Mzansi account, a low-cost bank account aimed at extending banking services to the black majority.

But still many systems provide too many obstacles for the poor to gain access to financial services and integrate the MFI industry. Hence, a large-scale breakthrough will require a proper regulatory financial infrastructure. Governments need to ensure that the poor and their possessions have sound legal status so they can open a bank account and can use the little assets they have as collateral for a loan; the Inter-American Development Bank shows that most property in Latin America cannot be used as collateral for lack of an effective legal framework. Moreover, an increase in transparency is needed, from credit registries to proper accounting standards, such that lenders have the information to make sound and objective decisions, instead of relying on irrelevant factors like gender or ethnicity.

In conclusion, financial sector development is an important tool for the development community eager to attain the MDGs. It will be hard work making progress towards an inclusive financial system which helps the poor to escape poverty, hunger and humiliation. But as Muhammad Yunus has shown us, it can be done.

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The mission of the World Bank is to help developing countries and their people reach the Millennium Development Goals by working with partners to alleviate poverty. To do that the Bank concentrates on building the climate for investment, jobs and sustainable growth, so that economies will grow, and by investing in and empowering poor people to participate in development.

The International Monetary Fund is an international organisation of 185 member countries. It was established to promote international monetary cooperation, exchange stability and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment.

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Although globalisation has been a key driver of the recent economic expansion that has benefited millions of people, these benefits have not been shared equitably either between or within countries. In many cases, particularly in Africa, globalisation has also served to intensify the income inequality gap. Although not a panacea, it is being increasingly realised that an inclusive financial system, one that ensures broad access to a wide range of financial services – from credit and savings to insurance and remittances – can help bridge this gap, leading to reduced poverty and sustained broad-based economic growth.

A rather high percentage of people have missed the globalisation train. And as the train picks up steam, the distance between those on the train and those left behind is increasing: in 1990, for example, the average American was 38 times richer than the average Tanzanian; today, the average American is over 60 times wealthier.

The lack of access to financial services by so many people worldwide illustrates this inequality. The vast majority of ‘bankable’ people in the world – more than three billion – still do not have access to affordable financial services. Only four per cent of the sub-Saharan African population have bank accounts, compared with the 18 per cent global average. Only one per cent of Africans has a loan or credit facility with a formal financing institution. These striking realities are illustrated in Table 1.

Obstacles to financial services
Several factors limit the access of poor and low-income people to formal financial services. From the demand side, personal and social factors such as location, education and income levels, occupation, cultural issues, gender status, and lack of legal identity have an effect on access. Furthermore, the attractiveness and availability of financial products influence and limit their choices. Finally, the inadequacy of financial infrastructure and weaknesses of financial sectors can also limit access.

Inclusiveness brings benefits
An inclusive financial sector is one that offers poor and low-income people access to a full range of financial services such as credit, savings, insurance, remittances, mortgages, and pensions. These services should be offered by a wide range of institutions, including commercial banks, non-bank financial institutions, credit unions, financial NGOs and others. Most of these institutions should also become an integral part of the

Table 1: Percentage of population with a bank account

<table>
<thead>
<tr>
<th>Country</th>
<th>%</th>
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<tbody>
<tr>
<td>Tanzania</td>
<td>6.4</td>
</tr>
<tr>
<td>Lesotho</td>
<td>17.9</td>
</tr>
<tr>
<td>Namibia</td>
<td>28.4</td>
</tr>
<tr>
<td>South Africa</td>
<td>31.7</td>
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<tr>
<td>Swaziland</td>
<td>35.3</td>
</tr>
<tr>
<td>Botswana</td>
<td>47.0</td>
</tr>
<tr>
<td>Europe</td>
<td>89.6</td>
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</tbody>
</table>

Financial Inclusion

formal financial system in order to mobilise the resources necessary for their long-term growth. Through broad access to financial services, a financial sector that is inclusive helps to promote both economic growth and equity.

A robust financial sector that offers a number of flexible financial products and services and is open to all members of a society is important to a country’s economic and human development. There are many reasons why a country should strive to make its financial sector more inclusive; this paper outlines three. Inclusive finance strengthens a country’s overall financial sector, promotes inclusive growth, and reaches a large, under-served segment of the population.

**Strengthening financial sector development**

Much too frequently, the provision of financial services for the poor has been treated exclusively as part of social policy, separate and distinct from the rest of the financial sector. However, extending financial services to the excluded is also important to strengthening a country’s overall financial sector development.

In particular, microfinance institutions (MFIs), when well managed, play an increasingly important role. To illustrate, MFIs such as Kenya’s Equity Bank and Bank Rakyat Indonesia (BRI) have been among the most profitable, even among the various commercial banks in their countries. In 1997, when Indonesia was hit by a severe financial and economic crisis and the entire banking system was on the brink of collapse, the microfinance arm of BRI (Unit Desai) weathered the crisis period remarkably well. In fact, the volume of deposits held by BRI’s Unit Desai increased – in 1998 alone, more than three million new deposits were opened. Thus the short- and long-term impact of institutions like BRI is considerable. On the one hand, MFIs provide the savings and credit services needed by poor customers to reduce their risk, manage uncertainty and build on economic opportunities. On the other hand, these institutions are also important because they help poor clients to develop important financial literacy skills.

**Promoting inclusive growth**

Empirical evidence suggests that a well-developed financial system reduces inequality in the long term. Indeed, a lack of access to finance is often found to generate persistent inequality and slow down growth. Despite this, much remains to be learned about exactly how financial development impacts economic growth. But there is no question that increased access to finance helps the poor to better manage the risks they face, cope with external shocks and take advantage of economic opportunities. These are important factors that can help set up the foundations for inclusive growth.
Financial Inclusion

Providing financial services to small and entrepreneurial firms may also be an effective way to strengthen developing economies and to help them converge towards the high income levels of advanced economies. Furthermore, financing opportunities for the excluded non-poor in particular regions or among certain ethnic groups can assist in improving the functioning of labour and product markets and the efficiency of investment, leading to better employment opportunities for the poor in these regions.

Because finance is pro-growth as well as pro-poor, access to finance plays an important role in reducing income inequality and poverty. Thus, financial sector reforms that promote broader access to financial services should be at the core of the global development agenda.

Reaching the ‘bottom of the pyramid’ (BOP)

A large segment of the world’s population (almost four billion people) lives on under US$2 a day. In Africa, the problem of poverty is particularly severe: from 1990 to 2004, 71 million additional people joined the group living under $1 a day, making this segment of the population almost 50 per cent of the total. For people living in such extreme circumstances, gaining access to financial products and services can directly provide the tools to protect, diversify and increase their sources of income, thereby expanding economic choices and opportunities, and facilitating a move out of poverty.

The effects of improved access to financial services for the BOP can be observed in many ways, including generating new jobs and income, establishing a formal identity for people, providing education for children, enabling them to access timelier healthcare, and empowering women.

However, reaching this group with appropriate financial products and services is not just a question of moral imperative or philanthropy. It is also about co-creating a market around the needs of the poor through public-private-community partnerships (PPCPs) and promoting an economic system characterised by inclusive capitalism which respects its BOP consumers as individuals. PPCPs are increasingly growing in popularity because of their ability to combine the best elements of the private and public sectors to provide new forms of service delivery to the poor. Furthermore, because of new developments in information and communication technology (ICT), it is now considerably less costly and easier to reach the poor on a sustainable basis. New technologies have lowered transaction costs and helped to overcome traditional barriers to access, such as geographic isolation. Examples of innovations in technology that have made it easier to reach the poor include the use of mobile phones to provide banking (e.g. WIZZIT in South Africa, M-PESA partnerships with Vodafone, Faulu–Kenya and CBA in Kenya) and the use of ATMs and point-of-sale networks that increase financial institution outreach without the costs of opening an expensive branch network (e.g. Uganda Microfinance Ltd).

Serving the BOP market clearly requires a good understanding of this clientele and the formulation of new and creative approaches to meet their constraints and needs. Such an approach will offer the BOP segment products and services at an affordable price, while also (and perhaps more importantly) providing them with recognition, respect, fair treatment, and self-esteem.

Challenges to building inclusive financial sectors in Africa

Despite positive developments in the area of financial inclusion during the past few years, as outlined above, many poor and low-income people and micro and small enterprises, particularly in Africa, still lack access to a broad range of financial products and services on a sustainable basis. Africa is facing a number of particularly acute challenges: low population density and weak communication infrastructure that increase transaction costs and make access more difficult; overall weak institutional capacity and scarce trained human resources; and lack of access to domestic sources of capital, despite the high liquidity of the banking sector overall.
However, impressive developments have occurred in the continent that could pave the way for building inclusive financial sectors. For example, the recently amended legislation covering the West Africa Monetary Union (UEMOA) facilitates the role that non-financial cooperative institutions can play in providing financial services to the poor. In addition, some of the fastest growing MFIs are from Africa, as is the case of Equity Bank in Kenya, which added an average of more than 1,200 new customers everyday in 2006 and has developed an impressive mobile banking model to increase its outreach in rural areas. Innovative application of ICT using the internet and cell phones are also revolutionising access to financial services, including remittances, throughout the continent. These developments are compelling governments and policy makers to re-define their role and adapt the regulatory and legislative environments to encourage the emergence of inclusive financial sectors.

While the role of governments in creating an enabling environment for greater access to financial services is important, it is equally critical to recognise the key role of the private sector. Therefore, efforts need to be developed to ensure that the private sector in Africa (particularly private financial institutions) is actively engaged in the process of building inclusive financial sectors across the continent. The private sector, for example, can contribute to the development of financial services infrastructure, innovations in delivery mechanisms and product design using technology and other methods to increase efficiency and lower costs, and improve human and institutional capabilities.

Furthermore, access to capital for lending and improving management and information systems in Africa is a key area where the private sector can make important and substantive contributions. In particular, the private sector’s links with international markets will form an important part of building inclusive financial sectors.

Although there is progress on many fronts, many challenges remain in building truly inclusive financial sectors in Africa. These include:

- Creating a clear vision and commitment by policymakers to promote inclusive financial sectors as part of their development agenda
- Establishing enabling policy, legal, and regulatory environments to facilitate access
- Supporting the growth of strong institutions that provide a broad range of financial services at a reasonable cost to serve large numbers of people on a sustainable basis
- Ensuring more active involvement of the private sector
- Strengthening local financial markets and facilitating access to those markets by strong MFIs, as a means to support their growth in the long-term.

While these challenges may seem daunting, many governments and people in Africa are also recognising the importance of access to financial services as a critical tool in the struggle to overcome poverty, and are working diligently to assure such access. As a result, the future looks brighter than ever.

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The UN Capital Development Fund offers a unique combination of investment capital, capacity building and technical advisory services to promote the achievement of the Millennium Development Goals in the least developed countries. Its two practice areas are Inclusive Finance and Local Development. UNCDF currently works in 33 of the 50 LDCs with a total programme portfolio of approximately US$130 million. The organisation hosts the UN Advisors Group on Inclusive Financial Sectors.

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A Nigerian client of the Lift Above Poverty Organization (LAPO – an MFI) started a business buying and reselling fish in the neighbourhood with a small loan that she received. Photo: Adam Rogers, UNCDF.

Access to capital for lending and improving management and information systems in Africa is a key area where the private sector can make important and substantive contributions.
Policy level response to financial exclusion in developed economies: lessons for developing countries

Prof Elaine Kempson
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There is growing concern about access to financial services, stimulated mainly by debates around social inclusion and the profitability (and hence social responsibility) of banks. The situation in a developing economy – where half or more of the population uses no financial services – is clearly different from that in a country such as the UK, Australia or Canada, where only a minority of the population is in that position. Yet, perversely, the problem is most acute when only a minority of people lack access, since the opportunities for operating a cash budget are limited and the costs of doing so high. A key question is, therefore, how can developing countries build inclusive financial services that avoid the acute problems of financial exclusion experienced in countries with highly developed economies?

What do we mean by financial exclusion? The most commonly accepted definition is the lack of access to, or the inability to use, financial services to manage money day-to-day. It includes people who lack access – to a bank account where they can safely store money until it is needed; to transaction banking services, allowing them to make and receive payments other than in cash; and to affordable credit, to smooth the effects of a variable income or to meet a major expenditure they could not otherwise afford.

Experience shows that where there are considerable numbers of financially excluded people, high-cost or illegal moneylenders, cheque cashers and remittance agents tend to fill the void. Concern is mounting about the very high charges paid by unbanked consumers who use such fringe banking services.

The causes of financial exclusion

There is no single cause of financial exclusion; rather, three sets of factors play a role: macroeconomic/societal, supply and demand.

The proportions of people affected by financial exclusion tend to reflect:

- GDP per capita
- Levels of income inequality
- The make-up of the banking sector, and
- The extent to which wages (where they exist), welfare payments and pensions are paid directly into an account and not in cash.

The extent to which individual countries have had political initiatives to combat financial exclusion also plays a part.

Countries with high levels of GDP and/or low levels of income inequality as measured by Gini coefficients for equivalent disposable income (income after taxes and taking account of the size of the household) tend to have lower levels of financial exclusion. Inclusion also tends to be higher in countries where local savings banks and/or the post office are important players in the provision of banking services.
On the supply side, there is a range of barriers to access and use of financial services, including:

- Lack of geographical access
- Risk assessment techniques
- Identity checking requirements
- Price
- Inappropriate product design (including terms and conditions)
- Methods of service delivery
- Complexity of choice and lack of marketing to some segments of the population.

But it would be wrong to assume that financial exclusion arises entirely through a failure of supply. There are important demand constraints too. These include a belief that financial services are not intended for people on a low income; and a mistrust of banks. Consequently many people express a preference for using alternative financial providers even if they are very costly or insecure – local moneylenders or remittance agents for example. Linked to this are cultural and religious barriers to the use of mainstream financial services. Then there are factors that relate to the design of the financial products on offer, including fears about the (possibly hidden) costs and concerns about losing financial control. Operating in cash is seen as providing complete control.

From this it is clear that financial exclusion arises through a complex interaction of factors. Low GDP per capita means more people are on low incomes and are less attractive as customers for the commercial banks, who do not design products that meet their needs. This reinforces a belief that financial services are not appropriate to people on low incomes, and a preference for relying on cash and alternative providers. In this context, it is clearly important to build financial services that are inclusive – learning from experiences of countries with a large sector (such as the savings banks) that aims to meet the needs of people regardless of their income.

It is also important to note that many people who are financially excluded have used financial services in the past. Some disengage through choice – often because their incomes have fallen; some have had access withdrawn – perhaps as a result of financial difficulties or a drop in income; some are left without access following relationship breakdown and cannot gain access in their own name; while others find that continued use is prevented by changes in the way services are delivered, such as bank branch closures or widespread use of internet banking.

Tackling the problem

As we have seen, levels of banking inclusion inevitably rise in response to both increasing prosperity and declining income inequalities. There are, however, a number of supply and demand barriers that can stand in the way of achieving financial inclusion. There are a number of important lessons that can be learnt from the experiences of countries like Canada, South Africa and the UK that have tried to tackle financial exclusion.

Who is affected by financial exclusion?

Regardless of the levels of financial exclusion in a country, it seems to be the same groups of people who are affected. Exclusion tends to be concentrated among people on the lowest incomes, and the smaller the proportion of people affected the more concentrated it is among the very poorest. So, people not in employment, for whatever reason, are most acutely affected. People who work in the informal economy likewise have high levels of financial exclusion.

In countries where financial exclusion is high, people living in rural areas seem to be particularly affected, regardless of their income. This effect disappears, however, as levels of financial exclusion fall. But where levels are low, financial exclusion tends to occur in discrete pockets, where service provision is low and disaffection high.

Young people and the elderly experience the highest levels of financial exclusion, but for different reasons. Many young adults delay engaging with financial services until their income rises and/or they achieve economic independence from their parents. In contrast, older people who are financially excluded tend to come from a generation that has little or no experience of using financial services. Older people are particularly affected in countries where levels of financial exclusion are high – as are women.

People from cultural and religious minorities often face high levels of exclusion – this is particularly acute for Muslim minorities who frequently lack access to financial services that are compliant with Shariah law.

There is a need for low-cost no-frills bank accounts

The increase in the breadth and complexity of financial services in highly-banked countries has undoubtedly contributed to exclusion. Simple products, on the other hand, help ensure access to people whose needs tend to be more basic. Many developed countries have needed to reinvent simple bank accounts to achieve banking inclusion. Such accounts, typically, offer full access to transaction banking services but do not have an overdraft facility and have addressed both terms and conditions and charging structures that act as barriers to use by people on low incomes. These include:

- Requiring a minimum balance to open an account and/or a minimum number of transactions to keep it open – simple ‘no frills’ accounts generally do not have these restrictions
- Fees for failing to maintain a minimum balance and monthly lump sum fees regardless of levels of use, which impact hardest on people with low incomes or who only need to make a small number of transactions – simple accounts typically relate charges solely to levels of use
- Credit scoring applications for current accounts with an overdraft facility – simple accounts have no overdraft facility so do not need to be scored. In any case, the evidence shows that people on low incomes prefer an account that cannot be overdrawn inadvertently as this gives them greater financial control.

Developments in technology offer solutions and risks

Technological advances have made it cheaper for banks to conduct business electronically. In many highly-banked countries, however, this has tended to reinforce
financial exclusion as poor people’s needs are often not considered – leaving them reliant on services that are costly to provide and are, therefore, either in decline or attract additional fees.

Arguably one of the most important developments is real-time banking, which can be used to prevent unauthorised (and often unintended) overdrawing and allows customers to be in full control of their account. With this facility credit checks become less important and paper-based transactions can be replaced with ones using plastic cards and electronic funds transfer. Some countries have created a banking infrastructure that utilises real-time banking for all accounts. Others, such as the UK, have done so for basic bank accounts only; but because many retailers lack the equipment needed to check accounts online in real time, this has tended to restrict access.

At the same time, it is important that technological developments do not create new forms of exclusion. There is a real danger of this happening in countries (such as Sweden) where internet banking is fast becoming the norm. It is equally clear that the development of credit cards has reduced access to low-value cash loans, which are more costly to provide.

There is a need to encourage the use of financial services

Lack of demand for financial services is as great a problem as the failure of supply and also needs to be addressed. Financial institutions are often seen as being predominantly interested in meeting the needs of the better off, and consequently people on low incomes are reluctant to use them. Experience shows that there is a need to promote the use of banking services as well as increase access to them. But weaning people from alternative financial providers will not be easy – especially where their services better meet their needs – albeit at a price.

Not-for-profit organisations can have an important role to play

Levels of financial exclusion tend to be lower where not-for-profit organisations, including non-governmental organisations (NGOs), savings banks or post offices, play a role in delivering financial services. This is largely because poor people see them as more user-friendly; but often they offer a more local service than commercial banks. Some, such as savings banks and some microcredit organisations, offer their banking, savings and borrowing services direct to the public. Increasingly, though, such services are offered by not-for-profit organisations working in partnerships with commercial banks. It is, however, important that such organisations are fully integrated into the systems for electronic transfer of funds used by banks. Without this, people using the services they offer will remain on the margins of the banking system.

Achieving universal access to financial services

In an ideal world, competitive pressures would ensure that the banking needs of all people are met. Experience shows, however, that some form of intervention may be needed to ensure universal access to banking.

Least successful is legislation alone. Conferring a right to a bank account, without ensuring that appropriate accounts are available, will at best lead to many people who are marginally banked. Usury laws may protect people on low incomes from high rates of interest but, in doing so, deny them access to loans from a reputable lender.

Instead, most countries have relied on pressure being applied to banks to recognise their corporate social responsibility and provide access to financial services to all through the development of appropriate products and, where suitable working in partnership with others to ensure appropriate and accessible delivery. This is often achieved through voluntary agreement and experience suggests that careful and independent monitoring of compliance is more important than whether self-regulation or legislation has been used.

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Bristol University’s Personal Finance Research Centre (PFRC) has gained an international reputation for high-quality policy-focused research. Its work focuses on financial exclusion and inclusion, credit use, over-indebtedness, financial capability, financial decision-making, money management and savings. The centre carries out research for government departments, trade associations, regulatory bodies, charities and others. PFRC’s work has been influential in shaping policy, and several staff act as technical and policy advisors to government departments and others.

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How microfinance can work for the poor: integration with education and health services

In the past few years, microfinance has been widely heralded as a successful contributor to the alleviation of poverty and a valuable tool for achieving the Millennium Development Goals (MDGs). And with good reason: scores of studies have shown the positive impact that microfinance can have on the lives of poor people. A 2005 World Bank study of three microfinance institutions (MFIs) in Bangladesh, for example, found that 40 per cent of the entire reduction of rural poverty over 14 years was directly attributable to microfinance. But microfinance alone is not enough; the poor need access to a coordinated combination of microfinance and other development services to increase income, build assets and improve health, nutrition, family planning, education, social support networks and more. The authors discuss the steps to achieving this integrated service.

Microfinance provides people with access to credit and other financial services to start and grow businesses, build productive assets, and better cope with financial shocks – at interest rates typically well below those charged by traditional moneylenders. Moreover, microfinance institutions strive to serve those most in need. Of the more than 113 million microfinance clients around the world, it is estimated by the Microcredit Summit Campaign that about 84 per cent are women and about 72 per cent are ‘very poor’ (in the bottom half of those living below their country’s poverty line, or below US$1 a day).

While access to financial services is undeniably powerful, credit and savings products address only one factor of many constraining the poor – a lack of liquidity. Increasing income and assets alone is a slow and insufficient strategy for combating serious issues such as childhood malnutrition, avoidable maternal and neonatal mortality, the spread of HIV/AIDS and suffering due to preventable illness such as diarrhoea and malaria. What is needed is the coordination of microfinance with other vital assistance for the community. The integration of complementary services intended for the same population can lead to enhanced operational efficiencies and synergies of benefits. The question is how to develop a scaleable strategy for delivering integrated microfinance and other services that meet the multifaceted needs of poor people.

New era of integrated development services

At the halfway point on the MDG timeline, overall progress has been disappointing. Achievement of the goals by 2015 will call for new and innovative ways of working rather than ‘more of the same’. A strategic, overarching strategy to address poor people’s interrelated needs through creative partnerships that build on the best of different development sectors has the potential to lead to exponential rather than incremental reduction of poverty in the developing world.

Ideally, the 3,000+ existing microfinance institutions worldwide could provide an infrastructure or platform for reaching the poor through a coordinated combination of services. MFIs recognise the need, hear the demand and have a vested interest in cultivating a healthy, successful clientele with strong microenterprises.

Poverty and ill health

Poverty and ill health are intertwined and, as such, must be addressed in tandem. In the 2002 World Bank study Dying for Change, illness was the most commonly cited reason for “a downward slide into poverty…” ahead of losing a job, which took second place. The poor are more likely to be exposed to health risks because their work is physically demanding and often dangerous. But they are least likely to be able to afford healthcare when they are injured or fall ill.”

Dr Christopher Dunford, with Sheila Leahterman, Myka Reinsch Sinclair, Marcia Metcalfe, Bobbi Gray and Ellen Vor der Bruegge
Freedom from Hunger
Yet people often have no choice but to spend what little they have when injury or illness strikes. In a study conducted in Kenya, it was found that households in the bottom 20 per cent of the socioeconomic scale spent more than 10 per cent of their total expenditures on acute illnesses and that about 30 per cent of households faced ‘potentially catastrophic cost burdens’ as a result of illness. In research conducted by Freedom from Hunger in Bénin and Burkina Faso in 2006, it was found that poor microfinance clients spent an average of 30 per cent of their annual income to combat malaria alone. And according to another study in Thailand, 35 per cent of households experiencing an AIDS-related death “felt a serious impact on agricultural production, leading to a 48 per cent reduction in family income”. Ill health leads to lost productivity, which leads in turn to reduced earnings with which to prevent and treat illness. Neither improved financial stability alone, nor better access to health education, products and services alone, can solve the problem. The inextricable link between poverty and ill health makes a multisectoral solution paramount.

