EUROPEAN PARLIAMENT

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES

POLICY DEPARTMENT

CRITERIA FOR DIFFERENTIATION AND METHODS FOR PHASING OUT EU'S DEVELOPMENT COOPERATION FOR THE NEW DCI

DEVE

EN

2012

EUROPEAN PARLIAMENT

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES OF THE UNION

DIRECTORATE B

POLICY DEPARTMENT

STUDY

CRITERIA FOR DIFFERENTIATION AND METHODS FOR PHASING OUT EU'S DEVELOPMENT COOPERATION IN LIGHT OF THE COMMISSION'S PROPOSAL FOR A DEVELOPMENT COOPERATION INSTRUMENT (DCI) FOR 2014-2020

Abstract

The European Union has expressed its intention to concentrate its development aid resources where they are needed the most. To this purpose, the Commission has proposed to apply national per capita income-based criteria for the identification of countries that may no longer qualify for EU bilateral aid under the Development Cooperation Instrument for the 2014-2020 Multiannual Financial Framework. With the new scenario, the EU aspires to end poverty reduction-focused aid allocations to highly heterogeneous 'graduated', middle-income countries that house large amounts of poor people. The present briefing assesses actual and alternative criteria against which the EU could better adapt to the changing global geography of poverty. Furthermore, it explores the prospected impacts that a potential cut of bilateral aid may entail for 'graduated' countries and for the Union itself. Given the risk of loosing bilateral aid focal points in developing countries and the non-development nature of the Partnership Instrument, a strategic adaptation period is proposed, during which a more comprehensive and coherent EU global development policy capable to impact the people most in need could be adopted. This should encompass a transition toward a stronger focus on social cohesion, arguably the Achilles' Heel of most middle-income countries, as they progress on their economic development.

EXPO/B/DEVE/FWC/2009-01/Lot5/27 May 2012

PE 433.782 EN

This study was requested by the European Parliament's Committee on Development.

AUTHOR:

Dr Josep M. COLL, Senior Research Associate, EUROPEAN STUDIES UNIVERSITY INSTITUTE (AUTONOMOUS UNIVERSITY OF BARCELONA), SPAIN

Coordination provided by Ecologic Institute.

ADMINISTRATOR RESPONSIBLE:

Fernando GARCÉS DE LOS FAYOS
Directorate-General for External Policies of the Union
Policy Department
WIB 06 M 077
rue Wiertz 60
B-1047 Brussels

Editorial Assistant: Györgyi MÁCSAI

LINGUISTIC VERSIONS

Original: EN

ABOUT THE EDITOR

Editorial closing date: 16 May 2012.

Printed in Belgium

ISBN: 978-92-823-3741-7
Doi: 10.2861/81545

The Information Note is available on the Internet at
http://www.europarl.europa.eu/activities/committees/studies.do?language=EN

If you are unable to download the information you require, please request a paper copy
by e-mail : poldep-expo@europarl.europa.eu

TABLE OF CONTENTS

EXECUTIVE SUMMARY

Busan's High Level Forum on Aid Effectiveness reaffirmed the emergence of a new aid paradigm that is changing the pendulum from traditional aid to global development partnerships toward the provision of global public policies. This phenomenon is accompanied by a major shift in the global geography of poverty: currently, an overwhelming majority of poor people currently concentrated in middle-income countries (MICs). However, the EU's concern to allocate aid resources to the poorest countries clashes with this evidence. The proposed EC differentiation criteria, based in per capita income country classifications, do not capture the heterogeneity of the new poverty landscape.

This notwithstanding, alternative criteria based at focusing aid allocations also on large pockets of poor people offer a more coherent benchmark against which sorting development assistance to MICs. These criteria emphasise the relevant role that the latter countries play in a multilevel development dynamic. First, they potentially act as poles for regional development, thus encouraging spillover effects in spurring development in surrounding countries. Second, their synergetic cooperation with official donors renders substantial gains in terms of forwarding knowledge transfers to lower income countries (LICs). Third, MICs engagement with official donors in contributing towards the provision of global public goods (GPGs) is critical for addressing developmental global challenges through a mutually beneficial framework of cooperation. Fourth, MICs can become a key ally in leveraging policy coherence for sustainable development in third countries, beyond the scope of developed countries' policies.

Although EU bilateral aid relatively represents a very small share amongst MIC's non-aid dependent national budgets, there are prospected impacts which deserve consideration when assessing the suitability to apply certain differentiation criteria; in particular, the risk of turning away from addressing MICs' arguably major challenges: inequality and social cohesion. Furthermore, the potential cut of EU bilateral aid vis-à-vis MICs as a way to maximise its impact may be misplaced. Beyond the fact that MICs house a majority of the world's poor, there is no evidence unambiguously linking the degree of impact of aid on poverty reduction to the per capita income level. Indeed, reducing the percentage of poor largely depends, inter alia, on the extent of inequality and on how poor the poor are –i.e. the poverty gap.