**Microfinance as a development platform**

While microfinance is not a development panacea, it offers a robust platform for the delivery of complementary services that are needed – and frequently requested – by poor people. MFIs serve millions of poor people, especially women, on a regular basis, often extending their services to isolated, hard-to-reach places. What is more, the microfinance sector is focused on market-based business principles and financial self-sufficiency – providing demanded services at a price that is affordable to clients but also covers the institution’s operational costs. MFI clients repay their loans at astonishingly high rates and their loyalty to trust in the institution tend to be very strong.

Many MFIs provide financial services to groups of clients who mutually guarantee each other’s loans. These groups meet frequently to make loan repayments and deposit savings with the guidance of MFI field staff. Such regular meetings offer excellent opportunities for the provision of add-on services, such as training in health or financial management. This combination of a vast and rapidly growing network of distribution to hard-to-reach, loyal, economically active groups of poor people, a steady revenue flow from interest earnings and the drive to develop market-based products that pay for themselves, makes microfinance an attractive core component of a development programme that draws on the principles of self-help to alleviate poverty.

**Multifaceted and sustainable solutions to poverty alleviation**

Recognising the vicious cycle of poverty and ill health, and witnessing its impact on clients’ ability to repay, flourish, build assets and pull themselves out of poverty, some microfinance institutions have added nonfinancial services, such as dialogue-based education and linkages to health products and providers, to impressive effect. Figure 1 shows a range of health-related needs, as expressed by poor women in developing countries, and the complementary products and services that MFIs can offer in response, alongside microfinance services. This provides an example of a cohesive, integrated approach that uses microfinance as a platform for providing an array of complementary services that enable poor

![Image](attachment://figure1.png)
women and their families to lift themselves out of poverty and improve their health.

**Health education**

Equipped with more income and decision-making authority, microfinance clients have choices – often for the first time in their lives. As a result, coupling microfinance with behaviour-change education can be especially powerful. Many MFIs are offering training in topics such as the prevention and treatment of diarrhoea, malaria and HIV/AIDS; breastfeeding; rational use of local health services; as well as self-esteem, microenterprise management and financial planning.

The combination of greater knowledge of sound health practices and the increased income to act on that knowledge leads to dynamic, positive change.

Considerable evidence of impact has been documented for integrated microfinance and education, or ‘Credit with Education’ programmes. Rigorous studies conducted in Ghana and Bolivia showed significantly improved health and nutrition practices by mothers who attended regular meetings where microfinance transactions and health education were provided by the same field agent. Participating mothers were more likely to breastfeed their children and delay the introduction of other foods until after six months. They were also more likely to properly rehydrate children who had diarrhoea by giving them oral rehydration solution. These changes in nutrition and health protection practices were manifest in outcome measures such as increases in height-for-age and weight-for-age for children of participants. Notably, a study of Credit with Education clients in Uganda showed that 32 per cent of clients had tried at least one HIV/AIDS prevention practice, compared to 18 per cent of non-clients.

**Health financing and insurance**

Having more income and increased knowledge of sound health practices can only go so far. Unexpected health expenses can still wipe out a family’s savings and force an MFI client to sell their productive assets. So, in recognition of client demand to protect against health-related financial shocks and the MFI’s own interest in protecting its portfolio from illness-induced defaults, some organisations – such as Réseau des Caisses Populaires in Burkina Faso – are going beyond Credit with Education to deliver health financing mechanisms, such as dedicated health savings accounts and emergency health loans.

Health microinsurance takes this solution a step further. In Rwanda and the Philippines, enrolment in microinsurance programmes is becoming easier, thanks to the availability of loans from MFIs to spread annual premium payments over time. According to a World Bank report, linkages between MFIs and health microinsurance schemes in Rwanda have increased opportunities for scheme members to access credit for income-generating activities.

Although these health financing products look promising and align well with MFIs’ core competences, they do call for new expertise on analysing health-seeking behaviour, needs and costs, and designing efficient management mechanisms to prevent fraud, among others. The tremendous need and technical complexity associated with health microinsurance make this a particularly crucial area for additional investment and experimentation to devise templates for programmes that could be widely adopted and adapted.

**Links to health care providers**

If good local health care is not available, then a microfinance client’s increased earnings, good preventive health practices and health financing products will only go so far. Distance, quality and affordability can be major barriers to timely health care – particularly in rural areas, where providers are sparse, transport is difficult, and public services are not well funded. Rather than develop expertise in health care, MFIs can leverage their local influence and business acumen to create reliable linkages with providers, negotiate rates, and advocate better quality and accessibility of health care.

The largest MFI in the Philippines, CARD, has negotiated exclusive discounts for its clients with private providers in rural areas to increase access to more affordable primary care. The Bolivian MFI, CRECER, contracts with doctors who travel to isolated areas to conduct ‘health days’ during which general check-ups, blood-pressure testing, Pap smears and other essential services are offered en masse. In Cambodia, the MFI-run GRET-SKY health insurance project uses its leverage to improve the quality of care in public facilities and helps channel poor people away from inappropriate and expensive care delivered by private (often traditional) providers and towards local public health centres. Such provider linkages also help to leverage and sustain local medical services, thereby leading to broader community development outcomes.

**Access to health products**

A package of services to address the poverty and ill health of very poor people is incomplete without access to crucial health products. Increased financial resources and knowledge about preventive health measures cannot help microfinance clients avoid malaria when insecticide-treated bednets are not sold in their community, prevent
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Bobbi Gray is Research and Evaluation Specialist at Freedom from Hunger, responsible for designing and directing impact evaluations of the organization’s innovations. Bobbi’s work has helped establish the positive impact of integrated microfinance and health education services on clients’ food-security levels in numerous countries around the world.

Founded in 1946, Freedom from Hunger brings innovative and sustainable self-help solutions to the fight against chronic hunger and poverty. For nearly 20 years, the California-based organisation has been training local partner organisations throughout West Africa, Asia and Latin America in the Credit with Education methodology, which continues to be regarded as a major innovation in the field of microfinance for its self-sustaining combination of financial and practical training services. Success with this programme has led Freedom from Hunger to develop other innovations that combine microfinance with education and health to achieve lasting food security.

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Conclusions
A careful analysis of the local service gaps, consumer demands, institutional capabilities and business incentives leads to the development of a package of context-specific, cohesive, interrelated services that can be provided directly by MFIs, or through strategic partnerships with other public or private organisations. The integrated package of microfinance and nonfinancial services does not need to be costly or unduly complex; for example, in Credit with Education, the addition of dialogue-based education to the village-banking type of microfinance service costs the MFI only about 6–10 per cent more than without education, and benefits the MFI through increased client retention.

Evidence now supports the integration of microfinance with nonfinancial services as an approach that has potential for enormous contribution to the achievement of the Millennium Development Goals. However, high-level support is needed to extend integrated services at a large enough scale to achieve outcomes on national and global levels. Promotion of integrated approaches via leadership briefings, statements of national policy and advocacy through individual country development agencies would signal the importance of applying this approach more widely. Governments and development agencies can expedite achievement of the Millennium Development Goals by supporting the integration of poverty-focused microfinance and non-financial services.

HIV if condoms are not available, protect children from diarrhoea when treatment tablets for contaminated water cannot be found, or buy the prescribed antibiotics when the supply is outdated, the quality of medicines sub-optimal or the prices exorbitant.

In response to such needs, BRAC in Bangladesh uses a network of health workers to sell essential but scarce health products door-to-door, and the fast-growing Indian MFI, Bandhan, is experimenting with a similar model. Some West African credit union networks have purchased insecticide-treated bednets and sold them at group meetings. The Bénin MFI, PADME, is developing a partnership with Population Services International to ensure that essential health products are distributed to shops in target communities and encourages its clients with suitable shops to offer such products.

Bobbi’s work has helped establish the positive impact of integrated microfinance and health education services on clients’ food-security levels in numerous countries around the world.

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Financial Inclusion

Helping youths make the most of money

Financial inclusion’ is the term used for extending banking services to those who are outside the formal banking channels and who cannot access mainstream financial products. Exclusion imposes higher costs on individuals who need to be educated about making sound financial decisions. Today more and more governments have recognised the economic benefits of promoting financial inclusion and have initiated programmes aimed at addressing this need. Programmes in financial inclusion generally focus on microfinance, financial literacy and banking the unbanked. This paper focuses on the role of financial literacy among younger citizens.

While financial institutions occasionally educate citizens about various financial terms and products, they have a vested interest in promoting their own products and services and this may cause individuals to question the credibility of the information being provided. It is therefore advisable that a financial education programme be led by an organisation with a non-profit interest, such as a regulator, government, or non-governmental organisation. Such a programme should have clearly identified objectives; identify target groups; develop strategies for the delivery of core modules; and identify costs of delivery and partners for financing.

To be effective, the programme must be conducted over the medium to long term and should employ a variety of techniques aimed at improving individual's knowledge of financial concepts. Whatever the approach, there is a need for a strongly interactive format. The ultimate objective is to help develop financially capable citizens who can differentiate among products and services and make decisions that are better suited to their needs. A dedicated budget is needed and it is for this reason that such a programme requires the collaboration of governments, regulators and the private sector.

It is first important to assess individuals' knowledge of their financial environment and determine the issues that limit their ability to utilise financial services effectively. The problems they face may arise from real barriers inherent in the operations of the financial institutions themselves or psychological barriers arising from lack of information and guidance. Financial literacy seeks to address the latter.

Training programmes should seek to assist children to develop good savings habits from as early as possible. However, it is sometimes recommended that priority be placed on youths who are on the threshold of adulthood and who are about to embark on the more independent university or work-life. Information provided may be more readily utilised and take deeper root when implemented in a shorter time frame. Programmes should educate young people on the different types of financial products and services available on the financial markets and should help identify the benefits and drawbacks. Training modules generally address the need to budget and save; the pitfalls of excessive credit; the benefits of investing; and retirement and pension planning. Business planning may also be appropriate.

The Commonwealth pilot programme

The Commonwealth Secretariat, in collaboration with the Central Bank of Trinidad and Tobago, implemented a financial literacy pilot training (‘the TT programme’) among youths between the ages of thirteen and seventeen in five different districts of Trinidad and Tobago. They were taught concepts related to savings,
investment, credit and budgeting and took part in various hands-on activities and games to reinforce the basic principles taught. The programme generated strong interest among those who participated.

At the beginning of the training session, a simple test was administered to determine the participants’ knowledge of ten given financial terms. They were asked to provide an explanation of the following in their own words: credit, insurance, interest, dividends, risk, investment, deposit, withdraw, budget, and shares. There was strong belief at the outset that the target group was knowledgeable about these basic financial concepts. At the conclusion of the meeting the test was re-administered and the participants were asked to redefine the same ten financial terms. Table 1 provides a summary of the completed answers.

The table indicates that there was a significant improvement in the participants’ understanding of financial terms. Before the programme only four per cent of the youths were able to correctly explain nine or all ten questions. Immediately following the lectures and activities, 46 per cent were able to do so. Where only 42 per cent provided correct explanations to six or more of the questions prior to the programme; more than twice this amount (94 per cent) were able to do so following the programme. Moreover, those able to describe just two or less of the terms fell from 10 per cent to just one per cent.

The data indicate that despite expectations, a significant number of youths may be aware of financial terms but may lack in-depth understanding of the meanings. It is therefore evident that financial literacy programmes help enhance knowledge, at least in the short term.

### The importance of simple and clear literature

A financial education programme is aided by the provision of financial literature written in clear and concise language. In Canada, policymakers recognised that most financial literature was written above the literacy level of 42 per cent of its population. They sought to issue financial literature in plain, simple, direct language and encouraged financial institutions to do the same. Clearer understanding of financial literature, would place citizens in a better position to select financial products more suited to their needs. The UK has also developed extensive material for citizens and youths on finance. Resources such as those compiled by the Personal Finance Education Group (PFEG) serve as useful background tools and provide a wide range of concepts, worksheets and activities for children in both primary and secondary school.

Countries with less mature financial systems may need to develop literature that is more suited to their own environment and culture. For the TT programme, the Secretariat adapted some of the material available from PFEG to produce a booklet on *Making the Most of Your Money*. The booklet presented information, worksheets and games on a range of financial terminology and practices.

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### Breaking misconceptions

The young people in the TT programme also filled in a brief questionnaire to determine their savings and spending habits. Some of the survey questions tested their knowledge of traditional home-based savings schemes and sought to determine whether there was a preference for these schemes over saving with a financial institution.

An analysis of the findings indicates that a small minority already express distrust about financial institutions; while a large proportion showed ignorance about the benefits of banking.

Almost three-quarters of the participants were aware of informal methods of savings such as ‘sou-sou’. A sou-sou is a community or workplace-based type of savings scheme outside of a formal financial institution. Members agree to contribute an agreed sum on a weekly or monthly basis; all of which is passed on to participating members in turn. No interest is gained and the person may receive an amount marginally less than that which was saved, if a management fee is deducted. When surveyed, 45 per cent of the students who were familiar with a sou-sou felt that this method was better than saving in a bank. They believed that a sou-sou facilitated easier savings; saved time and money; prevented individuals from making withdrawals as they wished; and allowed easy access to a pool of money. A small minority felt that a sou-sou was better because banks could not be trusted, stole or deducted money from your savings or charged money for making late payments.

When the students were exposed to the concept of accumulation of interest on savings, they recognised that while a sou-sou may be useful to encourage discipline in savings, it was necessary to save where money could earn interest. Teachings on compound interest also helped reinforced how money could grow. Many of the young people voluntarily expressed an intention to save more at a financial institution.

Policymakers must therefore develop strategies which improve the financial capabilities of citizens. It is also important to bring individuals into the formal banking sector and provide information on how they can access financial services. Research indicates that those who lack access to financial services include, among others, low income earners, the unemployed, youths at risk and individuals with low basic numeracy or literacy skills. While these individuals may deliberately exclude themselves from the formal financial sector, financial institutions and policymakers have often not done

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Financial Inclusion

Do youths save effectively?

The TT programme was aimed at more rural communities and targeted young people from lower to lower middle income families. The survey conducted revealed that 91 per cent of the youths received regular money allowances from parents and carer. While two-thirds indicated that they received financial advice from an adult on how to manage money, there was strong evidence of the need to implement better budgeting and management of savings. Less than half of the students surveyed knew the total amount of funds they received in one month and 24 per cent felt that they were spending too much on unnecessary items. A review of the spending patterns of the group revealed that recreation and consumer items made up a large majority of discretionary spending. In general the participants spent on clothing, snacks, adding minutes to cellular phones, rental of DVDs and socialising with friends. During activities which encouraged the creation of budgets and allocation of incomes to everyday needs, the students soon began making hypothetical choices which facilitated savings. These choices included taking buses to work rather than taxis, packing lunches rather than eating in restaurants and purchasing reasonably priced clothing rather than opting for famous brand names and the most recent fashion. The poorer the individual in the example employed, the more rigid were the budgeting techniques employed.

With respect to savings, there was strong evidence that students were aware of the need to save and did make some attempt to do so. Of the youths surveyed, 87 per cent indicated that they had some form of regular savings, and in some cases savings were said to be as high as US$30 a month. Whether savings were put to productive use or maintained over long periods was questionable, as 49 per cent of the youths indicated that they saved at home rather than with a financial institution. When asked for a reason why they did not save at a financial institution, a quarter indicated that they had never thought of opening a savings account, one-fifth indicated that they did not have enough money to open an account; and 10 per cent either did not know how to open an account or were afraid of going to the banks. For youths from the rural areas, the main reason provided was the difficulty of obtaining transport to and from financial institutions. Even among youths that saved, 27 per cent found it difficult to deposit money and 57 per cent indicated that an adult saved on their behalf.

Conclusions and lessons to draw upon

The data reveal that in Trinidad and Tobago youths have access to resources that are not being channelled into effective savings. This was evidenced by the large proportion of young people who were willing to save but failed to utilise a financial institution to grow these savings, the confidence placed in informal savings schemes, and the spending patterns described above. Taken together there is some evidence that the youths are likely to make the wrong financial choices as they grow older.

It is important to motivate young people to make savings a voluntary and regular part of their financial decisions. To accomplish this, financial institutions must implement facilities that make it possible for youths to save independently and encourage ease of deposit. This is becoming even more relevant to Trinidad and Tobago and other developing countries displaying strong growth rates. Programmes must entice young people into the financial system and financial institutions must bear in mind that these youths will become the adults that later invest in mortgages and other financial products.

Cheryl Bruce is an Economic Adviser at the Commonwealth Secretariat and assists with the organisation of the Commonwealth Finance Ministers and Central Bank Governors Meetings. Her work is geared towards fostering financial sector development and this has recently been extended to include financial literacy. Cheryl previously worked as an economist and later a policy analyst in Banking Supervision.

The Commonwealth is an association of 53 independent states consulting and cooperating in the common interests of their peoples and in the promotion of international understanding and world peace. The Commonwealth Secretariat, established in 1965, is its main intergovernmental agency, facilitating consultation and cooperation among member governments and countries.

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Access to financial services – does financial liberalisation help?

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Liberalising the financial sector may be a good way for developing countries to stimulate greater dynamism, innovation and competitive pressure. But by itself it is not enough to promote financial inclusion. Governments need to create stronger incentives for banks to serve the lower income end of the market.

Access to financial services is important for growth and poverty reduction. Access to credit or a bank account that enables an individual to accumulate funds in a secure place over time can strengthen their productive assets by enabling them to invest in microenterprises, in new tools, equipment or fertilisers, or in education or health, all of which can play an important role in improving their productivity and income.

However, in many developing countries, access to formal financial services for the poor majority of the population remains very limited. Historically, government attempts to promote access, for example through interest rate ceilings designed to make finance more affordable, through directed lending, or through requirements for banks to set up branches in rural areas, have distorted the market, and have often been counterproductive and destabilising.

The impact of liberalisation

Government attempts to promote access have often been reversed in response to traditional policy prescriptions to promote financial sector development, which have focused on:

(i) deregulation – including the withdrawal of government intervention through the privatisation of state owned banks, the freeing up of interest rates, the removal of directed lending, and reduced reserve requirements, and

(ii) financial liberalisation – the removal of restrictions on market entry for domestic and foreign financial providers.

Promoting new entry and greater competition is expected to result in more dynamism, innovation, and efficiency in the financial services sector – and the evidence supports this claim. Evidence shows that foreign entry has helped to stimulate improvements in domestic banking performance, and has significant benefits for consumers through improved service delivery, and for the economy as a whole, because of the more efficient allocation of capital which occurs as a result of improvements in the evaluation and pricing of credit risks. (Claessens, Demirguc-Kunt & Huizinga (2000) The Role of Foreign Banks in Domestic Banking Systems in Claessens & Jansen (eds.) The Internationalization of Financial Services: Issues and Lessons for Developing Countries, Boston, Mass: Kluwer Academic Press).

Banking practices and regulation may also improve through the diffusion of skills and best practice, as domestic banks imitate more efficient practices, or acquire staff who have been trained by foreign entrants. The presence of foreign banks helps build a domestic banking supervisory and legal framework, and enhances overall transparency in the sector. Foreign banks also tend to be less politically connected and may therefore be less likely to exert self-promotional influence on the regulatory authorities.

Foreign entry may also stimulate innovation, and the provision of new products or better services by the foreign entrants themselves and by local banks. For example, one study showed that competition from new foreign entrants in Hungary stimulated the main domestic bank to develop new products such as bank cards and ATMs. (Bonin and Abel (2000) Retail Banking in Hungary: A Foreign Affair? Wesleyan University. Prepared as background paper for World Bank, World Development Report 2002: Institutions for Markets).

Foreign banks can also use their international experience to introduce innovations. For example, Citibank overcame the lack of credit information on enterprises in many developing countries by introducing a new mechanism for establishing creditworthiness based on an estimate of growth prospects in particular industries. (World Development Report (2005) A Better Investment Climate for Everyone, World Bank).
Given these benefits of market opening, the expectation has been that it would also promote better access to financial services, by reducing spreads and hence reducing the cost of credit, and by incentivising financial services providers to expand their client base. But the evidence to support this has been much weaker. (Brownbridge & Gayi, Progress, Constraints and Limitations of Financial Sector Reforms in the Least Developed Countries, IDPM, June 1999).

Most foreign banks have focused on areas where local profit opportunities are perceived to be the greatest – providing financial services to large firms in urban areas. There is evidence that access to credit for small and medium enterprises (SMEs) is improved indirectly by foreign entry, as the increased competition from foreign banks in the corporate sector forces domestic banks to seek new markets that they might not previously have served. (Clarke, Cull & Peria, Does Foreign Bank Penetration Reduce Access to Credit in Developing Countries?, World Bank Policy Research Working Paper 2716, 2001). But this does not appear to extend to households, and the poor majority of the population often still have very limited access to formal financial services even after liberalisation.

This means that when traditional government interventions in the financial sector to promote access (through directed lending, subsidised credit programmes, and interest rate ceilings – however damaging they may have been to the health of the financial sector) are necessarily withdrawn prior to opening, this may actually result in reduced access to financial services, while market forces unleashed by financial opening may by themselves not provide sufficiently strong incentives to encourage banks to widen access. So it seems that liberalisation by itself is not enough to ensure greater financial inclusion.

Barriers to widening access

There are many reasons why formal provision of financial services may be limited in developing countries, even after liberalisation. High levels of government debt have often constrained access to credit for private firms and individuals, and high inflation has discouraged saving. Poor physical and institutional infrastructure (e.g. intermittent electricity supplies, inadequate telecommunications services, weak institutions for contract enforcement etc.) raise the costs of provision, particularly to poor and rural areas. At the same time, most poorer people have no collateral or credit record, and many countries lack credit bureaux, all of which serve to deter lending. Regulatory requirements such as Know Your Customer rules, introduced to guard against money laundering, can also make it difficult for poor people to open a bank account as they may not have the necessary documentation.

Thus, widening access to financial services may simply be unprofitable in many cases. Indeed, given the many types of market failures present in financial services, the market is likely to under-provide. It is also the case that weak competition policy in some countries has resulted in quite a concentrated financial sector even after liberalisation, allowing high spreads to persist, blunting incentives to expand access to new, unfamiliar and risky market segments, even where they may be potentially profitable. And a lack of detailed information about the characteristics of these market segments has made it difficult for financial institutions to correctly assess the costs and risks associated with expanding access.

Fragmented markets

In many countries, any access that the poor do have to financial services may be through informal or semi-formal financial providers, such as moneylenders, microfinance institutions, or credit unions. However, these providers are usually unable to mobilise and on-lend funds on a large scale, or pool risks over large areas in the way that formal financial institutions do. Thus they are usually small in scale, patchy in coverage, and offer a limited range of services, which can be relatively risky and expensive. The lack of access to the deeper, formal financial sector constrains the ability of the poor to participate fully in markets, to increase their incomes, and to contribute to economic growth.

There is often a significant disconnect between these alternative financial services providers and the formal financial sector, in terms of operational methods, the customers they serve, and the regulatory constraints they face. This disconnect partly explains why additional competition as a result of market opening in the mainstream banking sector has a limited knock-on impact on the parts of the market serving the wider population, including low income clients. It also makes it difficult for these alternative financial providers to expand. Often they themselves do not have adequate access to finance with which to scale up their operations.

Governments can develop a regulatory and incentive framework that facilitates greater linkages between these different types of financial providers, thus bridging the gap that prevents the knock-on benefits of market opening in the formal financial sector to be realised. For example, policy, legal and regulatory changes can be introduced that enable formal financial institutions to more easily use informal and semi-formal agents as...
delivery channels thus reducing the costs of expanding access, and which enable informal and semi-formal institutions to more easily access formal finance with which to expand their own operations.

It is possible for large, foreign commercial banks to serve low income customers directly, but the evidence suggests this is most successful when they have established relatively independent microfinance operations. Peachey and Roe (World Savings Bank Institute, 2006) found that “Banks with specialised independent microfinance units or subsidiaries found it easier to institute microfinance lending policies, procedures and methodologies and avoid interference from the larger bank culture. Perhaps the most dramatic example is Bank of Nova Scotia that operated a group-lending programme in Guyana with loans mostly under US$300 under the umbrella of a large, sophisticated, foreign-owned commercial bank.” (Peachey & Roe, 2006 Access to Finance – What Does it Mean and How Do Savings Banks Foster Access?World Savings Bank Institute).

A role for government?

As noted previously, past government interventions to promote access have often been distortionary rather than helpful. But the foregoing discussion suggests that there is a role for government beyond liberalisation. First, it is clear that governments need to create an appropriate enabling environment to promote financial inclusion and tackle market failures. While action on these fronts is already under way in many countries, it requires far-reaching improvements in a number of areas, which will take time to achieve. Additional intervention may therefore be required to create stronger incentives for banks to serve the lower income end of the market.

Such intervention needs to be implemented carefully however. Market-friendly mechanisms need to be found. A variety of interesting approaches have been adopted in developed countries that could be considered. For example, the US Community Reinvestment Act focuses attention on access by publicly rating banks on their performance in making loans to people with low and moderate incomes. Other countries, including the UK, have established a requirement or model for a ‘basic bank account’, which sets the framework for banks to provide a simple, low cost, ‘no-frills’ bank account for lower income customers.

Voluntary charters or codes of practice developed by the banking sector themselves can also help provide the necessary incentives. Even then, moral suasion from the government, perhaps accompanied by the provision of better information about lower income market segments, may well be needed to help kick-start the process. Early indications suggest that the South African Financial Sector Charter, which was developed voluntarily by banks in response to pressure from the government, and which set targets for improving access, has been successful in generating significant growth in access to financial services and demonstrating that it can be profitable for banks to sell to lower income groups. This was assisted by the provision of detailed data on patterns of demand for financial services across the population through household surveys (www.finmark.org.za), which helped banks to identify potentially profitable customers and design new, more suitable products.

Governments may also be able to facilitate the use of existing networks, such as post office branches or retail outlets, to allow the delivery of financial services without the need to establish expensive new bank branches in all areas. New technology, including smart cards, mobile phones and the internet, can also help reduce costs and broaden access, if the appropriate infrastructure and regulation is in place. Governments can also encourage the use of formal financial services by making transfer payments electronically. As this is likely to be cheaper than other methods of distribution, the savings could if necessary be used to subsidise the establishment of additional access points as has been tried in the United States. (Claessens (2006) Universal Access to Financial Services: A Review of the Issues and Public Policy Objectives in Liberalisation and Universal Access to Basic Services, OECD).

Government intervention to incentivise a widening of access to financial services should be implemented carefully, in a market friendly and non-distortionary manner. The last thing that governments want to do is deter new entry altogether. But harnessing the market dynamism and innovation that financial liberalisation can bring, is likely to be a great deal more successful than the state-led approaches of the past in tackling the problem of financial exclusion.

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Foreign exchange: the extra dimension to efficient funding

We live in an economic society where tendering is now the established norm – whether it be for a construction contract in the building industry, or to be appointed as an advisor for a takeover or merger in the finance industry. These days this even extends to when competing for available funding in the Aid and Development (A+D) sector. In all forms of business, competition is a key element and most organisations are aware that a certain amount of proposed business will be bid for, but lost. In this environment of the competitive tender there is one exception that continues to be over-looked and neglected: foreign exchange, that is the changing of funds from the donor currency into the currency in which they will be spent.

As a company that has (conservatively) saved the A+D sector in excess of US$200 million over the past 20 years, we are still constantly flabbergasted at the approach to foreign exchange that is adopted by many significant players in the A + D sector. It is remarkable how often we come across an institution who has fought tooth and nail to secure funding for a worthwhile project. Costs have been kept to a minimum, voluntary help has been enlisted and yet when it comes to exchanging the hard earned funds into local currency, the USD, GBP, EUR etc are simply handed over to the local bank in a distant country, in exchange for the ‘rate of the day’. This has been described as being akin to saving to buy a car, but at the point of purchase simply handing over the money to the dealer and letting him choose the make, model and colour! No one would ever do that, so why do some choose to do so when buying local currency?

By failing to tender competitively for foreign exchange deals, particularly into the exotic markets, millions and millions of USD of value are lost without anyone ever being aware.

A cautionary tale

The pitfalls of simply entrusting local banks (in the country of the project in question) with the hard currency are numerous. Firstly there is the potential loss of value that may be incurred by relying on a sole rate source. We had a first hand experience of this when, in 2004, an aid organisation finally decided to competitively bid out the conversion of their US dollar inflows into Sierra Leone. The organisation had been sending a monthly amount of US$2 million to its bank and receiving the ‘rate of the day’. On this occasion they checked with their bank first what that rate would be before sending the funds. They also called our offices to get our rate for such a transaction. Our rate reflected the competitive local market rate, at the time being 10 per cent better than that offered by the organisation’s own local bank. Having never bid out its USD, this agency was never aware of the extent to which it was being short changed – in the region of US$200,000 a month! Naturally the agency began bidding out its foreign exchange transactions.

Whilst this example is extreme due to the quantum involved unfortunately, it is not that unusual. In many ways the scariest thing about this example is that the agency in question (and presumably its donors) were totally unaware of the large wastage of funds. This is one of the big problems with foreign exchange losses, they are often invisible – they do not appear on a Profit and Loss statement, nor are they often included in the ‘administrative costs’ figure that so many A+D sector organisations are scrutinised by. By failing to tender competitively for foreign exchange deals, particularly into the exotic markets, millions and millions of USD of value are lost without anyone ever being aware.

“...sector, every penny matters for the projects on the ground.”

Philip Smith, Director

Efficiency includes currency conversion

In an ideal world all donors whether they are a government agency, a charitable foundation, trust, or even a person on the street, should have the right to expect total efficiency in the way the beneficiary of that donation purchases the local currencies needed for the running of its operations on the ground. Organisations should always be naturally concerned when their local bank tells them that they are not allowed to receive local currency into their account, that it is illegal to bid other banks in the local market and that they are obliged to send their USD simply to their local bank. This is almost universally untrue. We, as an organisation, positively encourage our clients to take comparative prices when dealing...
with us – it is only by comparing what we can give, to what is available elsewhere, that our clients can gauge whether they are receiving good value or not. Likewise, we do not want them to deal with us if there is a better price elsewhere. We feel that it is ethically very important that funds raised in the name of development and relief, for much needed projects, are correctly applied and achieve the best possible value.

If it was a requirement set down by the Charities Commission that required all registered charities to provide clear and transparent reporting on all their transfers, the value added to the AID sector would be huge.

So what is the answer? Should certain members of the AID sector continue along the road of letting the car salesman decide what car the NGO is buying? Or should Donors demand transparency from the NGOs they fund, by forcing them to prove a competitive tender was entered into for their foreign exchange needs, in the same way that it is for all the other services that the NGO receives? How better to prove financial control, prowess and efficiency than to seek three bids on all currency exchanges over, say, $25,000. Although this may sound like a low level to start the process from, with the difference achieved often being in the 2+ per cent region, that can result in a saving of more than $500 on a simple transfer of $25,000, helping to stretch even limited budgets significantly further.

The reaction from many in the AID sector to these proposals is often that such a process places additional administrative burden and cost on them. However, is it really better to absolve oneself of the responsibility of what happens to funding once it has left head office, resulting in considerable potential loss of value, rather than potentially picking up an extra administrative burden and cost which will generally result in a return of five times the cost incurred? Ultimately it will be the funding agencies who decide – as they become increasingly aware of this black hole in NGO financial procedures, surely they will demand more transparent reporting on how the money was spent, rather than simply accepting that $100,000 was sent to country A for project B?

Surely the Donors are entitled to expect that their generous donations are not being wasted, or fraudulently expropriated, as has been known to happen. Local banks have not been unknown to enter into collusion with a local finance officer in a ‘you scratch my back, I’ll scratch yours’ type of arrangement. The finance officer allows the bank to change the funds at the rate it chooses, in return for which it grants various favours to the finance officer and sometimes also other members of staff. These ‘favours’ in our experience have ranged from gifts, dinners, trips, money and even in one case a new car!!

Huge additional value

If a competitive tendering process was forced on all NGOs by those that regulate and fund them, all of these issues could be avoided. If it was a requirement set down by the Charities Commission that required all registered charities to provide clear and transparent reporting on all their transfers, the value added to the AID sector would be huge – probably larger than any single fund-raising idea could possibly hope to raise. It may not prove to be quite so well received by the shareholders of certain banks though...

It is a disappointment to still hear from international aid agencies that they operate the way they do because they always have done so, or because their systems do not allow them to alter their established modus operandi, or that their programs or partners prefer dollars. People must be more accountable for what they do with the public’s money. Needless to say, some of the worst offenders are the larger agencies, who hold themselves up as having the highest moral and ethical standards and claim to lead the way.

In conclusion, we believe sincerely that the need for reform in the AID sector is great and that the changes could yield significant results. In a sector where every penny counts, we look forward to a time where greater guardianship is taken of the significant resources dedicated to AID and wait with baited breath to see who will make the first move.

“NGOs have a duty of care not only to the beneficiaries, but also their donors to maximize the value of every pound sent.”

Mark Horne, Foreign Exchange Sales

INTL Global Currencies has worked in partnership with international aid, development and charitable organisations for 20 years, trading and delivering their exotic currencies in preference to the international banks. INTL Global Currencies has significant experience in over 100 exotic foreign exchange markets and is able to offer highly competitive rates in these markets. We understand the need for expeditious, efficient and reliable delivery of local funds, and through our unique network of local banks and counterparties we are able to offer 1-2 day delivery anywhere in the world. INTL Global Currencies is a wholly owned subsidiary of International Assets Holding Corporation.

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Rethinking public financial management reform in developing countries: Commonwealth Secretariat introduces a gap-closing toolkit

In recent times, the rate of economic growth in all the regions of the world are in the upward spiral, and trends in developing countries demonstrates, also, that robust attention is being paid to financial governance – the linchpin of resource development. These come amid perpetual pressure being put on governments to increase public service delivery, as well as meet the wider fiscal social contract sealed with the electorates. In this context, the author explains the background to the new Commonwealth Public Financial Management Self-Assessment Toolkit (CPFM-SAT).

Progress in public financial management (PFM) reform is evidenced by a number of groundbreaking measures introduced by governments during the last decade. These include the harmonisation of revenue agencies for effective tax administration, in order to reduce dependency on external budgetary support. The Kenya Revenue Authority, for example, now generates 95 per cent of budgetary resource, thus reducing that country’s reliance on donor funds. In addition, the introduction of integrated financial management information systems (IFMIS) for a better management of resources is another step in the right direction. Almost all Caribbean member countries, for example, have installed IFMIS that are up and running; albeit with some hitches. Although not discussed in this article, it must be mentioned that the IFMIS story is still fraught with challenges in developing economies.

Furthermore, the modernisation of cash management through the introduction of Treasury Single Account (TSA), such as in Ghana, is another trend that has had impact on country PFM reforms. TSA, for example, saves huge amounts of resources in governments by informing debt management decisions and reducing the prospects of ill-considered domestic borrowing with high interest rates, which leads to a squeeze on domestic investments. Moreover, entrenching the independence of key institutions such as the auditor-general’s department is also gaining ground. In India, South Africa and Kenya, for example, the strengthening of external supervision through enhancing parliamentary functions has increased fiscal responsibility, transparency and accountability in the public sector. The list goes on.

External support
Country efforts have always been bolstered by a stream of support from international players to keep the momentum on reforms, as well as guide the process. On its part, for example, the Commonwealth Secretariat has published Guidelines for Public Financial Management Reform: Strengthening Transparency and Accountability in the Public Sector (2006), in support of the Commonwealth Heads of Governments Mandate on financial management (See 2003 Aso Rock Declaration). This is being reinforced by a follow-up publication, Commonwealth Framework on Internal Audit and Internal Controls, which is in process of publication. The Secretariat’s public expenditure management (PEM) programme, in the Governance and Institutional Development Division (GIDD), has also introduced a groundbreaking capacity building programme, ‘Building Pyramids in the Valleys’, which aims to transfer skills and knowledge from high capacity institutions within the Commonwealth. GIDD has also created a Thematic Fellowship of core financial management practitioners drawn from member countries to intensify the sharing of country experiences.

In-country policy initiatives have also been augmented by a steady flow of support from the donor community within the spirit of the Paris Declaration for aid effectiveness. The public expenditure and financial accountability (PEFA) framework – a support tool managed by the Washington based PEFA Secretariat – which aims to enhance assessment and better management of public sector finance, is the chief diagnostic tool introduced by the consortium of international stakeholders, including the United Kingdom Department for International Development (DFID) and the World Bank. This array of reform measures may suggest that the end is drawing near to the hassles that accompany financial governance. But that scenario is far from being achieved – in fact, judging from ongoing challenges facing developing economies.
Some PFM issues and challenges

While the introduction of reform measures, as mentioned above, have had a positive influence on financial governance, there remain a number of issues and challenges that jurisdictions must grapple with in order to achieve effective service delivery and a progressive level of development. Four major challenges are considered here:

- **Weak coordination of reform**
- **Institutional overload – creating too many institutions with no coordination strategy**
- **Placing too much emphasis on political will, with little regard to administrative and professional will, and**
- **Failure to appreciate and internalise in-country PFM assessment.**

A key challenge threatening reforms lies in the manner in which the activities of various reforms are coordinated. In other words, there is a lack of synergy. Every strand of reform – be it treasury reform, public procurement, debt management or the civil service – is interrelated and integral to sustainable economic development and good governance. Coordination of the reform process is significant, such that it requires a well-established structure or system that not only captures information and plans a strategy around unfolding events, but is equally equipped and peopled by capable officials and technocrats that could buy easily into political will, as well as manage political interference. In some developing countries, coordination is weak and has given rise to disjointed data management and a failure to track and analyse progress across all the sectors in the reform process.

In a number of selected cases, institutional overload – bloating reform by creating parallel institutions to carry out similar tasks – derails or stalls sectoral reform rather than improving it. The practice has witnessed the emergence of new structures to support sectoral reforms. For example, in the area of local government reform, rather than enhance an existing government ministry responsible for local government administration, a new unit is created to duplicate the functions of the ministry. At the end of the day, both the new and the existing institution do not talk to each other, thus dealing decisive negative impact on reform.

The question of a demonstrative political will – the linchpin of a successful policy implementation – has undoubtedly put professional and administrative will on a back burner. The premium placed on political will for achieving a successful reform has been such that the role of professionals and public sector chief executives have received little attention compared with the former. Undoubtedly, the latter’s role is complementary as well as critical. This is because permanent secretaries and senior professionals do influence the shaping of policies as well as drive implementation. It stands to reason, therefore, that although political leadership holds prominence over administrative and professional inputs, the latter are undoubtedly significant and must be brought to the fore in the discourse of reform. Little wonder, therefore, that in economies where the power and influence or professionals and chief executives are fully appreciated, it has become a common practice for chief executives to enter into performance contracts with ministers, to deliver results in accordance with approved departmental estimates. The argument therefore boils down to the simple fact that the will to get things done comes in a trinity: the will of the politician, the administrator and the professional – the PAP will – must blend in order to deliver successful reform agenda. It is time to move away from the age-old discourse of political will.
The fourth question that requires a rethink, which is also the chief focus of this article, comes in two guises: firstly, cultivating a willingness to adhere to best practice in financial management reform; and secondly, inculcating the capacity to conduct country financial management assessment independent of external assistance. Following the publication of the PFM Guidelines (2006), the Commonwealth Secretariat was hoping that member countries would adhere to the document, although with the understanding that some modifications will be required in accordance with national dynamics. Shortly afterwards, the Secretariat “identified two major challenges in the use of the work: the publication neither guarantees adherence to the principles of PFM reform, nor does it measure progress or take stock of the reform process.” It is in regard of these two major challenges that the Commonwealth Public Financial Management Self-Assessment Toolkit (CPFM-SAT) was crafted to enhance PFM reform.

Taking a closer look at the challenges surrounding country assessment, it is not uncommon for senior financial officials to receive more than two teams from development partners to assess the overall financial management system against a set of agreed benchmarks. While this practice is plausible in terms of ensuring that developments funds are efficiently coordinated and institutional structures such as external audit are effective within the governance framework, they do not, however, internalise the responsibility that must come with self-determination, self-discovery and the ability to identify weaknesses, independent of external players. It could be said, therefore, that unless the practice of assessment, monitoring and evaluation are effectively appreciated and internalised by developing economies, the prospect of achieving a system that is reliant on the internal machinery for strategic thinking and planning – the most important element of self determination – would be remote. This does not discount the value of external support in the form of financial and technical resource, which is indeed vital to reform. Put in another way, what it really means is that a cab driver who is able to read traffic signs on his own, would make a better driver than a driver who relies on third party assistance to realise that a red light requires him to stop. This gives rise to a PFM rethink.

The Commonwealth rethinks PFM reform process

Realising that the two major challenges – adherence to best practice, and internalising independent assessment – are failing trends in developing member countries, the Commonwealth Secretariat developed a gap-closing toolkit to assist developing member countries carry out assessment on financial management with little or nor external assistance. The toolkit, which is known as the Commonwealth Public Financial Management Self-Assessment Toolkit (CPFM-SAT), was developed within a period of 18 months through a widely consultative process at a number of seminars and workshops, as well as by a group of experts. The practitioners, including more than 100 senior finance and budget officials, were drawn from about 40 member countries. The CPFM-SAT was developed by the member countries themselves for the simple reason that reform must come with some sense of ownership (although not in every case). For each strand of PFM, practitioners asked the simple question: what constitutes best practice? This would be followed by group-based brainstorming discussions; at the end of which, answers are provided in the form of milestones and indicators in a plenary. The Commonwealth Secretariat only provided guidance and facilitated the process.

Features of the CPFM-SAT

The CPFM-SAT has been adapted into high level interactive software such that it generates a score (out of a total of 100) at the end of an assessment under each sub-area, and a global score and comment at the end of the overall assessment. For example, it can generate a score and appropriate comments at the end of assessing performance in Asset Management. The comments come in the form of an advice, which should be considered by the appropriate PFM coordinating unit, or the cabinet, for necessary action. The toolkit has a total number of 41 ‘milestones’ and 157 indicators, with scores ranging from one (lowest) to four (highest), for each indicator. The areas of assessment considered critical to reform are accountability and stewardship, planning and resource allocation, measurement, performance and value creation (see Figure 1).
Relevance of the Toolkit

The relevance of the toolkit lies in the fact that it is a country self-assessment instrument, which helps to inculcate and nurture the much-needed spirit of independent review and assessment. It brings with it the discipline of in-country monitoring and evaluation, independent of external inputs. In addition, since the work helps to identify country strengths and weaknesses, it naturally provides opportunities for adopting corrective measures, as well as building on identified strengths.

For heavily indebted poor countries (HIPCs) that are dependent on donor budgetary support, the prospect of identifying country weaknesses and strengths, independent of a joint assessment, is significant as well as strategic. The tool comes as a handy mechanism for the conduct of pre-joint assessments that provides traffic light signals on the areas where energy should be concentrated ahead of a joint assessment with development partners. The bottom line is, self-assessment provides a platform for a deeper appreciation of problems as well as understanding where a country is coming from, and where it is headed.

Relationship with other assessment tools

GIDD considers the CPFM-SAT as a supporting instrument of other assessment tools, in particular, the PEFA Framework, which is used by some Commonwealth member countries. It is hoped that while the PEFA framework consolidates joint assessment with developing member countries, the CPFM-SAT, on the other hand, will enhance in-country capacity in conducting pre-joint assessments. In essence, the latter complements the former.

The way forward

The CPFM-SAT will be introduced to Commonwealth Finance Ministers for endorsement at the high level meeting slated to take place in Georgetown, Guyana, from 15-17 October, 2007. During the presentation, ministers will be requested to consider a three-yearly Commonwealth-wide survey on the status of financial management in member countries. Ministers will also be asked to consider the introduction of exchange programmes as a means to facilitate the sharing of experience and best practice among member countries.

In conclusion, while PFM reform is gathering pace and continues to contend with challenges as discussed in this article, one of the greatest challenges remains the internalisation of country financial management assessment. This task falls squarely on the shoulders of countries themselves as well as development partners. The CPFM-SAT promises to fill the gap in partnership with existing frameworks.

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The Commonwealth is an association of 53 independent states consulting and cooperating in the common interests of their peoples and in the promotion of international understanding and world peace. The Commonwealth’s 1.8 billion citizens, about 30 per cent of the world’s population, are drawn from the broadest range of faiths, races, cultures and traditions. Among other things, it stresses the need to foster international peace and security; democracy; liberty of the individual and equal rights for all; the importance of eradicating poverty, ignorance and disease; and it opposes all forms of racial discrimination. The Commonwealth Secretariat, established in 1965, is the main intergovernmental agency of the Commonwealth, facilitating consultation and cooperation among member governments and countries.
Traditional criminal patterns in the Caribbean Basin region involve theft, burglary, simple fraud, murder for hire, drug trafficking involving marijuana between the islands and kidnappings. Law enforcement officials have discovered that direct investment is favoured and embraced by local traffickers. Therefore significant investments in real estate, luxury cars, speedboats and jewellery are common avenues for the disposal of illicit proceeds from these activities.

Additionally, the accounts of relatives and friends are popular vehicles for criminals to conceal their gains. A local drug trafficker utilised the services of his aunt who also served as his accountant and laundered his drug trafficking proceeds through her boutique.

However, the Caribbean Basin – not by choice but by virtue of geographic location – is also now recognised as a major transhipment corridor for the trafficking of illicit drugs. Our extensive, unprotected coastlines and ill-equipped, under-resourced protective services make us attractive targets to the extremely liquid, technologically sophisticated and highly motivated producers in the South in their quest to move their product to the consumer markets of North America and Europe.

A variety of methods are utilised. These include overland routes across South America to points near the Caribbean, then by ocean-going boat to identified drop-off points, to be picked up by speedboats and distributed between the islands.

One very creative example involved a cyclist from a European country who had travelled to a South American destination, and on his return home in his biking gear had cocaine concealed in the frame of his racing bike. Within the context of the jurisdictions covered by the Caribbean Financial Action Task Force, an estimated US$60 billion of drugs proceeds are reported to be laundered annually.

Laundering methodologies

However, the various methods by which criminal drug proceeds are laundered are well known. These include engaging the services of accountants, lawyers, money managers, bankers and real estate agents who may or may not be aware of the criminal origins of the money.

The trust accounts of stockbrokers have been used to purchase shares on the stock exchange through the stockbroker’s nominee account thus masking the true beneficial owner until the criminals decide to have them transferred in their names. Through this technique criminal enterprises can acquire shares in public companies and could eventually become majority shareholders in one or in a host of companies straddling the entire spectrum of a country’s economic activity.