All in all, the EU needs to fine-tune its development policy toward MICs. Its development assistance can play a catalytic, supporting role in addressing inequality and fostering inclusive development through redistributive policies, institutional reform and increased competitiveness. Building upon MICs' transition from aid to mainly technical support, and given the Partnership Instrument (PI) - DCI 'focus gap' resulting from the EC proposal, it is recommended herein to envisage a strategic adaptation period (SAP). This should encompass a new aid paradigm, new types of development cooperation, alternative financing mechanisms, and a renewed development agenda with MICs. Against this backdrop the EU could better exploit its potential to leverage policy coherence for development beyond developed countries' scope. Moreover, it can gain in terms of increasing development effectiveness and in promoting its comparative advantage as a global player.

1. BACKGROUND

1.1 A New Global Poverty Landscape

In the last two decades, rapid economic growth in highly populated countries has brought about a major shift in the global poverty landscape. While in the early 1990s 93% of world's poor lived in Low Income Countries (LICs), this pattern has now drastically changed with the vast majority of poor people (72%) living in Middle Income Countries (MICs).[1] This new geography of global poverty carries important implications for aid agencies. It questions a widely extended model of development assistance where aid allocations crucially hinge upon country classifications of per capita national income.

Furthermore, recent years have seen the rise of new development cooperation approaches aside of the traditional bi- and multilateral OECD-DAC[2] model. The proliferation of emerging economies among developing countries - BRICS and N11 nations,[3] has contributed to foster the outreach of the former's external activities. Their foreign policy objectives vis-à-vis partners within the developing world aim at boosting their political and economic weight in an increasingly multipolar global order. This phenomenon has given rise to rapidly developing forms of South-South and triangular cooperation.

Likewise, there are new cooperation trends regarding development financing, with the rapid increase of private flows and the engagement of non-state actors. These flows come from a more prominent role of for-profit organizations in development, the increase of charities and philanthropies, and the appearance of new forms of development financing, public-private partnerships and vertical funds.

The development community is well aware of the aforementioned new realities. In the last High Level Forum on Aid Effectiveness held in Busan, the main highlights were the recognition and inclusion of the new forms of cooperation and actors into the overall attempt to eradicate global poverty and inequality. Indeed, the Forum was a tipping point for adopting a global approach to effective development beyond aid. This new paradigm draws the transition from effective aid to effective development cooperation, thus responding to an international cooperation agenda increasingly focused on the provision of Global Public Goods (GPGs). This evolution entails a more holistic and multidimensional conceptualisation of poverty reduction as part of a global public policies' approach. It sets up the bedrocks for identifying the inter-relations and fostering coherence among the wide spectrum of public policies concerned with development that go well beyond poverty reduction,- i.e. environment conservation, climate change, public health, peace and security, migration and other critical issues for both developing and developed countries.

---

[1] Kanbur and Sumner (2011).

[2] Development Assistance Committee of the Organisation for Economic Co-operation and Development.

[3] BRICS: Brazil, Russia, India, China and South Africa; N11: Bangladesh, Egypt, Indonesia, Iran, Mexico, Nigeria, Pakistan, Philippines, Turkey, South Korea, and Vietnam.

1.2 The Evolution of the EU's Development Policy

Against this backdrop, bilateral and multilateral aid agencies need to adapt to the new development landscape. In line with the 2005 European Consensus on Development's (ECD) primary objective of poverty eradication, the European Commission (EC) supports the allocation of aid resources where they are most needed. The ECD stresses the importance of prioritising the poorest countries, i.e. Least Developed Countries (LDCs) and LICs. This notwithstanding, it does recognise the importance of continuing to support development and addressing poverty reduction in MICs.

The EC reflects the political will to adapt to these global challenges in its Agenda for Change[4], which is in line with the Lisbon Treaty and to some extent with the EU-2020 Strategy[5]. Specifically, the Agenda for Change emphasizes the need to 'target the resources where they are needed most to address poverty reduction and where they could have greatest impact'. This leads the Commission to focus aid allocations on the poorest countries rather than on countries that are in a growth pattern toward manifest economic development. As a result, it introduces a country-differentiated approach to determine aid allocations and the type of partnerships.

Differentiation will chiefly affect the DCI and the European Neighbourhood Policy Instrument (ENPI). According to the new EC proposal for the DCI, countries producing more than 1% of the world's GDP or Upper MICs[6] (UMICs) will in principle be excluded[7]. The allocation criteria intends to take into account the potential impact of the EU in promoting political, social, economic and environmental reforms and in increasing the leverage effect on development finance. Under these criteria, grant-based bilateral aid will likely be cut from a sample of "graduated" countries[8]. They comprise 11 Latin American and 8 Asian countries[9] when the new MFF enters into force in 2014.

2. CRITERIA FOR DIFFERENTIATION

According to the ECD, global geographic and thematic allocations must use 'standard, objective, and transparent resource allocation criteria based on needs and performance'. Regarding the new geography of global poverty, the proposed criteria exclude a large number of MICs, which host many of the world's poor by limiting the analysis to average macro-socioeconomic indicators. As a mode of example, excluding the number of people living below the poverty line in the "graduated", non-eligible countries of India, China and Indonesia means that the DCI will not target 55% of the world's poor[10]. Indeed, the concentration of poor people in a reduced number of MICs is apparent. Suffice to note that

---

[4] European Commission (2011). Increasing the Impact of EU Development Policy: and Agenda for Change. Communication. October. In: http://ec.europa.eu/europeaid/what/development-policies/documents/agenda_for_change_en.pdf - 10 April 2012.