Law enforcement officials believe that there are networks of legitimately established private companies operating in several Caribbean Basin jurisdictions, related in terms of ownership or control, and whose bank accounts are being utilised to receive and mask tainted funds. It has been shown that once a legitimate establishment has served its purpose in the laundering process, an exit strategy would entail the sale of the business. One of the variables in determining the sale price would have been the income flows as demonstrated by bank statements and other data. The rosy picture painted as a result of money laundering activity would at a later stage prove the undoing of the purchaser through the failure of the business. This loss of investment and the resulting unemployment would impact substantially on economic activity, particularly if the enterprise was a dominant player in the economy.

Moreover, if the purchase was financed through a bank facility, then the exposure of the bank or banks could…
erode confidence in the markets, the banking system and in the role of profits to indicate an effective company.

Small companies operating within the same sector as establishments aided with illegitimate proceeds could be forced out of business through dumping, as well as through legitimate competitive activity, with similar knock-on results on the banking system. National tax revenues will be reduced and levels of unemployment increased, and the attendant rise in criminal activity would place enormous strain on the social fabric of any country.

In the Caribbean, where some countries lack natural resources and where traditional agriculture-based economies have declined, tourism and offshore banking continue to be developed as important service areas for the generating of revenues. However, there are hidden dangers in these developments as legitimate structures are also being utilised in the layering mechanism for money laundering by criminals who emanate from outside the region.

In one jurisdiction, professionals made use of offshore trusts, international business companies and bearer shares to disguise and protect the illicit assets of their clients and thus the fees garnered for their professional services.

**Dangers posed by criminal organisations**

Criminal organisations now wield enormous social, political and economic power and can corner the market in a particular business sector or possibly exert control over the entire economy, particularly in small countries. The vast wealth at the disposal of the launderers, at times surpassing that of regional economies, allows international criminal organisations to penetrate political systems by influencing elections or through bribery of government officials. Moreover they have been known to suborn and corrupt financial sector personnel in order to ensure the longevity of their criminal enterprises.

Crime is profitable to criminals everywhere. The question is how is this threat to be effectively addressed? In the case of criminal proceeds from money laundering activity, the threat is severe. Macroeconomic policymakers should examine the apparent profitability of corporations engaged in money laundering activity under the veneer of legitimacy, where payment of corporation tax is considered but a small and necessary cost of successfully laundering the proceeds of crime. Such reviews could be instrumental in persuading governments to address these dangers with the urgency that is required.

**Defensive measures**

**National anti-crime committee**

Recognition of these dangers should lead to the creation of a national anti-crime committee comprising representatives from all stakeholder institutions in the fight against transnational organised crime. These should include the Attorney-General, Minister of Finance, judiciary, banking, money services, securities and insurance sectors, trust and company service providers, real estate agents, dealers in precious metals/stones, legal professionals, accountants, and the non-profit sector.

The remit of such a committee would typically be to oversee the overall implementation of government policy to fight crime by promoting effective collaboration between policymakers, financial institutions and their regulators, law enforcement agencies and the general public. Such a committee robustly undertaking its remit would be indicative of a strong and serious national policy commitment in the battle against cross-border financial crime.

One of the most important responsibilities of the committee must be to develop and sustain a strong, nationwide culture of compliance with international benchmarks against transnational organised crime in all its forms. In some instances in the Caribbean Basin region, such a position has led to jurisdictions being ahead of international standards on certain matters, such as the coverage of ‘gatekeepers’; the abolishing or immobilisation of bearer shares; the scope of the suspicious activity reporting obligation; and the undertaking of retrospective due diligence on all existing clients in keeping with modern ‘know your customer’ principles – all critical tools in the fight against transnational organised crime.

**Patrol boats and radar**

In other instances, one jurisdiction in a deliberate move to protect its coast lines against the drug trade as well its other vital interests has decided to acquire offshore patrol boats and to have 360-degree coverage of its borders by radar which have been installed and operational.

**Education and training**

Other improvements have included the need that all institutions – be they bank or non bank and the new designated non financial businesses and professions and their supervisory bodies – should be encouraged to adopt as a general rule the encouragement of high ethical standards of professional conduct in the operation of their establishments.

In one jurisdiction this educative initiative has included the publication of a document entitled *A Pamphlet for Retailers of High Value Goods... Taking the Profit out of Crime*. This pamphlet describes the financial intelligence unit, defines money laundering, explains the obligations of retailers of high value goods, when and what to report, identifying examples of what may constitute suspicious activity, as well as providing some insight regarding what happens when merchants file a suspicious activity report.

Management in these establishments must, as a highest priority, be encouraged to exercise vigilance in preventing their institutions from being suborned by criminals.

**Enhancing criminal justice capacity**

In one jurisdiction, during the course of criminal proceedings against several former high level government officials and businessmen concerning a major government contract, the preliminary enquiry lasted five years.

The judiciary, prosecutors and law enforcement must have the capacity to expeditiously preside over, prosecute and investigate complex, multi-jurisdiction and multifaceted criminal enterprises, using sophisticated techniques that may be unfamiliar.
Within the Caribbean region facilities exist for electronic or paperless trials, computerised case management and plans for the e-filing of documents to initiate new cases or advance existing ones. In two recent major serious fraud and money laundering cases – successfully prosecuted and involving layering activity – the total proceeds involved were approximately US$87.5m.

**International cooperation**

These domestic achievements should not be seen as isolated events, as assistance with similar levels of success is being provided to foreign authorities for money laundering investigations and prosecutions. In the fight against global criminal enterprises, the law enforcement community should strengthen their ability to provide international cooperation to their foreign counterparts through a number of forums, including Interpol and the Caribbean Customs Law Enforcement Council (CCLEC), as well as direct police-to-police contact.

**Public education and awareness raising**

These successes must be trumpeted to domestic, regional and international stakeholders. The criminals must know that there are concerted and determined efforts to pursue them and their ill-gotten assets. Part of this process should be the compilation and publication of these cases so that stakeholders could be educated on an ongoing basis on the latest trends and methods being utilised by criminals.

Within the CFATF efforts are continuing on a regional compilation of criminal typologies which we hope will be published during 2007/2008 and updated regularly thereafter.

**Compliance reviews**

While the domestic health-check mechanism for the strength of the anti-crime defensive infrastructure is part of the duties and responsibilities of the national committee, the external framework for compliance monitoring is the mutual evaluation programme, as developed by the global assessment bodies such as the Financial Action Task Force (FATF), FATF-style regional bodies like the CFATF, and the IMF and the World Bank. In short, this entails a visit by a team of regional and international experts to the jurisdiction over a two-week period where they test the legal financial and law enforcement architecture for compliance with the FATF 40 recommendations and the nine special recommendations against terrorist financing. The overall goal is not only protection of the domestic framework, but the protection of the international financial system from the predations of criminal enterprises.

**Technical assistance and training**

With this in mind, the international community provides resources so that technical assistance and training can be brought to bear on those areas that are important to the fight against crime, but which are less than compliant with acceptable international standards. The Caribbean Basin region has popular tourist destinations, with one jurisdiction attracting approximately 2.1 million visitors during 2006. However, with this success comes potential vulnerability to illegal cross-border movement of currency and negotiable instruments.

Through global technical assistance and training programmes, new equipment can be provided for customs departments, such as currency sniffing dogs and ion scanners. Cooperation could also be provided to some jurisdictions through the availability of regional or international police officers to engage in undercover activity – something that may be impossible or very difficult to undertake in small countries where local officers are well known in the community.

Another initiative that has been proposed for consideration for a number of years is an itinerant group of prosecutors skilled in serious fraud and complex money laundering schemes who will operate across the region, with the required initial and ongoing training being provided through bilateral arrangements with donor countries.

**International burden-sharing**

In recent years, as the risks from transnational criminal organisations have increased, the international standards to combat them have expanded in tandem, with significant cost implications for the global community. This is occurring in a climate where there have been reductions in aid and investment in real terms and unfavourable policy decisions by international organisations on trade issues.

Given these circumstances the challenges posed for macroeconomic policymakers are indeed formidable, particularly in small countries, as the need to adhere to ever-changing international standards demands the reallocation of scarce resources.

It is therefore understandable that there continue to be calls for a far-reaching dialogue at the highest international political levels so that the true cost of protecting the international financial system against the machinations of money launderers can be determined and more equitably shared by all states. This would enhance the global capacity to pursue criminals successfully and take the profit out of crime.

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The **Caribbean Financial Action Task Force** (CFATF) is an organisation of 30 countries along the Caribbean Basin which have agreed to implement common countermeasures to address the problems of money laundering and the financing of terrorism. It was established as a result of meetings convened in Aruba in June 1998 and in Jamaica in November 1992 when the Kingston Declaration was set forth and plans made for the establishment of the Secretariat. The CFATF was used as the model for the creation of other FATF-style regional bodies around the world.

The CFATF Secretariat is hosted by the Government of Trinidad & Tobago. Website: www.cfatf.org
E-governance in Commonwealth countries

New technologies bring increasing changes for governments around the world. This phenomenon is resulting in new challenges to governments whose citizens want access to government through an array of technologies, sound policies, privacy and security assurances, accessible services and other interactive programmes between government agencies and the citizenry. E-governance is a dominant concept that is efficiently driving the implementation of e-government and technology projects around the world.

The ‘e’ in e-governance refers to all aspects of technological implementation in governments throughout the Commonwealth countries. The ‘e’ is now referred in a multiple of ways in the sense that it can refer to e-consultation, e-readiness, e-participation, e-delivery, e-performance or any computations and combinations referring to governance and programme implementation. It is important to stress at the outset that the ways e-governance is used are multi-faceted. Implementing an e-programme in a developed country is very different from that in a smaller developing country that has limited financial or personnel resources. It is important that all implementation schemes take into account the possibilities and limitations that exist to get programmes up and running. Articulated below are the varying dimensions of e-governance and how the basic principles work for countries at different levels.

Definitions and nomenclature and the application of terms connected to any project being undertaken is important. E-government and e-governance can be defined as two very distinct terms. E-governance is concerned with the whole spectrum of the relationship and networks within government regarding the usage and application of information and communication technologies (ICTs).

- **E-government** is a narrower discipline dealing with the development of online services to the citizen, more the ‘e’ on any particular government service – such as e-tax, e-transport or e-health.
- **E-governance** is a wider concept that defines and assesses the impacts that technologies are having on the practice and administration of governments and the relationships between public servants and the wider society; dealings with the elected bodies or outside groups such as not-for-profit organisations, non-governmental organisations (NGOs) or private sector corporate entities. E-governance encompasses a series of necessary principles and steps for government agencies to develop and administer to ensure successful implementation of e-government services to the public at large. The differences between these two important concepts are further explored below.

The ‘e’ part of both e-government and e-governance stands for the electronic platform or infrastructure that enables and supports the networking of public policy development and deployment. It is by now widely acknowledged that the original impetus for acquiring and using electronic apparatus in government and governance arose from the earlier successes with the same kind of strategy in commerce. E-commerce had previously rested on credit and debit card processing for purchases, and on faxing of bulk orders and subsequent invoices in business-to-business transactions. In Canada, the United States and the United Kingdom, for example, the emergence of e-commerce by the private sector helped to stimulate and drive the evolution of e-government within departments and agencies. At the political leadership level it was clear that e-commerce was reflecting the enormous changes taking place in the economies of countries in the developed world.

Developed countries have the financial and personnel resources to move forward quickly and efficiently in the evolution and implementation of online services. In fact, many countries, during the nascent era of e-government in the early to mid 1990s implemented programmes that resulted in failures in bringing services online, which cost governments hundreds of millions of dollars. However, countries in the English speaking world, such...
as the United States, United Kingdom, Canada and Australia, when confronted with overspends, were able to absorb the losses and move on to develop online services with sufficient funding and necessary personnel for projects.

A different approach is needed to e-government implementation in developing countries. Essentially, many of these countries have been able to turn to donor international organisations and developed countries for finance and personnel resources.

Putting the ‘e’ on services, such as e-health, e-participation, e-voting, e-environment or e-weather, for example, serves as a guide to the wider subject matter of e-government and e-governance, that can, in time, be imprinted on the public mind. More importantly, the use of terms such as e-government, e-governance and e-democracy leads to the creation of an identifiable discipline. This then widens the development of the subject beyond the parameters of simply government boundaries to the larger spheres of civil society, associations, unions, the business community, international organisations and the academic world.

In society, it is the identifying of concepts through words and phrases that leads to cohesion and order. Subject matters create an ambience between stakeholders throughout the society. For example, ‘public transport’ or ‘environmental issues’ are phrases understood by citizens who then relate them in their minds to the mass movements of our times. This is the way e-government must continue to evolve.

In time, technologies will change the way society shapes itself and this will lead to a widening of this subject matter into new spheres. At that point a new nomenclature will arise reflecting the change articulated in future generations. But this new nomenclature will only be an extension of the discipline that began to evolve in the late twentieth century. The danger in this time of modernity is the urge to move with the latest fashionable ‘craze’. It is the job of governments to maintain stability at times of great change in which we are now living. Part of this stability is forward thinking, while still keeping rooted in acceptable principles and processes. Government, governance and democracy have been with us for a long while. By adding the ‘e’ to these words we maintain a stream of thought and a conceptual framework with which the public can relate. Governments are not in the business of creating fads. It is the job of governments to absorb the losses and move on to develop online services with sufficient funding and necessary personnel for projects.

E-government programmes are now ‘citizen-centric’ in that governments conduct in-depth surveys to determine what particular services take first priority. For example, in some countries, such as Canada, an early innovation was the implementation of online filing of tax forms. Over the years this and other online services have proved to be successful across all sectors of society. A ‘citizen-centric’ approach to e-government recognises that the needs of the citizen come first and will result in successful implementation of online services. In many countries, citizens take for granted the right to go online and engage in information gathering or communication via email or through government websites to public servants. Government websites around the world are now vast information repositories.

### Citizen-centric government

Research looking at the activities of many governments and international organisations around the world indicates that much has been done, and continues to be done, to move into this new form of online governance. Governments on the whole are aware of the changing expectations of their citizenry, and of the desire, especially by not-for-profit groups and emerging e-democracy groups, to have a say in the evolution of government policy. How governments deal with this could very well determine future relationships between government and the citizenry. This is a serious governance issue that many governments are now facing. As a result, for example, the UK government at the national and local level has evolved extensive e-participation programmes allowing citizens to engage in dialogue with government departments. This is happening globally, as not only governments but many e-democracy groups have emerged in many countries, developing tools, resources and programmes to involve citizens in the fast growing e-democracy movement worldwide.

E-government continues to be implemented throughout the Commonwealth through a series of important actions. These include political leadership and input of senior public servants, cross-government departmental cooperation, working partnerships with the private sector, especially in the IT sector, and consultation with citizens and groups in society. The latter can be achieved through a number of mechanisms, such as surveys and focus groups, in order to determine what members of the public want in terms of online services.

### E-governance in developing countries

It must be stressed that there are vast differences in the implementation of e-government in developed and developing countries. For example, some key elements of success in developed countries are sufficient, experienced and professional personnel with:

- Funding
- Resources
- Political support, and
- The ability to build technology infrastructures.
The five points to be implemented to assure the evolution of e-government projects and initiatives in developing countries are:

- Political approval of funds and resources from a variety of international organisations
- Leadership at the top echelons of government to see e-government projects implemented
- Sufficient financial and personnel resources
- Built-in policy issues such as security, privacy and accountability
- Committees from different levels of government or within departments cooperating to bring e-government to fruition.

The majority of medium-developed and developing countries receive extensive funds to implement e-government projects. International organisations such as the World Bank, the OECD, the British Council, the Canadian International Development Agency (CIDA) and the United Nations are just some of the donors. In some instances funding is on a lending basis although, overall, there are programmes from international organisations providing the necessary outright donations and grants. International organisations also often send experts and consultants to developing countries as advisors for the evolution of IT and e-government programmes.

An important route to ensure success for developing countries is the development of National IT plans. Such plans are vital to allow for all the different aspects of what needs to be done. An e-readiness assessment plan is crucial. The lack of such a plan can result in failure in the development of e-government projects. For example, one of the first steps to be made when moving forward with IT projects to serve the public is to determine the number of households, educational institutes, government agencies and departments, and commercial organisations that have online capacities over which services can be offered. This determines the number of services to go online and what funding and personnel are needed. An assessment as to the priority of services to be implemented also must be made.

An essential point to be made about e-government evolutions in developing countries is that the circumstances vary from country to country. In many jurisdictions e-government services would only be available in major cities. This is due to the fact that in smaller jurisdictions and towns the infrastructure is not there to implement the technology.

When there is no internet connection or facility to hand, mobile phones become a technology of choice to access government services online. Mobile phones have been made available at low cost or as donations in many countries.

While this is a solution to gain access to government services there is still the fact that in many poor countries there are too many people that do not have access to these services.

Challenges to wider implementation

E-government and e-government are now institutionalised programmes in the majority of countries around the world. There is a large grouping of materials on these subject matters online and in the halls and libraries of governments, universities, NGOs, consulting firms and a host of other groups in society. At this time only about one-sixth of the world population has some form of online access. There are many challenges that lie ahead to encompass the poor and disenfranchised of the world. E-government and its sister groupings can help to bring the information richness of the online world to more and more people.

We are at a stage of fundamental change in which the internet and all our new technologies are changing our cultures and the way we live. Our biggest challenge for the future is to encompass more of the citizens of the world.

Professor Thomas B Riley is the Chair of the Board and co-founder of the Commonwealth Centre for e-Governance (CCEG), and President of Riley Information Services Inc, Canada. He has been involved in public policy and information issues for over 35 years, beginning his career as an advocate for information and privacy laws in the early 1970s. He is the author of three books including Time’s End: a novel with commentary on where society might be going. He has researched and written on a wide range of issues in relation to public sector reform and the impacts of information technology for the past 20 years; he has also been in demand as a public speaker internationally on the role of governments in our changing technological environments.

The Commonwealth Centre for e-Governance (CCEG) operates on a global scale, with a board of Directors and Advisory Council from around the world. Members come from government, the private sector and civil society. The purpose of the CCEG is to provide insight and knowledge on the changing nature of government in our growing technology infrastructures. The CCEG is working to develop sets of best practices on how best to use technologies to implement the goals and objectives of public administration. It is the goal of CCEG to work with governments and international organisations to contribute to the growing knowledge base on e-government, e-governance and e-democracy. CCEG continues to contribute to developments in these subjects in both a theoretical and practical manner.

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The ‘global deal’ to reduce poverty: progress and responsibilities

By Eveline Herfkens
Executive Coordinator, the UN Millennium Campaign

When 189 governments from the North and the South signed the Millennium Declaration at the UN’s Millennium General Assembly in September 2000, there was a sense of urgency. Urgency to ‘free our fellow men, women and children from the abject and dehumanising conditions of extreme poverty, to which more than a billion of them are currently subjected’. They committed to work together to build a safer, more prosperous and equitable world for all its citizens by 2015 and they adopted the eight Millennium Development Goals (MDGs) that put people-centered development at the heart of the global and national agendas.

The Millennium Development Goals committed rich and poor countries to eradicate extreme poverty and hunger, eliminate gender inequality and environmental degradation, and ensure access to education, healthcare and clean water, all by 2015.

The MDGs brought together for the first time a shared vision, representing a global partnership based on shared responsibility by all countries, rich and poor. Developing countries pledged to improve governance and reform policies, channelling their resources towards the first seven goals. Rich countries, for their part, promised to deliver more and more effective aid, and to reform their trade policies to enable poor countries and people to earn their own way out of poverty.

The MDGs explicitly recognise that eradicating poverty can be achieved only if governments of both rich and poor countries live up to their promises. Terms for this ‘global deal’ were reaffirmed at the Financing for Development Summit in Monterrey in 2001 and at the 2005 UN Summit.

The developing countries have primary responsibility for achieving the first seven goals: to reduce poverty, to increase literacy, to improve health services and so on. But rich countries acknowledged in Goal 8 that poor countries cannot achieve the goals unless rich countries increase and improve the effectiveness of aid and change the rules of trade to foster development.

From a global perspective, progress in achieving the goals is promising: a significant number of countries are in the process of achieving at least partially the objectives set by the goals, while some countries in East Asia and Latin America are actually surpassing the objectives set. On current trends, the first goal, regarding poverty, will be met at the global level by 2015. This would be a striking success, even if this good progress at the global level largely reflects progress in the populous countries of India and China. Progress on the second goal (education) has also been good, even if not sufficient.

However, there are some targets on which we are lagging seriously behind and the worst of these concerns child mortality. Moreover, the situation in sub-Saharan Africa is particularly worrisome. If current trends continue, this continent, on average, will not achieve the goals for another century. But even here, some of the poorest countries are on track for achievement of several goals. Success stories can simply be explained as cases where the global compact has been implemented. The government concerned has reasonably good policies and rich countries have been relatively generous and helpful with aid and debt relief, backing their poverty reduction strategies.

So the global deal can work … if both parties live up to their commitments.

Achievement of the Millennium Goals will not happen unless developing country governments take full responsibility for their actions and their governments work properly.

Responsibilities of developing countries

As the primary responsibility is with developing countries, let me first focus on their part in the ‘global deal’. Achievement of the Millennium Goals will not happen unless developing country governments take full responsibility for their actions and their governments work properly. Even in the most aid-dependent countries, aid is a minor part of overall development finance. The way a country spends its own resources is much more relevant for the achievement of the goals.
Given the wide diversity between countries, there is no one-size-fits-all recipe, and priorities have to be set locally. But the following issues, on which even the poorest country can improve its performance, are key.

**The budget**
Accountable, transparent and effective management of public financial resources is critical. According to recent World Bank estimates approximately five per cent of global GDP still disappears through corruption and mismanagement. This figure is much higher in developing countries that are lagging in achieving the goals.

The goals need to be reflected in the Poverty Reduction Strategies or National Development Plans and these, in turn should be aligned with the budget process. In too many developing countries public spending actually benefits primarily the rich not the poor. If the MDGs are to be achieved, policies need to be pro-poor, gender-sensitive, as well as allow for sufficient public expenditures for basic social services.

Public finance is not just about expenditures. It is also important to maximise revenues, e.g. by fair tax legislation and effective tax collection. Domestic revenue mobilisation is the only sustainable long-term option for financing development. Resource-rich countries need to maximise the revenues they obtain from the exploitation of their exhaustible natural resources. An important step they could take in that direction is to join the Extractive Industry Transparency Initiative (EITI), ensuring disclosure of all revenues from multinational mining operations.

**Sectoral policies**
Sectoral policies need to be translated into effective service delivery (in health, education, sanitation, water, etc.) for all citizens all over the country. It is also important to ensure that all policies (including trade and tax), do not discriminate against the rural poor and that the government invests enough in rural development. Small farmers need support to get access to credit and markets. And we must not forget that trade policies need to be sufficiently pro-poor. In some developing countries protective trade barriers in fact protect the rich, at the expense of the poor.

**Legislation**
In many developing countries inheritance, property and tax laws urgently need to be reviewed to ensure women can fully participate and contribute to development. Also, in order for poor people to lift themselves out of poverty by unleashing their entrepreneurial spirit, legal reform is needed to improve the business climate particularly for domestic investors. In many developing countries the volume of capital flight is actually larger than that of aid received.

**Governance**
Last but not least is the cross-cutting issue of improved governance to create the capable state needed to achieve the Millennium Development Goals. Action is required to improve the quality and efficiency of the public sector:

- **By modernising and reforming the bureaucracy**
- **By decentralisation through empowerment of local authorities, and**
- **By ensuring that political processes are inclusive, not just politically representative through elected parliaments.**

Robust public participation is also a requirement, through the media and civil society, particularly groups that give voice to minorities and women that are at risk of missing the goals. Experience has shown that the greatest success stories are where the Millennium Goals have been debated, adapted, and owned locally. This means that they have become part of a national vision for 2015, not just by the government but by the public at large. Only then can the goals be successfully integrated into national plans, poverty reduction strategies, sectoral policies and national and sub-national budgets; only then can they be successfully mainstreamed into the sinews of government at every level, ensuring that all resources (human and financial, external and domestic) can be mobilised and invested in achieving the goals.

The ultimate test of course is for these policies and plans to be translated into real services and benefits at the local level. Active participation of citizens and their organisations at both the planning and implementation stages can help to ensure transparent and accountable government mechanisms that are responsive to the needs of all sections of the population. Only then can corruption be effectively fought and the huge ‘integrity dividend’ be redeployed for achievement of the goals.

**Responsibilities of rich countries**
Now to focus on what the ‘global deal’ implies for the rich (OECD) members of the Commonwealth – the UK, Canada, Australia and New Zealand – and on the progress made by these countries, as reported by the OECD/DAC.

**Quantity of aid**
While Official Development Assistance (ODA) trends have improved, the reality remains that ODA levels still fall short of the 0.7 per cent of GNI promised by most countries. In 2006 Australia (0.30 per cent), Canada (0.30 per cent), New Zealand (0.27 per cent) were all well below the average donor country effort (0.47 per cent). These countries have also failed to set a deadline, supported by planned annual ODA increases, to achieve the 0.7 per cent. The UK, the world’s second largest donor (after the US), promised to do so by 2013, and achieved 0.52 per cent in 2006.

In absolute terms, Canada gives less aid than Sweden, a much smaller economy; New Zealand’s aid is smaller than that of tiny Luxembourg and Australia – a huge continent – gives about as much aid as Belgium or Denmark. All are modest players in the international donor community.

**Quality of aid**
Increasing the effectiveness of aid is as important as ODA volume. In 2005, in his report *In Larger Freedom,*
Kofi Annan urged donors to de-link aid from their geopolitical agendas, which divert aid from poor countries that need external concessional resources. The UK, Australia and New Zealand have a strong focus on low-income countries. However, Canada lacks focus on the poorest countries. While it pledged that half of its ODA increases would benefit sub-Saharan Africa, for years to come Canada will continue to be a small donor there.

Both Canadian and Australian aid are quite supply-driven, while Canada’s aid programme is one of the most widely dispersed; as a result Canada has no critical mass of assistance in any recipient country.

**Trade**

International trade has a tremendous potential to reduce poverty worldwide. But present trade policies discriminate against developing countries. Despite significant liberalisation in recent decades, trade barriers are still high – especially on labour-intensive goods and services in which developing countries have a comparative advantage. Reducing these is essential for developing countries to trade their way out of poverty.

The most trade-distorting policies are in the agriculture sector. As two-thirds of the world’s poor live in rural areas and depend on agriculture, putting an end to the distortion of international and local agriculture markets is a crucial ingredient to achieve the first Millennium Development Goal.

Among rich countries, the European Union is the worst offender on this issue. While the UK has for years made strong statements about the need to eliminate these subsidies it has not been very successful in convincing the rest of the EU membership. Australia and New Zealand actively fight EU agriculture protectionism. Canada should take a more proactive approach in analysing the impact on developing countries of its non-aid policies such as trade and agriculture.

**Conclusion**

The MDGs are still achievable if we break with ‘business as usual’ and dramatically accelerate and scale up action.

At the halfway mark to 2015, it is late, but not too late for countries to reconcile rhetoric with action. But as the United Nations Secretaries-General (both Kofi Annan and Ban Ki-Moon) have repeatedly stated, when talking about the Millennium Goals: “The lacking ingredient is political will.” The Millennium Goals will not be achieved at the United Nations. We at the UN can create a platform for governments to make commitments but we cannot force compliance by our member states. Only their citizens and parliaments can hold governments to account.

Let me conclude with quoting Ghandi: “the difference between what we do and what we are capable of doing would suffice to solve most of the world’s problems.”

Governments around the world are perfectly capable of acting to close the glaring gap between commitment and delivery: in fact many of them are doing so. We are the first generation that can put an end to poverty and should simply refuse to lose this opportunity.

**Eveline Herfkens** In October 2002, then UN Secretary-General, Kofi Annan, appointed Eveline Herfkens as the Executive Coordinator for the Millennium Development Goals Campaign. Prior to this appointment, Ms. Herfkens served as the Netherlands Minister for Development Cooperation (between 1998 and 2002). During this time, she was also a Member of the World Bank and IMF Development Committee and a Co-founder of the Ustinen-Group. Ms. Herfkens served as Ambassador/Permanent Representative of the Netherlands at the United Nations and other international organizations—including the World Trade Organization (WTO)—in Geneva (between 1996 and 1998). Ms. Herfkens was an Executive Director of the World Bank Group in Washington D.C. (between 1990 and 1996). Ms. Herfkens was a Member of Parliament in the Netherlands (between 1981 and 1990).

The Millennium Campaign, launched in 2002, informs, inspires and encourages people’s involvement and action for the realization of the Millennium Development Goals. An initiative of the United Nations, the Campaign supports citizens’ efforts to hold their government to account for the Millennium promise.

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**The Paris Declaration**

The impact of foreign aid is too often weakened because it is delivered by many high-cost small individual bilateral programmes, governed by multiple and complex requirements. The good news is that, at the OECD, donors acknowledged they were part of the problem and promised in the Paris Declaration agreed in the Spring of 2005 to become part of the solution. They committed:

- To respect home-grown developing country strategies
- To align donor support to these strategies
- To work together to coordinate and harmonise procedures, and
- To do away with individual projects, evaluations and missions.

The UK played a leading role in forging this international consensus.
The goal of reducing maternal mortality (Millennium Development Goal No 5) will not be met unless resources are urgently focused on where they will make the biggest difference: ensuring all women deliver with a health professional. Such skilled care will be most cost-effective when provided in a functioning health facility, and must reach the poorest women. The authors make the case for this strategy, and highlight the importance both of addressing human resource and financial barriers, and of robust monitoring and evaluation of inputs, processes and health gain. Failing to achieve MDG 5 will be a collective disgrace – for both rich and poor countries. This paper emphasises both what must be implemented now to reduce maternal mortality based on current knowledge, and the need to address gaps in evidence and genuine dilemmas in health policy and programme decision-making.

Stopping women dying during childbirth: how are the Commonwealth countries doing?

The Commonwealth Finance Ministers Meeting 2007

Oona M R Campbell, London School of Hygiene and Tropical Medicine and Wendy J Graham, University of Aberdeen

Each year over 565,000 women die during pregnancy or childbirth worldwide; 52 per cent occur in the Commonwealth states. Globally, the disparity in the risk of these maternal deaths between rich and poor countries is one of the largest of all public health indicators: for example, one in six women in Sierra Leone die of these causes compared to one in 3,800 in the UK. Maternal deaths are, however, only the tip of the iceberg of suffering related to difficult pregnancies. Maternal ill-health is the largest contributor to the burden of disease among women of reproductive age, and when maternal and perinatal conditions are combined, the burden is larger than for HIV/AIDS, malaria, or tuberculosis (Figure 1). If a mother dies or has a debilitating complication, the survival and wellbeing of her children are also compromised, the family may disintegrate, and there are economic consequences for the household, community and society.

The Fifth Millennium Development Goal (MDG 5) is to ‘improve maternal health’, judged by two main targets for 2015: a 75 per cent reduction in maternal mortality and universal coverage of deliveries by health professionals (namely midwives, nurses or doctors). But recent assessments show disappointing progress since 1990, with just five low-income countries (including India and Nigeria in the Commonwealth) accounting for half the deaths in the world each year. 2007 is the 20th anniversary year of the Safe Motherhood Initiative. The fact that MDG 5 is so far off track is receiving heightened attention and seen as deplorable given that some countries, including three Commonwealth states, have essentially eliminated these tragic deaths (see Figure 2 overleaf). So why do women still die during pregnancy and childbirth?

We know what to do to prevent maternal deaths; it’s just not being done

When it comes to maternal mortality, we know what works. A recent series of the Lancet journal argued that strategies to reduce pregnancy-related deaths can be among the most successful efforts to target a specific cause of death. Of course saying we know what works epitomises the ‘advocacy of optimism’ essential to maintaining the commitment of politicians, including finance ministers, donors, UN agencies, and professional bodies. Having agreed that saving women’s lives is essential, only a few key strategic decisions need to be made. These choices are now being driven and encouraged by the shift by donors to results-based financing, with maternal mortality reduction widely-regarded as a ‘prized’ result. The priority is to persuade and support key government decision-makers, including finance ministers, to make a real difference to the lives of women and babies through focused, effective intervention.

Figure 1. Contribution to global burden of disease, 2005.
strategies. We identify where the Commonwealth states stand with respect to implementing these key strategies and highlight lessons to be learnt.

**Key strategies and lessons for the future**

**Women are at particular risk during delivery: this is the crucial time for effective care**

The risk of maternal death is highest during labour, delivery and the first 24 hours after delivery (what is called the intrapartum period). Where women are when they deliver, who is attending them, and how quickly women can be transported to referral level care determines the interventions that are needed and feasible.

There are efficacious drugs or procedures for preventing or treating virtually all life-threatening maternal complications, and their costs are affordable. Strategies aim to bring together packages of interventions and direct these to the target populations of women who need them. A ‘best bet’ strategy is one that includes an effective package of interventions, a service delivery platform that can achieve high coverage of the intended target group, and is acceptable to populations and governments and thus likely to be sustained.

The ‘best bet’ strategy must target all deliveries – both normal and complicated

Current evidence shows that the ‘best’ intrapartum care strategy enables women to routinely deliver in a health centre, private clinic or maternity home, with midwives as the principal providers but with other attendants also working with them in a team. Such health centre-based care can cater to normal births but also includes basic emergency care for managing complications. More advanced treatments, such as blood transfusions or caesarean sections must be readily available at the referral level (district hospital). Two recent cost-effectiveness analyses found health centre-based care to be among the most cost-effective options, with clear benefits to both mother and baby. Ensuring such facilities are close enough for women to deliver in should also mean women are close enough to seek care if complications arise before or after delivery.

**Worldwide less than half of all deliveries occur with a health professional present**

Figure 3 shows the percentages of deliveries with health professionals in Commonwealth countries. This indicates that many states, especially those with low levels of maternal mortality, already meet the goal of universal coverage. Most have achieved this complete coverage by institutionalising births. For those who have not, scaling up deliveries with health professionals in facilities, while simultaneously ensuring access to referral level care, presents a huge challenge, requiring a 24-hour service, which is often not currently available. Furthermore, reviews of the preparedness of various tiers of the health system show that health centres are the level that most often fails to meet service and quality requirements, and thus urgently requires further investment.

**Two key bottlenecks to scaling up delivery care are skilled professionals and financing**

Among the biggest challenges facing poor countries in providing the ‘best bet’ strategy described above are...
adequate provision and deployment of skilled providers, and financing. There are massive human resource constraints in many countries, especially in rural areas. Some of these can be addressed by staffing combinations whereby, for example, midwives work in teams supported by staff with less competences.

Financial barriers widen the poor-rich gap in access to delivery care and in maternal mortality

There is strong evidence for a wide and widening gap between poor and rich women in delivery with a health professional, access to caesarean section, and the risk of maternal death. In Tanzania, for example, the poorest women have a three-four times higher risk of death. Universal access to skilled delivery is a barometer measure for MDG 5, and key to achieving equity in maternal health. Uptake indicators must, however, be tracked and evaluated alongside markers of the quality of care received, and the health gain achieved – for mothers and babies.

There are various global price tags for scaling-up maternal and newborn services to achieve universal coverage. Although these vary according to model assumptions, the additional budget needed from governments and donors is in the range of US$5.1 billion to $6.1 billion per year by 2015 for 75 priority countries. But the potential gains from scaling up are enormous: maternal deaths could be halved by 2015, at an extra cost to country health budgets of between US$0.22 to $1.18 per capita. In many low-income countries, households continue to pay a disproportionate share of the costs for accessing government maternity services, particularly for emergencies. For the poorest families these costs can be catastrophic. There is now strong evidence to support removing user fees for delivery care. For such initiatives to succeed, governments must replenish the income lost from the removal of user fees, address the supply side barriers, especially related to staff and quality of care, and implement effective mechanisms to ensure increased demand from the poorest women, such as cash transfers or vouchers, and transport subsidies.

Delivery care is the priority, but other complementary strategies must also be in place

Mention should be made of three complementary strategies which reduce the risks of maternal death outside the intrapartum period – antenatal care, family planning and abortion services. Antenatal care provides benefits in terms of neonatal survival and maternal health, but the potential to impact significantly on maternal mortality is limited. In some countries, investment in antenatal services needs to be balanced against the requirement to expand delivery care, and should focus on providing only those interventions which are effective, such as antimalarial prophylaxis. The patterns of uptake of antenatal services in Commonwealth countries are shown in Figure 4 (overleaf). A woman who is neither pregnant nor recently delivered cannot die of maternal causes. Avoiding unwanted pregnancy through family planning services is thus an extremely effective form of primary prevention of maternal deaths. And finally, unsafe abortion is a major cause of maternal mortality in some countries, yet when conducted in a safe environment, induced abortion is less risky than childbirth. Were it not for legal, political and cultural constraints, medical abortions could potentially be available at a household level and attain high coverage, thereby averting a substantial proportion of maternal deaths; abortion policies around the world can be seen at http://www.un.org/esa/population/Publications/2007_Abortion_Policies_Chart/2007AbortionPolicies_wallchart.htm.

Demonstrating progress is crucial for all strategies: what you count is what you do

Monitoring key indicators is essential to planning programmes, determining inputs, redressing deficiencies and assessing outcomes. Our graphs illustrate the status of Commonwealth countries with respect to a few key indicators, and also show that many countries have no data. For example, in international databases, Grenada and Tuvalu have no estimates of maternal mortality; the UK, Canada and Malta lack data on antenatal care; Cyprus and Brunei lack data on contraceptive prevalence; and the Seychelles have no data on the proportion of deliveries with health professionals.
Investment is needed in routine information systems and all opportunities seized for measuring maternal mortality, such as the 2010 round of Decennial Censuses. Among the Commonwealth States there are many examples of good practice in information gathering. For example, India has long had a sample registration scheme which is used to provide vital statistics, and has recently produced estimates of maternal mortality. Jamaica has a series of high-quality studies of the levels and cause of maternal mortality which have informed their national programmes. The UK Confidential Enquiry into Maternal Deaths has over 50 years of experience investigating quality of care through in-depth reviews, and has served as a model for similar processes in other countries, such as South Africa and Malaysia.

Ministers of Finance have always had a pivotal role to play in maternal mortality reduction

Ministers of Finance have the unenviable role of balancing budgets across sectors, so needing to take a multi-sectoral perspective to development. Maternal mortality reduction is much more than a medical issue, and depend also in the long term on progress in other sectors, such as transport or education. At the same time, delivering improved maternal health through the health sector has benefits for other health conditions and for wider development – reducing inequities and promoting women’s rights.

The time has come to focus resources where they will make the biggest difference to the lives of women, babies, families and societies. Intrapartum care represents the greatest opportunity to achieve this impact. Universal access to effective delivery care must be achieved using strategies which also maintain women’s choices and dignity. This should be the right of all women. None of us would want our daughters or sisters to deliver without someone who can manage complications and help ensure a healthy outcome for mother and baby. When countries are held to account for progress on MDG 5, and as results-based financing becomes the main mechanism for receiving external assistance, all ministers will wish and need to show that care at the time of delivery is safe and appropriate, particularly for the poor. The burden of mortality is highest among the poorest women, yet their access to care is weakest. MDG 5 cannot be met without addressing this fundamental inequity.

There is a pressing need for ‘vision’. In signing-up for MDG 5, countries have indicated their aspiration. The aspiration is meaningless unless it is translated into a clear strategy for achieving this. The Commonwealth countries cover the whole spectrum of challenges and strategies seen globally. There are many examples of good practice and innovation within this community, and unique opportunities to learn from each other. There is no time to delay – share, learn, and prioritise delivery care.

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The London School of Hygiene & Tropical Medicine is Britain’s national school of public health and a leading postgraduate institution in Europe for public health and tropical medicine.

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Laboratory Specialist Services (LSS) has been under current ownership since 1994 – when South Africa became a true democracy as trade sanctions were withdrawn and the gates to international trade opened up. It was an opportune time to engage with global leaders in the field of Molecular and Cell Biology and LSS were successfully appointed the exclusive Southern Africa distributors for a number of international manufacturers.

In 2005 LSS were contacted by the global leader in the manufacture and supply of UN-compliant packaging solutions. Through intensive market research amongst our existing clients, a substantial demand for UN-compliant products was identified. As most Southern African countries receive limited government funding, LSS devised a way for scientists to be compliant in their packaging at an affordable price.

Together with a respected Research and Development company, LSS designed a light-weight, rigid outer container, available in two sizes, validated according to UN Regulations. The rigid outer container is polyurathane-lined for temperature control. It is designed to withstand rugged handling, can be cleaned for re-use and is supplied with all the required and regulated labelling as a standard feature. This rigid outer box becomes part of the required 3-layer packaging system, which brings about significant savings, as an over-pack is no longer needed.

In 2007 the UN regulations were amended, requiring the secondary layer of packaging to be leak-proof. This had an enormous impact on the packaging cost as currently used “jiffy” bags were not leak-proof. Once again, LSS thought outside the box, and applied lateral thinking to solve the problem. The solution: a leak-proof 95kPa Pot, which acts as the second layer of packaging.

Without changing standard operating procedures, medical technicians could simply pop the “jiffy” bag into the 95kPa Pot, supplied with the boxes, and remain compliant at a limited additional cost.

Prior to LSS intervention, pathology packaging was used on a once-off basis, and discarded. This problem was discussed with Onderstepoort Veterinary Research Institute (OVI) (Sub-Sahara Africa’s major veterinarian institute) in Pretoria, who arranged with the relevant courier companies to return the light-weight packaging at a most inexpensive rate. Apart from the “jiffy” bags, all their packaging became re-usable and therefore affordable. This strategy has proved most successful and made it possible for veterinarians, as well as human and forensic pathologists throughout SA to be compliant with the UN Regulations for the transport of pathology samples.

A practical PowerPoint presentation is available in South Africa, demonstrating how the regulation systems work, as well as showcasing our innovative range of products.

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Laboratory Specialist Services
COMPLETING THE SERVICE CIRCLE
In 2000 HIV/AIDS was placed firmly on the global agenda with UN Security Council Resolution 1308. This recognised that “the spread of HIV/AIDS can have a uniquely devastating impact on all sectors and levels of society.” A year later, in July 2001, there was a UN General Assembly Special Session on HIV/AIDS. Since then our understanding of the epidemic and its potential impacts has deepened, and changed. AIDS will not be a major problem in some countries, and it is time to recognise this. But, where it is a concern, it is a development issue to be considered by all sectors of government, especially the Ministers of Finance.

Early fears that the disease would spread rapidly outside Africa have been shown not to be the case. In India, for example, it was estimated in the UNAIDS 2006 Report on the global AIDS epidemic that there were 5.7 million people living with HIV. In July 2007 this was revised downward to 2.5 million. This is not to underestimate the individual tragedy of each infection, but rather to suggest there are some areas where AIDS will have a considerable impact and others where its importance can be downgraded, although surveillance must be maintained.

Globally, those countries hardest hit by HIV/AIDS are both in southern Africa, and member states of the Commonwealth. Life expectancy in these countries has plummeted and the health sector is particularly adversely affected. This will slow or halt development. Ministries of Finance, which focus their energies on macroeconomic issues, may not fully appreciate the extent of impact or the long-term implications of the loss in human capital. This article draws attention to such issues, encouraging better planning to avert the consequences of this preventable disease.

There are some areas where AIDS will have a considerable impact and others where its importance can be downgraded, although surveillance must be maintained.

Globally those countries hardest hit are southern Africa Commonwealth member states. These are shown on the map in Figure 1, the so-called ‘red’ countries. According to UNAIDS, adult HIV prevalence exceeds 20 per cent in four of these countries: Swaziland, Lesotho, Botswana and Zimbabwe. It is between 10 and 20 per cent in South Africa, Namibia, Zambia, Mozambique, and Malawi. It is these countries that are the focus of this article. We would note that Caribbean commonwealth countries and Papua New Guinea need to be monitored as the levels of infection here are higher than in other countries in their respective regions.

Research has thus far failed to explain why southern Africa has been so hard hit by HIV/AIDS. However, socio-economic variables, cultural factors and sexual behaviour all play some role. Poverty, income inequality, gender inequity, long-term concurrent partnerships, the lack of male circumcision, and the prevalence of co-infections are factors that come under the spotlight. What they highlight is that there are no easy solutions to curbing the spread of the epidemic. There are countries, outside southern Africa, where the HIV appears to be under control: Uganda brought early hope to Africa by...
showing how high levels of political commitment can work to stabilise HIV prevalence. In other locations, such as Tanzania, the peak of prevalence is much lower for reasons that are not fully understood.

This article focuses on the data and what it means for the health sector and development more broadly. It is a call for a realistic look at AIDS in the worst affected countries.

Epidemiological basis for understanding impact

In southern Africa, the first AIDS cases were detected in the mid-1980s and prevalence continued on an upward trajectory into this decade, as shown in Figure 2. Zimbabwe and Botswana registered a peak in HIV prevalence around 2001. One by one, other countries have followed suit. The turn around in HIV prevalence is due to natural progression and (we hope) to the influence of prevention and treatment initiatives.

Our best source of information for tracking the spread of the epidemic is HIV prevalence, testing amongst women attending antenatal clinics. Its disadvantage is that it captures a very specific population – sexually active females who access public antenatal care – who may be at higher risk of infection.

Given the long wave nature of epidemic and the time lags between HIV infection, AIDS illness and death, the stabilisation in prevalence rates is little consolation when considering impact. The number of deaths and rate of orphaning will increase for years to come. HIV/AIDS impact will get progressively more intense unless significant numbers of people are treated.

Impact of HIV/AIDS on the health sector

Established by World Health Organization (WHO), the 2001 Commission on Macroeconomics and Health report highlighted the importance of health as an investment for economic development. It estimated a 10 per cent improvement in life expectancy would be associated with a rise in economic growth of 0.3-0.4 per cent. HIV/AIDS is having a dramatic impact on life expectancy. The 2006 UNDP Human Development Report data from 1970-75 and 2000-2005 is reproduced in Table 1 below. It is striking how much life expectancy has fallen (the exception being Mozambique, which started from a low base). Development – economic, social and political – would, in the absence of HIV/AIDS, have meant life expectancy should have risen to the mid 60s.

AIDS further ravages the health sector, so reducing its ability to provide essential health services. Given the importance of health, both in its own right and as an input for economic growth, a fundamental objective of governments in the context of HIV/AIDS should be to maintain and improve the quality and reach of health services. The impact of HIV/AIDS on the health sector is a double-edged sword: the demand for healthcare is increasing, while the capacity to deliver services is being eroded. The two dimensions of the problem need, urgently, to be understood and addressed.

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HIV/AIDS is placing huge demands on health services in the countries of southern Africa. As early as 1995, Kara Hansen and others writing about the costs of HIV/AIDS care at government hospitals in Zimbabwe in Health Policy and Planning (2000) estimated 50 per cent of adult medical inpatients in a selection of Zimbabwean hospitals were HIV positive. By 1998, studies in South African and Swazi hospitals were demonstrating similarly high figures. Although alarming, these figures are not a true measure of the demand for care, since not all sick people access care or believe in the value of Western medical intervention. HIV/AIDS is a complex illness to manage; in the late 1990s in Zimbabwe, Hansen showed the costs of treating HIV positive patients was almost twice those of those who were HIV negative.

A particular concern is attrition of healthcare workers due to HIV/AIDS, the extent of which has not been consistent across countries.

While the economic burden of escalating healthcare demands as a result of HIV/AIDS is often acknowledged, additional costs associated with ensuring the supply of healthcare are not. A particular concern is attrition of healthcare workers due to HIV/AIDS, the extent of which has not been consistent across countries. In some Commonwealth countries, such as Zambia, Malawi and Uganda, AIDS-related deaths have been identified as a major factor contributing to staff shortages. In Zambia, a 2006 editorial in The Lancet by Rich Feeley calculated that deaths alone could account for a nurse vacancy rate of 37 per cent. In South Africa and Swaziland, on the other hand, health worker attrition as a result of death has generally been less of a threat than expected given the stage of the epidemic that we are in. Nonetheless, the costs are huge. Almost a whole year of nursing time is lost each time a nurse succumbs, including time taken off work due to illness and the time needed to retrain a replacement, all of which ultimately has to be funded by the state. In Malawi work published by Muula and colleagues in 2006 estimated it to cost US$31,726 to train a nursing sister, with a lost investment of between US$241,508 (seven per cent interest rate per annum for 30 years) and US$25.6 million (25 per cent interest rate per annum for 30 years) for each nursing sister leaving service.

The number of people with AIDS in southern African countries will continue to increase, with these people requiring care. While there is hope of a decrease in opportunistic infections as more people are put on antiretrovirals (ARVs), these drugs are still enormously expensive and will only ever buy time. On first line ARVs, people can expect at least four extra years. The cost, we have heard, for drugs alone is US$94 per person per annum. We believe it will be closer to US$250 with tests, personnel and health facilities. Furthermore, in many African countries the point has not yet been reached where a real difference can be seen as a result of treatment. Médecins Sans Frontières (MSF) recently outlined the low ARV coverage rates in countries where they work: 50 per cent in Malawi, 16 per cent in Mozambique, 27 per cent in South Africa and 31 per cent in Lesotho. The bottom line is that if health systems did in fact provide care to all in need, then the demands (and costs) would be huge. However, they don’t, and sadly there are a number of disincentives for health systems to respond appropriately to the demands of the epidemic. Most obviously, if people can’t access care, then they don’t place any burden on health services. Similarly, if the quality of care provided is sub-optimal, then the costs of treatment to the provider will be lower and people will seek care less readily.

In summary, the economic costs associated with simply maintaining the functioning of a sector such as health in the context of HIV/AIDS can be huge and yet failure to do so would be of grave detriment to economic growth.

Long-term economic costs

At the household level the economic costs of HIV/AIDS are undisputed. The 2006 reviews of the socio-economic status of AIDS-affected households by Barnett and Whiteside have unanimously shown the direct relationship between households affected by HIV/AIDS and subsequent impoverishment. The changes in income and expenditure patterns include:

• A greater share of household resources consumed by medical and funeral expenses
• Less money spent on food and other regular expenditure items, and
• Less money spent on education.

The catastrophic levels of healthcare expenditure in AIDS-affected households are of great concern. When a household’s income diminishes as a result of illness there is the potential for a cycle of decline that, in the worst case, results in dissolution.

So how does the impact of HIV/AIDS on individuals, households, and sectors reflect on macroeconomic growth? This is the bread and butter of the Ministries of Finance and Central Banks. The short answer is that it doesn’t, at least not the ways we originally anticipated. Early in the epidemic models suggested AIDS meant economic growth rates would be 0.56–1.47 per cent lower. An Africa-wide estimate was that in the 1990s growth was reduced by 0.8 per cent.

Set against this are data from individual countries. Uganda had the worst epidemic in the world yet managed consistent economic growth estimated at 6.5 per cent per annum from 1991 to 2002. Botswana’s growth rate over the same period was 5.6 per cent. South Africa has seen steady growth for the past five years. In 2007 after spending 20 years of watching the epidemic develop we are forced to conclude that macroeconomic impacts are hard to find.
The reason may be largely because of ‘second-order effects’, resulting from the ways in which firms and government sectors respond to first-order impacts of HIV/AIDS. This is well described by Professor Nicoli Nattrass of the University of Cape Town. These effects are difficult to predict, since they depend on specific decisions taken by private and public sector economic actors. For example, firms may increase their reliance on casual labour to avoid having to pay for escalating staff medical costs. In government departments work may simply not get done. Slow processes of adaptation mean that individuals and households are often left worse off, so that the economic functioning of firms and government sectors is preserved in the short term.

More recent studies have moved beyond such immediate effects to account for other factors related to social development and social welfare, including the indirect and intergenerational effects of the epidemic on related indicators. These studies project the long-run economic costs of HIV/AIDS could be much higher. Failure to implement aggressive policies to preserve the mechanisms that generate human capital formation across generations could, according to the most dire predictions, result in economic collapse. This is the message the Ministers of Finance need to hear, but it is not clear who can give it.

In 2007 after spending 20 years of watching the epidemic develop we are forced to conclude that macroeconomic impacts are hard to find.

Predictions of macroeconomic growth are based on a series of assumptions and it is easy to get caught up in debates on the merits and pitfalls of these, so losing sight of some of the key messages. These are:

1. HIV/AIDS impacts may be severe, but do not translate into an obvious impact on macroeconomic growth.
2. The issue of human capital is one which may well define the degree of HIV/AIDS impact on macroeconomic growth. Interventions such as antiretroviral therapy, which preserve this, can go a long way towards buffering such impact.
3. Projections do not highlight the way in which different sectors of the economy will be differentially affected by the epidemic.
4. Indicators which account for population trends, such as GDP per capita, are limited indicators of welfare.

Conclusions

The HIV/AIDS epidemic has not yet caused catastrophic economic and social collapse, although there are authors (Price-Smith and Daly) who have suggested it might be implicated in the dire predicament Zimbabwe faces. That however does not mean Finance Ministers should ignore it. From a human development point of view it is catastrophic, as we have shown. This alone will have macroeconomic effects. Averting the impact requires putting people on ARVs. This may be financially manageable in a few countries, but at the end of the day will require donor support in the long term. This means that the Finance Ministers have a stake in seeing prevention measures that work. As we have also shown, already stressed health systems are under increasing pressure, and that is bad for everyone’s physical and economic health.

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The new University of KwaZulu-Natal unites two major educational institutions – the University of Natal and the University of Durban-Westville. The University of KwaZulu-Natal aims to be a truly South African university that reflects the society in which it is situated, not only in terms of race, gender and class, but in terms of how it structures its values and priorities and how it responds to social needs.

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Further reading on HIV/AIDS


“In Africa, Oddly, Animal World Is Terra Incognita.” So read a heading in the New York Times of an article by marc Lacey, and those of us who have the privilege of working closely with African learners unfortunately can testify to the truth of this statement. Environmental literacy is a key concern in any emerging democracy, equipping citizens with the ability to make informed choices and no conservation effort can be successful without the support of all a country’s population.

Cheetah Outreach was well placed to take up this challenge and integrate a conservation message into key learning outcomes of the national education curriculum in South Africa. Natural Science was selected as a close link. A team of teachers from different communities in the Western Cape Province set about developing an activity-based resource including strong life orientation, literacy and numeracy outcomes. Facilitated by the education officer of Cheetah Outreach, this team brought years of experience and cultural richness to the process as well as keeping the delivery practical and easily accessible to all schools.

After two years of trial and error, what emerged was the AAWARE (Animal Awareness for World and Regional Education) Teacher Resource, supported by large colourful information posters ready for presentation to the curriculum advisor of the Western Cape Education Department. After piloting in a variety of schools the resource was translated into Afrikaans and Xhosa to serve schools of the Western Cape Province.

Next came delivery. Teachers were workshopped to demonstrate and train. After a further two years all primary schools in the province were resourced. A partnership with the De Wildt Cheetah and Wildlife Trust started delivery into a further three provinces and another language was added.

Today, AAWARE has crossed the borders into Botswana where it is delivered by the Cheetah Conservation Botswana and Namibia, where it forms the basis of the Cheetah Conservation Fund’s teacher’s resource. Skilling learners in natural science, it also stimulates pride in our natural wildlife heritage and plants the seed of a conservation ethic.

Auckland Zoo, New Zealand, Australia Zoo, Australia and the Angel Fund, Cincinnati Zoo, USA all support with funding. Uniting continents, this programme is testament to what can be achieved by partnerships.

In Southern Africa “Animal World is Terra Incognita” no more.

CHEETAH OUTREACH: www.cheetah.co.za - cheetah@intekom.co.za
Abolishing school fees and maintaining quality: are the two compatible?

Dzingai Mutumbuka
Chair, the Association for the Development of Education in Africa (ADEA)

Recent years have seen an encouraging decline in the number of children out of school, both worldwide and in Africa. In 2004, 77 million children were not enrolled in school (of which 38 million were African, as compared to 98 million in 1999 (of which 43 million were African). The most remarkable progress has been observed in those countries that have taken bold measures to reduce or completely abolish school fees and other direct and indirect costs. However country experiences in school fee abolition raise questions about the impact on education quality. In this article, the author outlines the main challenges as well as innovative strategies being developed by countries to ensure that access to education for all is addressed without compromising quality.

School fees are a significant barrier in the expansion of schooling. There is plenty of evidence showing that they are a major obstacle preventing children from the poorest families from accessing and completing quality basic education. Countries that have taken the bold step to eliminate school fees have witnessed dramatic and rapid increases in enrolment rates. In sub-Saharan Africa, for example, primary school enrolment grew from 3.4 million to 5.7 million (+67 per cent) in Uganda in 1996, from 5.9 million to 7.2 million (+22 per cent) in Kenya in 2003, and from 1.5 million to 3 million (+100 per cent) in Tanzania in 2003. Less impressive, albeit remarkable, increases in enrolment have also been observed in Lesotho (+11 per cent in 2001), in Mozambique (+12 per cent in 2005) and in Ghana (+14 per cent in 2006).

No child should be prevented from going to school because of financial reasons

Acknowledging that school fees are a major barrier to access and that school fee abolition may be the single most important policy measure to trigger a drastic increase in school enrolments prompted UNICEF and the World Bank to launch the School Fees Abolition Initiative (SFAI) in 2005, subsequently joined by ADEA and other development partners. The main goal of the initiative is to mobilise support within a context in which no child is excluded from access to education because of financial reasons. The initiative aims to make dramatic improvements in access to good quality basic education by supporting policies aimed at addressing the cost barriers to education faced by households and families. School fees consist of a broad range of costs – in addition to tuition fees – and may include the costs of textbooks, stationery, uniforms, PTA contributions, costs related to sports and other school activities, transport costs, contributions to teachers’ salaries (especially in some community schools located in rural areas), opportunity costs and other burdens on poor families.

SFAI has three objectives:

• To establish a knowledge base and network for the abolition of school fees
• To use this knowledge base to assist, guide and support countries in planning and engaging in sound and sustainable school fee abolition processes
• To facilitate, promote and advance the global dialogue on financial obstacles to access to education.

A first meeting was organised by UNICEF and the World Bank in Nairobi, in April 2006, focusing on lessons learned from school fee abolition in sub-Saharan Africa. In 2007, ADEA, UNICEF and the World Bank organised a meeting in Bamako, June 19–22, which tackled the main challenges facing countries that have engaged in the school fee abolition processes (see Box overleaf). The main challenges are two: maintaining quality while at the same time admitting more children to school; and ensuring the long-term financial sustainability of school fee abolition initiatives. This article focuses mainly on the first challenge.
Quality is essential to avoid reversing hard-earned gains

Because the abolition of school fees entails a dramatic and sudden surges in enrolment, it is essential that steps to improve access are not taken at the expense of quality. Overcrowded classes and meagre resources that are no longer available because fees are abolished can reverse hard-earned gains and demotivate teachers, parents and students. While the challenge is great, experience from several countries shows that access and quality are not incompatible and can be addressed simultaneously. Two strategic areas affecting quality should be looked into and planned carefully:

• Meeting the demand for teachers, classrooms and school materials, and

• Empowering parents and schools through capitation grants.

Meeting the demand for teachers, classrooms and textbooks is the first challenge

When fees are removed, the greatest challenge is to provide the needed supply of teachers to cope with the surge, and then to give them adequate support and in-service training. This can be an opportunity for assessing how the existing teaching force is being used and how it may be drawn on more effectively before evaluating the need for new teachers. A number of countries have accommodated the enrolment surge by increasing the pupil/teacher ratio or class size, but such a strategy is often detrimental to student learning. Other options include the recruitment of unemployed upper secondary graduates, contract teachers, retired teachers and volunteers. However, planners will need to consider that the recruitment of these types of teachers will require intensive in-service training and support to ensure that quality is maintained. Other teacher-related strategies to deal with the surge include better management of school hours and of the school year, introduction of multiple shifts, in-service training on multi-grade teaching, innovative teaching and learning practices and providing accommodation for teachers, especially in remote rural areas.

As the teaching force increases, managing deployment also becomes a major challenge, which includes that of providing teachers in remote rural areas. Policies that link new teacher positions directly to schools are a way of addressing this challenge and ensuring at the same time that local communities have a greater say in teacher recruitment and are more involved in teaching issues. Community involvement affects quality as it is a key to supporting teachers and reducing absenteeism.

Finally, a factor that needs to be borne in mind when assessing the teaching force is the impact of HIV/AIDS on teacher absenteeism and depletion. Classroom construction and rehabilitation is a major quality challenge because construction and rehabilitation take time and are costly. Since few countries which have
abolished fees have medium- to long-term construction and rehabilitation plans, school buildings and furniture are continually deteriorating. Temporary strategies for providing enough classrooms include greater occupation of existing classrooms and making use of unoccupied locations and facilities. In the medium and long term, community-driven and locally-adapted construction and maintenance are cost-effective alternatives which are providing child-friendly and qualitative school environments.

Textbooks and other teaching and learning materials are some of the most cost-effective inputs for improving learning. It is therefore important to ensure an increased, timely and adequate supply of textbooks and materials as an immediate measure to address the quality concerns of school fee abolition. This can represent an opportunity for improving textbook policies and strengthening the procurement and distribution system. In some cases improving public/private partnerships and shifting textbook production to the private sector has proved successful.

Empowerment and information in the public domain are powerful tools

School fee abolition processes are also triggering reforms for more effective decentralised education management and finance systems. The transferring of fees between the central and local level and the utilisation of fees are being scrutinised in many countries and strategies are being developed to ensure a proper flow of resources to the schools.

In a number of countries, block or capitation grants have been introduced to replace the fees and revenue loss at the school level and have had a positive impact on both access and quality. This corroborates research conducted by ADEA within the framework of its exploration of the factors and conditions underlying quality that has stressed the importance of management systems that shift resources and accountability to the local level. Experiences with capitation or block grants to schools reveal several advantages: school grants are revitalising school committees and enhancing community participation in decisions about resource allocation and quality improvement; they are thereby strengthening the capacity of schools in planning and budgeting, procurement and management; and they are promoting local-level solutions, administrative efficiency and accountability.

The biggest challenge related to block and capitation grants is ensuring accountability. In Africa, Uganda’s, Tanzania’s and Kenya’s successful experiences are attributed to the setting up of two instruments:

• School committees composed of teachers and parents who have been trained by accounting firms to manage the grants
• The public disclosure of information on the management and use of the funds, which has been shown to be a most powerful instrument for ensuring effective accountability.

Abolishing school fees can spark off policies to improve quality

A number of countries, particularly African countries, will not be able to achieve Education for All and the MDGs unless bold policy measures are taken to address the education cost barriers. Strong political determination will be needed for such initiatives to be set in motion. However, in order to lead to success, political determination must be accompanied by rigorous planning, carefully laying out needs to be met and resources to be mobilised as well as considering the direct impacts on quality and learning achievement.

While well thought-out planning is needed, including planning for financial sustainability (not covered in this article), experience shows that school fee abolition initiatives can both increase access drastically and set off reforms that will restructure current systems and practices for the better and improve quality.

Dzingai Mutumbuka is currently Chair of the Association for the Development of Education in Africa (ADEA). He is also Sector Manager for Human Development at the World Bank, leading work in Eastern and Southern Africa. Before joining the World Bank in 1990, he served as Minister of Education in Zimbabwe between 1980 and 1989. Before that he participated in the liberation struggle for independence. He has contributed to building one of the best education systems in Africa.

The Association for the Development of Education in Africa (ADEA) was established at the initiative of the World Bank in 1988. Then called Donors to African Education (DAE), its objective was to foster collaboration and coordination between development agencies in support of education in Africa. ADEA now focuses on developing partnerships between Ministers of Education and funding agencies in order to promote effective education policies based on African leadership and ownership. ADEA has explored the issue of quality improvement extensively. A synthesis of lessons learned has been published as ‘The Challenge of Learning: Improving the Quality of Basic Education in Sub-Saharan Africa’, ADEA, 2005. For information on the decentralisation of book selection and procurement, refer to ‘Changing Public/Private Partnerships in the African Book Sector’, Perspectives on African Book Development Series, No 15, ADEA Working Group on Books and Learning Materials. Information on SFAI, including documentation on technical issues and country developments, will be available on the SFAI website which will be launched in October. Consult www.schoolfeeabolition.org.

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Information and communication technologies to link the poor to markets

The development and proliferation of information and communication technologies (ICTs) have accelerated economic and social change worldwide. They are particularly important in the development context. ICTs have the potential to accelerate growth, create jobs, reduce migration pressure from rural to urban areas, increase agricultural and industrial productivity, increase services and access to them, facilitate the diffusion of innovations, increase public administration efficiency and the effectiveness of economic reforms, strengthen competitiveness in developing countries, and encourage greater public participation and democracy. This paper addresses several pressing questions surrounding ICTs.

While the use of information and communication technologies (ICTs) remains concentrated largely in the developed world, ICT diffusion is beginning to reach developing countries, including poor rural areas, bringing with it high hopes of positive development outcomes. Yet although technological innovations such as cellular telephones and wireless broadband access are playing an important role in building ICT levels globally, strong inequality still remains. The rapid growth of ICTs in developing countries is partly a result of very low initial access, and therefore in absolute terms developing countries and many Commonwealth countries are still well behind the developed world in access to ICTs. As Figure 1 shows, total telephone access in South Asia and sub-Saharan Africa grew by an average of 22 and 17 per cent per year, respectively, from 1990 to 2003, but their current levels of access are still just 6.2 and 5.8 per cent. Inequality of access is even greater within developing countries, especially between urban and rural areas, where the digital divide continues to widen.

Figure 1. Annual average variation rate of the number of telephone lines (fixed and cellular), 1990-2003, and current levels of penetration. Sources: International Telecommunication Union, World Telecommunication Indicators Database (Geneva, 2004); and authors’ own elaboration.
ICTs are unique in having an impact beyond the individual user’s welfare. ICT infrastructure offers economies of scale that stimulate network building and consequent spillover benefits. ICTs enable interactive communication unhindered by distance, volume, medium, or time. They promote greater inclusion of individuals within networks and, even more important, increase the diversity of participants by overcoming the barriers of physical distance and social standing. The immediacy and reach of ICTs also promote faster, more efficient, and ultimately better decision-making across all fields of endeavour.

Some commentators, however, hold much more sceptical views of the benefits of ICTs for development. They argue that access to ICTs largely depends on education, income and wealth; and that the so-called ‘digital divide’ is only a part of a much broader development divide.

The variety of views about ICTs confirms that their role in development is unclear, and little research has been conducted on the direct and indirect links between ICTs and poverty reduction. In addressing the key questions about ICTs and development, this paper is based on the new book Information and Communication Technologies for Development and Poverty Reduction: The Potential of Telecommunications, published by Johns Hopkins University Press.

**What link exists between ICT growth and economic growth?**

In assessing the potential for ICTs to promote economic growth that benefits the poor, two central questions remain to be answered:

- First, has a causal relationship between ICTs and economic growth definitely been established, or are other factors involved?
- Second, is the resulting growth pro-poor, and, if not, what conditions could make it so?

Estimates for 113 countries over a 20-year period show a positive link between telecommunications infrastructure and income, as well as between telecommunications infrastructure and gross domestic product (GDP). The estimates based on this panel of countries – including all Commonwealth countries – suggest that a one per cent increase in the telecommunications penetration rate might be expected to lead to a 0.03 per cent increase in GDP. At the same time, models for different country groups revealed that telecommunications infrastructure had a non-linear effect on economic output, particularly for lower and higher middle-income countries. These results imply that telecommunications networks need to reach a critical mass for a discernible impact on economic output to result. In particular, growth effects were found to be strongest in areas with telecommunications penetration rates of 5–15 per cent. Above and below this threshold, growth effects were limited. Given that the average telecommunications penetration rate in low-income countries is very low, significant network investment and expansion are needed before ICTs can begin to affect growth. Marginal improvements in telecommunications infrastructure, such as the levels shown for sub-Saharan Africa in Figure 1, are unlikely to yield any discernible growth effects.

This result is crucial. The benefits of networking are critical to the concept of ICT-induced growth, and if the minimum critical mass is not achieved, the required network externalities will not happen. By their very nature, ICTs have the potential to reduce relative inequalities among countries and regions. Across countries, where levels of inequality differ, ‘leapfrogging’ – fast-track access to new ICTs – sometimes occurs, but sometimes does not. ICTs and their associated benefits are not yet reaching poor countries, and especially poor rural areas within countries. These different outcomes are largely determined, along with public action, by institutional arrangements for regulation and effective privatisation. In addition, technologies and service provision are concentrated in developed countries, so there is the question of whether the appropriate technologies are being provided, and at affordable cost. Could this be another cause of restricted access in poor countries?

**Do weak institutions block effective use of ICTs?**

Research shows that ICTs cannot be developed without strong institutions that overly facilitate private investment. Many of the national telecommunications monopolies in developing countries were privatised in the 1980s and 1990s, introducing them to competition. This stimulus, combined with ongoing technological change, prompted the constant development of new services in some developing countries, especially the exponential increase of cellular telephone penetration in poor countries. But this increase has not occurred in all countries; in some, the stimulus is taking effect slowly, erratically, and with uncertainty. For example, in some countries (such as Argentina, Chile, Mozambique, Peru, Senegal, and Uganda), the government is facilitating rapid ICT progress with the help of nongovernmental organisations (NGOs) and the private sector. In others (such as Cameroon, Congo, Ethiopia, North Korea and Zimbabwe), the government stands in the way of reform. Within countries, the inequality is even greater. The lesson for reducing unequal access seems clear: governments need to differentiate market efficiency gaps from true access gaps (effectively, missing markets) and then respond with the appropriate set of interventions for each case.

With a market efficiency gap, a difference exists between what markets are achieving under current conditions and what they could achieve if markets function well. To correct this kind of gap, the government must focus on establishing market-oriented policies and regulations that create a level playing field for the private sector and new entrants. The only questions relate to how far the market can reach commercially and how best to implement more competitive conditions,
and in what order. Strong, autonomous, and capable regulatory agencies are needed to:

- Assure market competition and freedom of business/technical choice
- Provide attractive licences designed to encourage growth
- Apply the minimum of regulations necessary, and
- In particular, promote cost-effective access charges for new entrants.

These types of regulatory institutions are hard to build, especially because local expertise in the area is lacking. Professionals need to be trained in every aspect.

With a true access gap, on the other hand, public intervention in ICT provision is still required for some areas and population groups that would not be served, even under the most optimal, efficient, and liberalised market conditions. Certain people and locations invariably lie beyond market limits. In such cases, the government may need to induce service provision through, for example, incentives like subsidies involving public-private (or NGO) partnerships. What is the best way to implement subsidies to maximise scale economies and production, consumption, and network externalities, while achieving sustainability? There are three main conditions:

- Bottom-up identification of demand and consumer willingness-to-pay
- Recognition of the importance of market competition in allocating subsidies, and
- A clear, stable, and credible legal and regulatory environment.

**Impact of ICTs on SMEs**

Collectively, small to medium-sized enterprises (SMEs) are perceived as an engine of growth in developing countries, but they face a formidable task – surviving and competing in a global market. As one of the driving forces of globalisation, ICTs may deliver unprecedented opportunities.

SME case studies provide substantial evidence of increased ICT adoption in low-income countries and positive ICT effects on SME performance. Wide use of the available technologies shows that ICT adoption is perceived to be a key element in remaining competitive. For example in India, a Commonwealth country, the case study by Lal (2006) in the garment industry suggests that labour-intensive industries may be advanced through the use of ICTs.

Nevertheless, the impact on firm performance in most cases is small. Given that SMEs in the case countries have used ICTs for a relatively short time, time lags may be a factor, as may low penetration rates in developing countries. In addition, and perhaps more important, the lack of complementary infrastructure may reduce the opportunities for firms adopting ICTs to perform better. The concentration on quantitative performance indicators may also have omitted notable improvement in the qualitative performance of the firms.

**Household access to ICTs**

“He who has no friends is poor,” goes an African saying. The reduction of the information gap at a low cost is of central importance for the poor. Even though access is still very restricted in rural areas, it is fair to say that ICTs have an important positive impact on rural households. Chowdhury, Galdo and Torero (2003) show that for another Commonwealth country, Bangladesh, the gains in welfare from using local telephone calls compared with alternative means of communications (mail, travelling, radio communication, and other means of communication) show a considerable gap. Just within the poorest quintile, the minimum estimated gains in welfare from local telephone calls compared with regular mail were US$0.11 for Bangladesh. Similarly when analysing the impacts over household consumption in Laos, after comparing similar households on all characteristics with the exception of access to phone, an increase of 22 per cent in per capita total consumption was found, and 24 per cent in per capita cash consumption as a result of access to telephone.

The welfare effect of telephone use in rural households is verified by users’ perceptions of the benefits, the high demand for service, the substantial consumer surplus associated with telephone use, households’ willingness to pay, and results from econometric analysis. It is possible to increase that positive impact by making ICTs more accessible in rural areas, adapting new technologies to rural settings, and using old technologies in innovative ways, such as providing information services by telephone.

In both SMEs and households some policy problems remain, however. First, most case studies reveal that major regulatory impediments lead to lack of private-sector participation in telecommunications, and consequently to insufficient competition. As a result, access costs are too high, interconnection between networks is problematic, and infrastructure cannot be shared among operators. Second, a number of potential barriers to the effectiveness of ICTs remain. Apart from...
issues of access and price, barriers to ICT effectiveness fall into three principal categories: barriers involving skill levels, such as in accessing internet information; barriers involving ICT use for development-related purposes; and barriers related to content relevance. In many low-income countries, access to telephones is the basis of pro-poor ICT growth because specialised skills are not needed and because telephone access forms a platform for more advanced ICT adoption.

The role of ICTs in providing pro-poor public goods and services

ICTs can be a powerful tool for improving the quality and efficiency of government services, such as health and education, although a clear gap still exists in the use of ICTs for the delivery of public goods. Cross-country analysis indicates that telecommunications investment may well be associated with improved health status. Prominent applications for health include the creation of ‘telemedicine centres’ that offer medical advice or health information to rural inhabitants via email or the internet. ICTs have also been used to design global telecommunications networks that link healthcare workers around the world via email. ICTs have also been used for educational purposes, such as the African Virtual University and the use of the internet to disseminate information on farming technologies and changing prices to 30,000 villages across six states in India.

These cases, however, are isolated at this stage. Poor people are still excluded from many public services, and ICTs have not been adapted to the appropriate delivery of pro-poor public goods in general. The need remains for innovative ways to provide access to public services using ICTs. The strong link perceived to exist between ICT attributes and the Millennium Development Goals (MDGs) reflects this reality. Successfully harnessing the power of ICTs could make a substantial contribution to achieving the MDGs, both directly through the delivery of public goods and indirectly through the creation of new economic opportunities.

Conclusion

ICTs are an opportunity for development, but not a panacea. For the potential benefits of ICTs to be realised in developing countries, many prerequisites need to be put in place: prompt deregulation, effective competition among service providers, free movement and adoption of technologies, targeted and competitive subsidies to reduce the real access gap, and institutional arrangements to increase the use of ICTs in the provision of public goods.

Given the diverse potential benefits of ICTs, especially in the provision of public goods, subsidies traditionally used for poverty alleviation could be adapted to create incentives for the use of ICTs. For example, conditional cash transfer programs, which are largely tied to education or health, could be implemented at the community level to provide internet access to children where educational and health services are delivered.

Another example is to increase access to savings and banking services through banking cards for low-income households, as in recent experiments in India. At the same time, such programmes would contribute to the necessary critical mass of ICTs.

Access to information through ICTs is a question not only of connectivity but also of capability to use the new tools and relevant content provided in accessible and useful forms. Connectivity has been a priority, as a prerequisite for the other two, but given the speed at which technologies are evolving and can move – unconstrained by overly restrictive licenses and global patenting – costs could fall significantly, facilitating adoption. Hence, we should respond to the need for all three Cs – connectivity, capability and content – to progress in tandem.

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Joachim von Braun has been Director General of the International Food Policy Research Institute (IFPRI) since 2002. Under his leadership, IFPRI has continued to grow, and has significantly expanded its teams based in Africa, Asia, and Latin America in response to research challenges and partners’ needs. He received his doctoral degree in agricultural economics from the University of Goettingen, Germany in 1978. He has published research on international development and agricultural economics. Within the CGIAR, von Braun has helped to organise the creation of a Global Food and Agriculture University.

International Food Policy Research Institute (IFPRI) is a member of the Consultative Group on International Agricultural Research (CGIAR). IFPRI’s vision is a world free of hunger and malnutrition. Its mission is to provide policy solutions that cut hunger and malnutrition. This mission flows from the CGIAR mission: “To achieve sustainable food security and reduce poverty in developing countries through scientific research and research-related activities.”

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Financing slum upgrading: the crisis of urbanisation

The year 2007 marks a historic crossroads in human history: it is the year in which, for the first time, half of humanity will be living in towns and cities. By 2030, the proportion will have increased to two-thirds of the world population. We are at the dawn of a new urban era when homo urbanus – the town-dweller – will dominate the landscape. And yet most of the growth is in the slum areas, where lack of resources is the universal experience. It is patently clear to all of us in the United Nations system as a whole that if we fail to achieve the Millennium Development Goals in towns we will simply fail to achieve them at all. It is important that the methods of financing slum upgrading are given proper attention and priority.

It could be a cause for celebration that more than half of the world’s population live in towns and cities. After all, cities have always been centres of economic and cultural creativity. But the reality is very different. As we live through a time of unprecedented, rapid, irreversible urbanisation, the cities that are growing fastest are those of the developing world. And the fastest growing neighbourhoods in these cities are slums. Indeed, 2007 will also be the year in which the global number of slum dwellers is forecast to reach the one billion mark.

Only recently have world leaders paid attention to the crisis of slums. In 2000, one of the Millennium Development Goals, specifically Goal 7 Target 11, called for ‘improving the lives of at least 100 million slum dwellers’. Target 10 is also directly related to improving the living conditions of slum dwellers. This aims to reduce by half the proportion of people without sustainable access to safe drinking water or basic sanitation by 2015.

It is important to note that we at the UN think that the slum target is much too modest. Already, since 2000, the population of slum dwellers has increased by the same figure. In fact, if we continue with business as usual, by 2020, there could be two billion slum dwellers.

This means going to scale. This is why a cornerstone of UN-HABITAT’s new Medium-term Strategic and Institutional Plan is partnerships. We have no choice but to catalyse new partnerships between government and the private sector. This is the only way to finance infrastructure and housing at the required scale – the scale needed to stabilise the rate of slum formation, and subsequently reduce and ultimately reverse the number of people living in life-threatening slum conditions.

This will require, in addition to sustained economic growth, direct and focused efforts to make cities more productive and socially inclusive. Yet there is every likelihood that in the coming 20 years, conventional sources of funds will simply be unavailable for investment at the scale required to meet the projected demand for urban infrastructure and housing.

Urbanisation and neo-liberal economics

In an era of neo-liberal economics predicated on market-led growth, interest in financing recognises the limits of public expenditure. It reflects the failure of public planning and delivery systems to keep pace with rapid urbanisation. It further reflects the initiatives of non-state actors to increase the supply of housing and infrastructure in the absence of adequate public intervention.

The shift in emphasis from public to private sources of finance raises questions about the role of the state in housing and urban development and, by extension, about the future policies of international development cooperation agencies and financial institutions.

Structural adjustment and the collapse of national housing corporations

Most states in the developing world experienced in the 1970s an economic and political crisis that led many to implement structural adjustment policies in the next decade. Governments devaluing their currencies to promote exports eliminated price supports, aligned their economies with global markets, cut public expenditures on social services, privatised state-owned enterprises, and liberalised financial markets.

National housing corporations in many countries either collapsed or scaled back operations. Public expenditure on housing dropped, as did public
investment in urban infrastructure. By the 1990s, public finance for housing and urban infrastructure was all but eliminated, save ad hoc programmes of development cooperation agencies and NGOs designed to minimise the social consequences of structural adjustment.

The advent of rapid urbanisation coincided with economic crisis and structural adjustment. First in Latin America, then in South and South-east Asia, and more recently in Africa, rural-urban migration combined with population growth to increase the size of cities. Urbanisation without requisite economic growth resulted in urban unemployment; urbanisation without public services resulted in inadequate shelter, water and sanitation; urbanisation without economic growth and public services resulted in poverty and slums. Municipal authorities barely capable of meeting their payrolls were vulnerable to corruption, unable to collect revenues, or plan, let alone finance the burgeoning housing and service needs.

The demand for services

The demand for services in the absence of public supply created two types of innovation and corresponding sources of finance: private entrepreneurs who saw in slums a business opportunity, and urban poor organisations keen to improve their living and working conditions. The entrepreneurs built shacks without services for rent, or provided unofficial services (water, credit, sanitation, electricity, security, etc.). Rates were calibrated on capacity to pay, small unit provision, high unit cost, and on high volume.

The organised poor mobilised savings and acted collectively or individually to secure land, build homes, and gain access to services. Microfinance institutions emerged to offer credit to entrepreneurs and the organised poor. Rather than rely on public finance, slums generated investment, fostered rent-seeking opportunities and offered a source of cheap labour to industry, upscale residential neighbourhoods and the central business districts.

Radical change in the formal private sector

The combination of structural adjustment, rapid urbanisation, weak municipal planning and services, and a distinct slum economy has created conditions for radical changes in the formal private sector – and hence, a new source of finance for housing and urban infrastructure.

While many banks have confined lending to traditional, higher-income markets, others have diversified lending to reach rapidly growing urban populations, building upon precedents set in slums by entrepreneurs and urban poor organisations. Innovation of this kind has been accelerated by competition among banks for traditional, higher-income markets, the lucrative business of microfinance, and downward pressure on interest rates. Primary mortgage institutions have also emerged, especially in countries with established domestic capital markets that can subscribe to debt instruments as a source of long-term financing so essential for housing finance.

For private service providers, structural adjustment has had unanticipated consequences in countries with rapidly expanding urban populations. Privatised utility companies see in slums a large, untapped market – a population of slum dwellers who pay more per unit cost of service than higher income households. By working with entrepreneurs and urban poor organisations, private utilities are developing innovative systems to extend their services to slum dwellers and the urban poor.

The role of government

The shift from public to private sources of finance for housing and urban infrastructure in cities of Africa, Asia and Latin America would suggest that governments no longer have a significant role to play in financing human settlements development. On the contrary, the role of the state has never been more pertinent. Only government policy, public investment and municipal planning can ensure financial sector reforms that translate into private investment in affordable housing and basic services.

Government legislation on pension funds, for example, can create a source of long-term capital and trigger institutional investment in debt instruments to finance municipal infrastructure and/or mortgage facilities. Targeted public investment is also crucial. It is estimated that 30 per cent of the cost of home construction is made up of expenditure in water and sanitation. By dedicating public expenditure to infrastructure, the state can spur massive private investment in housing – a volume of shelter hundreds of times greater than could be constructed by government funds. Municipal planning is a prerequisite for mainstreaming private investment, particularly approaches to planning that build upon – rather than exclude – the dynamism of the slum economy and the integral role it plays in urban development.

Development cooperation

The change in the way affordable housing and urban infrastructure is financed at country level has significant implications for development cooperation. Official development assistance will never finance the massive housing and service deficit in cities in Africa, Asia and Latin America, nor should it.

The accumulated savings and purchasing power of urban poor and the capital housed in pension funds and among private investors as well as dedicated public investment constitute sources of finance that make official development aid pale by comparison.

The future of development cooperation is to channel funds in ways that accelerate the actions of local actors to harness these sources of finance. This includes a combination of targeted technical assistance and credit enhancements, equity investments, and bridging finance that preferably can build local capacity and leverage multiple sources of finance. It also involves creative partnerships between multilateral and bilateral development agencies and international finance institutions geared toward fast-tracking investment for infrastructure.

More fundamentally, development cooperation will require coming to terms with the social and economic
Consequences of rapid urbanisation and addressing urban poverty by drawing on the potential of innovations in financing.

Non-financial constraints

However, it is important to understand that constraints to mobilising financial resources for investment in shelter development are both financial and non-financial in nature. Non-financial constraints include land legislation that makes it difficult to use real estate as effective collateral, as well as inappropriate national and local regulatory frameworks governing land use, occupancy and ownership.

Finance is only one dimension of securing sustainable solutions that can fill the gap between the two extreme outcomes of current processes: inadequate, affordable shelter; and unaffordable adequate shelter.

Experience in both developed and developing countries shows that filling this gap contributes effectively to the objective of reducing poverty by creating jobs, attracting investments, improving health and raising economic productivity. Such efforts typically include:

- Good urban management, planning and governance to ensure that all citizens, particularly women, the young and the elderly, have a strong voice in decisions that affect their lives
- Efficient land markets and property administration that prevent land speculation and urban sprawl and provide sufficient affordable land for the urban poor
- Enforceable zoning and land use regulations that facilitate compact and mixed-use urban development and reduce the ecological footprint of cities
- Affordable and environmentally sound infrastructure including transport, energy, water and sanitation
- Financial markets and systems that can provide affordable housing credit and long-term municipal finance.

As the only United Nations body vested with responsibility for promoting the sustainable development of the built environment, UN-HABITAT needs all the support it can garner for its new reform plan. Part of the overall reform of the United Nations, this plan covers the years 2008-2013, and provides a new shared vision.

UN-HABITAT sees a way forward in five key areas of focus: advocacy, monitoring and partnerships; participatory urban planning, management and governance; affordable land and housing; environmentally-sound and affordable basic infrastructure and services; and, most importantly, strengthening human settlements finance systems.

As the population of our cities, especially in the developing world, explodes, it becomes increasingly important for the international community to provide the political will and resources to address the problems of urbanisation and especially the urban poor. Without such commitment, our cities will be socially and environmentally unsustainable. What is worse, the children of homo urbanus may well be condemned to playing on garbage heaps.

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The United Nations Human Settlements Programme, UN-HABITAT, is mandated by the UN General Assembly to promote socially and environmentally sustainable towns and cities with the goal of providing adequate shelter for all.

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Financing infrastructure investment: potential fiscal risks of public-private partnerships

New mechanisms to develop infrastructure have pushed back traditional financing from annual budget allocations, giving rise to new fiscal risks. These risks include, for instance, an increased fragmentation of the budget process and the creation of contingent liabilities for the government. Risks from these factors have in many cases been compounded by inappropriate institutional arrangements within the public sector to identify, quantify, and manage the complexities of new financing mechanisms. This paper focuses on key fiscal risks from public-private partnerships, and outlines options for containing them.

Over the last few decades, countries have significantly broadened their options for financing infrastructure investments. Different institutional mechanisms that have been developed – including revenue earmarking, dedicated road funds, and public-private partnerships (PPPs) – have pushed back traditional financing from annual budget allocations. Often, these mechanisms have been motivated by the need to find more predictable funding sources than those provided by tight government budgets, and a desire to circumvent restrictions and controls that apply to traditional financing.

PPPs refer to arrangements where the private sector supplies infrastructure assets and services that traditionally have been provided by the government. PPPs have three key characteristics:

• Private execution and financing of public investment
• An emphasis on both investment and service provision by the private sector, and
• Risk transfer from the government to the private sector.

PPPs are changing the role of the public sector in financing infrastructure projects, both in developed and in emerging economies. While the infusion of private capital and management was seen as a new way to ease rising fiscal constraints for infrastructure investment, the idea that private management of public projects generates efficiency gains has become increasingly popular. As a consequence, the role of the public sector has started to shift from financier/owner/manager of projects to regulator and guarantor, and its involvement in the productive economy has shrunk. Simultaneously, private sector initiative has started to invade areas that were previously considered in the exclusive domain of the public sector.

PPPs have been used in sectors as diverse as transport (e.g. roads, railways, bridges, and tunnels), education (schools, museums, libraries), health (hospitals and clinics), water (sanitation plants, irrigation systems, pipelines, etc.), and public administration (courts, police stations, and prisons). Experiences of different countries suggest that economic infrastructure (for instance in transport) is usually a more straightforward candidate for PPPs.

PPPs can potentially be more efficient than traditional public procurement of assets and services. For the government, PPPs can support increases in infrastructure investment without immediately adding to government borrowing. At the same time, better management in the private sector and its capacity to innovate can lead to increased efficiency, better quality, and lower cost services. For the private sector, PPPs offer new business opportunities in areas where the public sector was, in many cases, the only supplier. However, PPPs can also be used mainly to bypass spending controls, and to move public investment off budget and debt off the government balance sheet, while the government still bears most of the risk involved and faces potentially large fiscal costs.

In practice, PPPs have been surrounded by controversy over their economic benefits. In industrial countries, issues have arisen because of an often generous helping hand of the public sector in support of the projects, including a variety of subsidies, guarantees, barriers to competition, and contract renegotiation after substantial errors in demand projections. In developing countries, additional issues have emerged, including a need for support from multilateral agencies. Also, governments at times have needed to assume the liabilities of private sector operators. The Mexican government, for example, took on about two percent of GDP of private debt in 1994 to resolve problems faced by the concessionaires’ creditors.
PPPs and fiscal risks

Like all projects, PPPs entail different risks. These can be summarised as follows:

- **Construction risk:** design problems, and cost and schedule overruns.
- **Financial risk:** the possibility that a project’s cash flow may fall short of the level needed to repay the project loans and capital invested, for instance due to interest and exchange rate variability.
- **Demand risk:** the possibility that the demand for the services provided declines, reducing the cash flow generated by the project.
- **Availability risk:** possible lack of continuity and quality of service provision.
- **Political risk:** situations where government actions could impair the private sector’s earnings potential.
- **Force majeure:** risks beyond the control of public and private partners (i.e. natural disasters).
- **Residual value risk:** uncertainty regarding the market value of the infrastructure asset at the end of the contract.

PPPs should be pursued when they achieve efficiency gains, critically requiring that different risks be assigned to the party that is best equipped to manage them.

However, PPPs can also be used to bypass budgetary procedures, thereby exacerbating risks faced by the government. In general, PPPs allow governments to avoid or defer spending on infrastructure without deferring its benefits. Even PPPs that do not deliver value-for-money (VfM) can be a tempting alternative for financially constrained governments, as they can support increases in infrastructure investment without immediately adding to government borrowing. Hence, while potentially holding a promise for efficiency gains and easing fiscal constraints for infrastructure investment, PPPs can also simply be a tool for bypassing expenditure controls, delaying borrowing, and moving public investment off budget and debt off the government balance sheet. Sometimes, governments can be left bearing most of the risk involved and facing potentially large fiscal costs over the medium to long term.

Fiscal risks are also more likely to arise when the overall institutional framework governing PPPs is poorly developed. Fiscal risks will be more pronounced when investment projects are of poor quality, the legal and fiscal institutional framework is weak, and accounting and reporting systems do not transparently disclose the fiscal implications of PPPs.

In practice, the fiscal consequences of these risks can take one of the following forms:

- Future commitments from the budget to honour minimum income guarantees
- Contingent liabilities in the form of guarantees to secure private financing
- Commitment to purchase the output of the private partner by making regular payments to the private provider
- Bailing out the private partner when the latter becomes financially distressed, and
- Renegotiations with the franchise holder to increase investment expenditure on infrastructure assets in the short run in exchange for additional future cash flows for the private partner, which results in forgone future revenues for the government.

**Conditions for successful PPPs**

The shift to a new model for infrastructure development implies major challenges for governments. The new best practice model does not mean a total retreat by governments; on the contrary, best or better practice involves moving to good governance, underpinned by several requirements that aim at ensuring that PPPs mobilise additional resources for and increase the efficiency of public investment. Without greatly improved governance, the shift to increased private sector partnership could just mean monopoly powers being transferred to the well connected in the private sector. Moreover, without improved governance, private sector partnership would eventually flounder and the demands for infrastructure will not be met, as risks would become unacceptable.

Conditions for successful PPPs can be summarised as follows:

- **PPP projects should be integrated with the government investment strategy, medium-term fiscal framework, and the budget cycle.** PPP projects should be part of the government investment strategy and be pursued only when they offer VfM compared to standard public procurement. This would allow optimising project impact while raising profitability for a given level of investment. To ensure that the fiscal implications of PPPs are fully taken into consideration in the government’s medium-term fiscal framework and the budget, PPP projects should not be allowed to move forward outside the regular cycle of other investment projects.

- **The quality of services under PPPs should be contractible.** If the government can specify the quality of services it wants the private sector to supply, and can translate these into measurable output indicators, then it can enter into a contract with the private sector which links service payments to service delivery. The less clearly specified the contract conditions, the greater the risk of costly renegotiation of the contract during its implementation. Even if the quality of service is contractible, ensuring build quality may be more problematic. Shortcuts in construction can be hidden for many years, creating future liabilities for the government and possibly leading to costly renegotiation.

- **Adequate risk sharing is a key requirement if PPPs are to deliver high-quality and cost-effective services.** Successful PPPs require that the different types of risks be borne by the party that can manage it best. Assignment of various risks to the adequate party should be clearly defined in the contract. Assessing risk transfer is difficult given the multitude of risks and the complexity of PPP contracts. However, understanding can be improved by isolating individual risks and identifying which parties have control over them. Another option would be to assess the extent of risk transfer based on the overall risk characteristics of a PPP, as done in the UK.
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PPP accounting and reporting

The lack of an internationally accepted accounting and reporting standard for PPPs remains a possible obstacle to future efficiency. Existing standards are applicable only to a set of PPP projects (i.e. operating contracts, concessions and operating leases, and transfer of PPP project assets to the government). Eurostat has recently issued a decision classifying the assets of PPP projects as either public or private based on risk transfer, with implications for the accounting treatment. However, classifying the assets of a PPP project as either public or private does not allow capturing the actual extent of risk transfer and risk sharing. PPP projects are essentially risk-sharing arrangements that require each of the partners to assume and manage specific risks in the provision of infrastructure services.

In addition to disclosure requirements, the IMF recommends the following treatment of government obligations (contingent or certain) that arise in PPP project contracts for policy analysis:

- For projects that are considered private investments, future payments by the government (contingent or certain) should be counted towards primary spending, i.e., they reduce the primary balance.
- For projects that are considered public investments, the service component of future payments by the government should be recorded as primary spending, while the debt service component should be separated out and included in the overall projected interest and amortisation payments. All debt is recorded as a liability of the public sector and added to the government’s debt stock.

Proper control

New financing mechanisms have often been motivated by tight government budgets and a desire to circumvent budget controls that apply to traditional options. In many instances, these new financing instruments have led to an increased fragmentation of the budget planning process. Furthermore, inappropriate institutional arrangements within the public sector to identify, quantify, and manage the complexities involved in new financing mechanisms have amplified these problems.

PPPs provide a new way for financing infrastructure investments, but they have to be structured appropriately and supported by a well-developed fiscal and legal institutional framework. The goal should be to increase efficiency by attracting private capital and not to move investment spending off budget. Governments need to assess carefully the risk associated with PPPs, and ensure the adequate sharing of this risk with the private sector, with the risk borne by the government appropriately reflected in the fiscal accounts. It is essential that PPP operations be fully and transparently disclosed, and incorporated into medium-term policy analysis.

This paper was co-authored by Gerd Schwartz, Ana Corbacho and Taline Koranchelian. All authors are with the International Monetary Fund, but the views expressed in this paper are those of the authors and should not be attributed to the IMF, its Executive Board or its management.

The International Monetary Fund (IMF) is an international organisation of 185 member countries. It was established to promote international monetary cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment.

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International tourism: a driving force for economic growth of Commonwealth countries

Since 1950 the number of international tourist arrivals has grown from 25 million to over 800 million in 2005. Today international tourism receipts account for a huge percentage of worldwide exports of goods and services, and reached US$735 billion in 2006. These statistics make tourism one of the most dynamic industries of the modern economy. Many Commonwealth members rank in the list of the world’s top emerging tourism destinations. The author investigates whether tourism actually represents a key determinant for economic growth in these countries.

Tourism is one of the most dynamic world industries, showing an annual growth rate in international arrivals of 6.5 per cent over the last half-century, according to statistics from the UN World Tourism Organization (UNWTO). Even though the majority of international tourism still takes place within the developed world, in recent years tourism to developing countries is becoming a significant phenomenon. New destinations are increasing their market share, while the main traditional tourist-receiving regions – Europe and the Americas – have grown below the world’s average rate. Both these regions, in fact, represented a joint market share of over 95 per cent in 1950 and 76 per cent in 2000. In the same period, Asia and the Pacific grew at a rate of 13 per cent on average a year and Middle East at a rate of 10 per cent (Table 1).

The first four months of 2007 seem to confirm these performances: Asia and the Pacific are still the motors of international tourism expansion (+9 per cent), followed by Africa (+8 per cent) and the Middle East (+8 per cent). In the light of these trends, UNWTO estimates that international arrivals will reach nearly 1.6 billion by the year 2020. Again, Asia and the Pacific, Africa and the Middle East are forecast to record growth at five per cent year, compared to the world average of 4.1 per cent (Figure 1).

Tourism to developing countries: some general facts

Looking at UNWTO statistics, the following general facts seem to characterise international tourism to developing countries:
- The number of international arrivals in the same region is highly variable across countries, and across areas within the same developing country.
- Middle-income countries represent the majority of destinations.
- Low-income countries show the highest growth rates in tourist arrivals.
- Developed countries are the main source of tourism flows to developing countries.

Table 1. International tourist arrivals (1950-2005) – Average annual growth (%)

<table>
<thead>
<tr>
<th></th>
<th>World</th>
<th>Africa</th>
<th>Americas</th>
<th>Asia and the Pacific</th>
<th>Europe</th>
<th>Middle East</th>
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<tr>
<td>1950-1960</td>
<td>10.6</td>
<td>3.7</td>
<td>8.4</td>
<td>14.1</td>
<td>11.6</td>
<td>12.3</td>
</tr>
<tr>
<td>1960-1970</td>
<td>9.1</td>
<td>12.4</td>
<td>9.7</td>
<td>21.6</td>
<td>8.4</td>
<td>11.5</td>
</tr>
<tr>
<td>1970-1980</td>
<td>5.3</td>
<td>11.6</td>
<td>4.0</td>
<td>13.9</td>
<td>4.7</td>
<td>14.3</td>
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<tr>
<td>1980-1990</td>
<td>4.7</td>
<td>7.8</td>
<td>4.1</td>
<td>9.3</td>
<td>4.1</td>
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<td>1980-1985</td>
<td>2.9</td>
<td>6.1</td>
<td>0.9</td>
<td>7.4</td>
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<td>2.7</td>
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<tr>
<td>1985-1990</td>
<td>6.5</td>
<td>9.5</td>
<td>7.3</td>
<td>11.3</td>
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<tr>
<td>1990-2000</td>
<td>4.6</td>
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<td>3.3</td>
<td>7.0</td>
<td>4.1</td>
<td>9.6</td>
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<tr>
<td>1990-1995</td>
<td>4.2</td>
<td>6.1</td>
<td>3.3</td>
<td>8.0</td>
<td>3.5</td>
<td>7.3</td>
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<tr>
<td>1995-2000</td>
<td>4.9</td>
<td>6.7</td>
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<td>1950-2000</td>
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<tr>
<td>1950-2005</td>
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<td>8.1</td>
<td>5.4</td>
<td>12.5</td>
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</table>

Figure 1. International tourist arrivals (1950-2020).
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Of the world’s top emerging tourism destinations in the period 1995–2004 – i.e. destinations growing at a rate above the world average and with an increase of at least 100,000 arrivals – many are Commonwealth developing countries. In particular, Zambia grew at a rate of 13.6 per cent followed by Malawi (10.5), Malaysia (8.6), Ghana (8.3), Tanzania (7.9), Maldives (7.8), Mauritius (6.9), Belize (6.5), Bangladesh (6.3), Pakistan (6.2), and Trinidad and Tobago (6.1). Moreover, four Commonwealth developing countries ranked in the list of the 50 world’s top tourism destinations in 2006 (Malaysia, South Africa, Singapore, India).

From an economic point of view, international tourism receipts reached US$735 billion in 2006 – US$883 billion including international passenger transport – with an increase of US$57 billion (+4.5 per cent) compared with 2005. In other words, more than US$2.4 billion a day is earned by the tourism industry, making it the fourth export category after fuels, chemical and automotive products.

The economic impact of tourism

Generally speaking, tourism demand depends upon the economic conditions in the main generating markets. In particular, when GDP growth exceeds four per cent, international tourist arrivals rise; similarly, when world economic growth is lower than two per cent, tourism growth tends to fall.

Unfortunately the contribution of tourism activity to a country’s economy is not easily quantified, since tourism does not represent a clearly identifiable industry: firstly since it involves many different products (transport, mail, entertainment, etc.); and secondly because some products (for example, a meal in a restaurant) can be sold both to tourists and local residents.

In detail, tourism can determine direct and secondary effects on domestic economies. Direct effects represent impact on businesses that sell directly to tourists. They are changes in production as a consequence of changes in immediate tourism expenditures (if tourist arrivals rise, hotels and restaurants increase their sales with an expected increase in the wages for hotel and restaurant workers).

Secondary effects measure economic activity that results from the circulation of tourists’ money within a country. They account for impact on businesses that sell indirectly to tourists (indirect effects: for example, industries selling products and services to hotels and restaurants) and for economic changes due to spending by employees working in the tourism sector (induced effects).

Positive effects of international tourism in Commonwealth countries

The contribution of tourism to local economies through direct, indirect and induced effects may be particularly pronounced in the Commonwealth’s developing countries. This is especially the case in small island developing states (SIDS), which represent more than 50 per cent of the Commonwealth’s developing members. Given the low opportunities of economic diversification, tourism may become an occasion for development and improvement of living standards for local people in these countries.

The positive effects of international tourism to the Commonwealth’s developing countries can be measured in terms of:

- **Income level and employment opportunities.** Being highly labour-intensive, the tourism industry may represent a key source of income in these countries through wages and salaries. It offers many employment opportunities for the local population through supply of basic goods and services (hotels, restaurants, taxis). Moreover, it stimulates the supply of goods and services in backward and forward industries and may generate informal employment (street vendors, informal guides, etc.). In SIDS it may contribute to gender equality.
- **State revenue.** Tourism can contribute to government revenues both directly (through taxes on incomes from tourism business and employment) and indirectly (by taxes on goods and services provided to tourists).
- **Investment.** Tourism can stimulate local governments to undertake infrastructure improvements, since it requires a high standard of transport, communication, water and energy supply and other public utilities. In many Commonwealth countries these improvements can provide essential services for rural communities that would otherwise be excluded from general infrastructure provision.
- **Balance of payments.** Tourism represents the main source of foreign exchange earnings for many SIDS, thus generating balance of payments benefits. The foreign currencies can be employed to reduce national debt or to finance growth in other economic sectors.
- **Diversification of economy.** Tourism can help to diversify more traditional economies since it represents a good alternative to sectors such as agriculture and manufacturing. The uncertainty of crops and the unpredictability of prices in agricultural production on one hand, and the needs of skilled labour and physical capital in the manufacturing sector on the other, make the tourism industry an excellent source of substitution or complementary incomes. In addition, it can generate demand for new goods or services that can themselves become a growing sector. In this sense, tourism is such a multi-faceted sector that it can certainly represent an excellent tool for development.

Some negative effects

Obviously, tourism does not represent a panacea to solve all economic problems in these countries. Some of the less welcome effects are listed below:

- **Tourism may bring about ‘leakage’,** given that part of the receipts does not remain in the host countries, thus diminishing the beneficial consequences. This frequently occurs in the Commonwealth’s developing countries where tourists often arrive thanks to all-inclusive package tours bought in their home countries.
In this way, large percentages of travellers’ expenditures (sometimes more than two-thirds) may leave the local economies. In addition, because of the lack of local producers, resources and expertise, host countries cannot supply all the services and products required by tourists (for example food and drink). For this reason these products and services must be imported from other countries, bringing about more leakage.

- The high public investment required by tourism may divert capital from other crucial sectors such as health and education.
- Frequently tourism generates only seasonal or part-time jobs, and does not contribute to full-time employment.
- The increase in demand for goods and services by travellers may bring an increase in prices for local people; this can be compensated for only if local incomes rise proportionately.
- Tourism is price-elastic: changes in prices can determine shifts in tourism arrivals. This can have negative effects on those Commonwealth countries with too much reliance on visitors when a source country experiences an economic downturn.
- The infrastructure requirements (transport, communications) and facilities (hotels, restaurants, shops) may cause depletion of natural resources, pollution, and pressure on the natural environment.
- The lifestyle of local people may be altered, possibly bringing changes of identity and values, cultural conflicts, as well as ethical consequences such as crime generation, child labour, prostitution and sex tourism.

### A quantitative analysis

Although from a theoretical point of view international tourism may actually bring about economic growth in Commonwealth countries, an empirical verification was needed. This case-study aims to verify this hypothesis employing a panel data approach. Data for this study was drawn from the *World Development Indicators* (World Bank, 2005) and from the Penn World Table. Following the standard empirical literature on this topic, economic growth of Commonwealth countries was measured in terms of the following regressors:

- Real gross domestic product per capita in the previous period
- General government final consumption expenditure (percentage of GDP)
- Gross fixed capital formation (percentage of GDP)
- Adult male literacy rate (percentage of males ages 15 and above)
- Total trade (exports plus imports) to output ratio
- International tourist arrivals per capita, to capture the effect of international tourism flows on economic growth of destination countries. This variable represents the number of overnight visitors who travel to a country for a period not exceeding 12 months. Moreover, it includes the number of tourists visiting a country in which they have their usual residence, but outside their usual environment.

Some Commonwealth countries (Brunei, Bahamas, Kiribati, Maldives, Nauru, Samoa, Solomon Islands, Tuvalu) were eliminated from the dataset because of the lack of data; others (Australia, Canada, New Zealand and UK) were removed with the aim of focusing exclusively on developing countries. Therefore, the definitive dataset was composed of 41 countries. To avoid measurement errors and the effects of cycles on variables a 14-year period was considered, between 1990 and 2003 (data on tourist arrivals are available only since 1990 for all countries considered). More details of the methodology can be supplied on request.

The results confirm the theoretical expectation that the tourism industry exerts a positive impact on growth in Commonwealth developing countries. The tests were repeated for regional groupings, and these showed that the contribution of tourism to economic growth was particularly marked in Asian countries, followed by Africa, with the Caribbean result less significant.

### A key development tool

The tourism sector can represent a determinant factor for economic growth of the Commonwealth’s members, in particular where opportunities of economic diversification are limited. Increasing tourism flows can bring many positive economic consequences to host countries, particularly in terms of income and employment opportunities, state revenues, diversification of economy and foreign exchange earnings.

Obviously, the tourism industry cannot by itself solve all economic problems, but may represent a key development tool. The important political consequence is that domestic governments should invest more in this industry, improving public infrastructures, communication, water and energy supply and other public utilities.

An opportune strategy may be to re-invest part of the tourism profits to attract new tourists – for example through appropriate promotions and marketing strategies. The remaining gains should be dedicated to helping local people to maximise the economic benefits from tourism. In this way, the tourism sector may become a real driving force for economic development among the Commonwealth’s members.

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Public-private partnerships in developing countries: the SADC context

Prof Andreas Antoniou
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The Commonwealth Secretariat and the South African Development Community (SADC) Development Finance Resource Centre (DFRC) jointly organised an expert-led workshop to discuss issues related to promoting public-private partnerships (PPPs) for infrastructure investment and service delivery in the SADC region. This article summarises both those points of clear consensus, and those on which the debate is continuing.

The SADC workshop held in December 2006 in Sandton, South Africa, and hosted by the Industrial Development Corporation (IDC) of South Africa, was attended by a range of private sector experts as well as representatives from SADC governments and the SADC secretariat. The aim of the workshop was to provide a structured forum for participants to present and debate a range of issues relevant to improving infrastructure development in the SADC region, but also in Africa more generally. The issue of post-conflict countries (PCCs) – relevant to a number of SADC members – was also specifically addressed. The outcomes were presented at the 11th Commonwealth HIPC Ministerial Forum (April 2007, Washington DC, USA), where infrastructure development was one of the key items on the agenda.

The discussions at the Sandton workshop centred on the role that PPPs could play in addressing infrastructure constraints in Africa, with general consensus emerging in three key areas:

- Role of PPPs – their potential and limitations
- Key constraints facing successful development of infrastructure PPPs, and
- Approaches to encouraging infrastructure PPPs.

The role of PPPs – their potential and limitations

The participants recognised and agreed that PPPs are important mechanisms in addressing the ‘infrastructure gap’ currently observed in developing countries, and particularly in Africa. The importance of PPPs was specifically noted in the context of continued withdrawal of Official Development Assistance (ODA) from economic infrastructure sectors and its redirection towards humanitarian aid and support for social sectors (e.g. health, social safety nets, education). Structured appropriately, PPPs have the potential to introduce greater commercial discipline and thus sustainability in developing and operating infrastructure services, as well as leverage in private finance into sectors where commercial realities allow.

The participants also agreed that despite their ever greater presence, PPPs are not readily understood in the SADC region and more widely within Africa. This has led to unrealistic expectations of what can be achieved through partnering with the private sector and what risks the private sector is able to bear. It was generally agreed that further capacity building within the public sector would be beneficial as a way towards seeing more and better value for money PPP transactions in Africa.

Finally, it was stressed by all the participants that PPPs can only ever be a supporting instrument within the context of much greater government spending on infrastructure development. While the participants recognised the shrinking fiscal space that many African, and in particular HIPC, governments faced, PPPs and private finance will never be able to replace the need for government investment, in particular in less commercially viable infrastructure sectors such as water and sanitation and rural roads.

Key constraints facing successful development of infrastructure PPPs

Key bottlenecks in PPP development often occur early in the project cycle. These include:

- Constraints related to weak enabling environment, such as underdeveloped legislative and regulatory frameworks and an unstable macroeconomic environment, and
- A shortage of well structured ‘bankable’ projects – for which returns would be available to the private sector.

In addition, there was a general consensus that many infrastructure projects in Africa continue to require
considerable subsidy to make them viable, even if they are developed on a PPP basis. While in part the need for subsidy is driven by the high costs and risks in developing such projects, the limited affordability of the consumer base continues to be a major constraint. Greater availability of performance-based subsidies — such as output based aid (but also on a greater scale) built into the design of projects could make them more suitable for private sector participation through achieving the bankability which remains such a challenge to so many African PPPs.

In recognition of high risks and costs involved in preparing infrastructure projects, the donor community has been making resources available for project preparation activities, as reported by an Infrastructure Consortium for Africa (ICA) study (undertaken by CEPA). While the participants recognised that this support exists, it was agreed that it continues to be fragmented and limited in both scale and scope, given the costs associated with developing projects. The shortage of support for very early stage project cycle activities was particularly noted. Further work to support greater stakeholder co-ordination and awareness of this problem was strongly encouraged.

Finally, the participants agreed that a robust and continuous political commitment by the relevant governments, and their institutions, to support PPP projects is one of the most critical elements in seeing more such projects developed.

**Approaches to encouraging infrastructure PPPs**

The aim of the workshop was not to develop a definitive roadmap for PPP development. In the diverse national and regional circumstances of the SADC, HIPC and post conflict countries this would neither have been possible nor necessarily desirable.

There was a general agreement that the following issues are likely to be helpful in creating the environment for more PPPs to be developed in the African context:

- Governments and ministries were urged to work towards standardising PPP contracts and other relevant documentation, as well as sharing information and experience at an intra-regional level.
- Lack of sector-specific information, on demand and service usage patterns for example, is often cited by investors and project developers as one of the key impediments to greater involvement in African PPPs.
- Governments are called upon to recognise the limitations of PPP solutions, and in particular to recognise that the private sector’s involvement is dependent on their ability to earn a risk adjusted return and thus make a profit.
- In addition to contracts, long-term relationships with national and international investors are one of the key building blocks to successful PPP programmes.

**Issues for debate**

The workshop participants focused much of their attention on discussing three areas of debate as regards to the development of infrastructure PPPs in the SADC and wider African context. The first of these was related to the potential need for an entity which would act as an early stage facilitator of PPP projects, the second focused on the optimal institutional structure of PPP units aimed at supporting infrastructure PPPs, and the third on specific PPP project design issues.

**PPP facilitator**

A number of participants suggested that there is a need for a facilitating entity which would act as catalyst for the development of PPPs in developing countries. Such an entity, which may or may not be a party to the eventual PPP agreement, would focus on bridging the gap between national/regional policy objectives and initiation of PPP projects. This very early stage work is likely to entail raising awareness of the potential and limitations of the PPP approach, bringing interested parties together to begin discussions and generally acting as a facilitator of PPPs by reducing initial uncertainty and coordination costs. More specifically, this may entail securing initial government commitment (whether at a national or regional level), ensuring donor participation, promoting the project to private sector developers and carrying out preliminary information gathering exercises and relevant market analyses.

**PPP Units**

Within the context of a general consensus that more could be done to support PPP project preparation in Africa, DFRC presented the case for a new facility to support infrastructure PPP projects in the SADC region – the SADC Project Preparation and Development Fund (PPDF). It was suggested that the PPDF would be an integral part of the SADC Development Finance System, working closely with the existing regional DFIs and the DFRC itself. Its aim would be to prepare and take ownership over infrastructure projects from identification/conception, through feasibility activities, project structuring/packaging, appraisal and ultimate sale to private sector partners.

Although donor support does exist for project preparation activities, DFRC has argued that more support is required, particularly in the very early stages of project preparation. In particular, while African countries were eligible for most of the existing support, they had to compete for it globally. The proposed PPDF, on the other hand, would focus its efforts specifically on the SADC region.

Other participants raised concerns of growing donor fatigue for new initiatives and questioned whether greater initial mileage could be realised through better coordination of the activities of existing facilities.

Two further key questions were discussed in relation to PPP Units:

- Which project cycle activities should be performed by such units? The required skills to design PPP projects as well as monitor contract arrangements are often not readily available in line ministries, and an increasingly common way to provide this expertise has been through specialised PPP Units. Against this, concerns
were raised regarding the range of roles that such units might play, particularly in regards to project development, which is arguably the riskiest activity in the whole project cycle. The concern centred around the ability of essentially public servants to fulfil this role, which has traditionally been played by commercial entities who have their own capital at risk in the project. Activities further along the project cycle, such as feasibility studies and transaction advisory, have been suggested as potentially more suitable for such institutions to undertake – activities which are currently undertaken by DFIs such as the International Finance Corporation (IFC).

Another ongoing discussion concerns the potential for conflict in the roles of project promotion and appraisal. Proposals were put forward that a separation of sponsor and appraiser responsibilities should be promoted.

Finally, the participants also debated to what degree it is possible to reconcile the public sector procurement/management mindset, which is often focused on consumer protection, and the need to structure profitable opportunities for private sector investment.

Infrastructure PPP project design issues
The cornerstone of any PPP transaction is the transfer of some degree of risk from the public to the private sector. All participants agreed that the key to successful PPPs is the ‘appropriate’ risk transfer between parties, including:

- The transfer of the right kind of risks. Risks need to be managed by the parties best placed to manage them (e.g. construction or performance risk by the private sector and political risk by the public sector).
- The transfer of appropriate level of risk. An appropriate level of risk needs to be transferred to the private sector so that value for money can be achieved, but at the same time it is important to guard against excessive transfers of risk taking place which would render private sector partners uninterested or projects overly expensive (as risk mitigation is a cost built in by the private sector).

The debate also covered the balance between ‘fixity’ and ‘flexibility’ in PPP contracts, that is the need for legal certainty in contracts versus the need for the contracts to allow adaptation to new events and circumstances.

While the need for greater subsidies was recognised, the precise basis and justification for this – that is, the where and when – was less clear given the scarcity of such subsidy. While many donors have sought to target such subsidies as far as possible on the very poor, the case was made that the positive economic externalities of better infrastructure, irrespective of their precise incidence, created a case for greater use of subsidy. Most participants agreed that most infrastructure projects carry with them considerable positive, wider economic development externalities, which ought to be taken into account when appraising and supporting infrastructure PPPs. These include the wider economic benefits of better rural transport systems through improvements in local roads, greater power reliability in the country through building of a new power plant and/or public health benefits of a better sanitation system. It was recognised, however, that valuing these wider economic benefits is difficult. The onus is therefore on governments to make policy decisions on whether any recognised wider economic benefits would justify their financial support for projects whose projected revenues are deemed to be insufficient or overly risky for the project to go ahead on a standalone basis.

This paper draws heavily on a report prepared by Cambridge Economic Policy Associates (CEPA) which was commissioned by the Commonwealth Secretariat on the outcomes of the Sandton workshop, entitled Harnessing existing facilities to promote Public-Private Partnership for infrastructure investment and service delivery.

Key messages
- The key messages that emerged from the workshop are:
  - There is a need for better coordination between existing donor facilities which provide support for infrastructure project preparation in Africa.
  - More resources are required to support early stage infrastructure project preparation in Africa.
  - A need may exist for some form of a PPP infrastructure facilitator to raise awareness of PPP approaches, bring different parties together and generally reduce coordination costs at the very early stage of PPP project development.
  - When creating PPP Units it is important to take account of the possible conflict of interest between the two roles often assigned to such a unit – that of a project sponsor and appraiser. A separation of these two responsibilities should be encouraged.
  - Greater scale of ODA flows into the economic infrastructure is required, whether to support public sector or PPP infrastructure projects.

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