[5] Arguably, whereas economic, social and territorial cohesion is a fundamental part of the internal EU 2020 strategy, the Agenda for Change is devoid of all reference to cohesion despite its earlier consideration in the preceding Green Paper.

[6] According to the list of recipients of ODA of OECD/DAC.

[7] However, additional criteria relating to their needs and capacity is used: Human Development Index, Environmental Vulnerability Index, aid dependency, economic growth and Foreign Direct Investment.

[8] The term "graduated" refers to the countries that would no longer be funded from EU bilateral aid under the EC's proposed DCI.

[9] 17 UMICs: Argentina, Brazil, Chile, China, Colombia, Costa Rica, Ecuador, Kazakhstan, Iran, Malaysia, Maldives, Mexico, Panama, Peru, Thailand, Venezuela and Uruguay; 2 LMICs with GDP larger than 1% of world GDP: India and Indonesia; 2 Exceptions: South Africa and Cuba.

[10] Based on World Development Indicators in Sumner (2010).

the so-called PICNICs (Pakistan, India, China, Nigeria and Indonesia) alone currently house up to 64% of the world's income poor.

Actual aid allocations are mostly based on quantitative criteria mainly linked to per capita income country classifications. This is carried out under the assumption that targeting aid to poor people in lower income countries is the most efficient way of reducing poverty. The criteria against this assumption argue that LDCs and LICs have a higher share of poor people than MICs. They are, therefore, more in need of aid than MICs as they have limited capacities to raise their own financial resources for development.

In practice, most allocation decisions are also shaped by donor-specific factors beyond the recipient's needs and generally suffer from a lack of coordination. This has led to some of the poorest countries being below-averagely aided -aid orphans- whereas others remain over aided -aid darlings. To tackle these funding disparities and accommodate the related Accra Agenda for Action (AAA) commitment 'to address the issue of countries that receive insufficient aid', an abundant literature has emerged over the last decade focusing on optimal aid allocation. Most recent discussions have obviously gravitated over the need to reduce or discontinue development assistance to heterogeneous[11] MICs with large pockets of poverty and whose per capita income has increased substantially.

Currently, there are two main strands in the literature providing criteria to differentiate aid allocations by donor agencies. The first strand draws on poor countries' macro- and socioeconomic average performance as the benchmark against which current aid allocations are assessed. The second strand provides some benchmarks that argue in favour of aid allocations accounting for the new geographic reality of global poverty based on the targeting of poor people, regardless of the poverty status of their country. While the former criteria hinge upon quantitative indicators such as –and mainly- national per capita income, or other poverty-related indicators, the latter focuses on the qualitative aspects that might be taken into account for a more coherent and integrated approach to global development.

2.1 Benchmark Criteria Based on Poor Countries

Geared at providing objective, standard and transparent criteria, the normative literature on aid allocation offers several approaches that broadly fall into three categories: the needs-based approach (implicit in the UN's plan to achieve the MDGs), poverty-efficiency and equal opportunity-based allocations. More specifically, Utz (2010) provides a compilation of aid allocation criteria classified into the following categories:

– **Egalitarian allocations**: each country receives the same proportion of aid, either in per capita terms or as a share of the GDP. Through the simplest allocation rule, larger countries would generally receive more aid than smaller ones.

– **Needs-Based Approaches and Performance**[12]: the allocation formula is a function of the proportion of people under the poverty line (headcount ratio); per capita income (to reflect the country's needs); the World Bank's Country Policy and Institutional Assessment (as a measure of performance); and the population (to capture the population bias in aid allocations).

– **Poverty-efficient allocations**: Collier and Dollar (2001) suggest a formula that links poverty with policy reform. This criterion assumes that the impact of aid on GDP growth is positive and

[11] Lower MICs versus Upper MICs; global player MICs versus small-sized MICs.

[12] In Utz (2010) this criterion is named 'allocations reflecting average donor behaviour'.

significant in LICs with a good policy environment. The rationale behind this criterion is that maximising global poverty reduction requires that aid be allocated where the marginal cost of poverty reduction is theoretically lowest, i.e. in LICs with good governance. This criterion, however, disregards the fact that pulling people out of poverty is not necessarily cheaper in poorer countries with good governance. In order to determine the cost of lifting the poor out of poverty in a given country, attention should also be paid at the distribution of incomes under the poverty line, something that is captured by the poverty gap index (PG).[13] It is thus possible that in fact a country with higher per capita income would more cheaply reduce the number of poor by the simple fact that many of them are just below the poverty line (low poverty gap), whereas a poorer country may have a higher proportion of poor with incomes well below the poverty threshold.

A relative to poverty-efficient allocations, **International Development Association's (IDA) performance-based allocation PBA** is used as the reference by multilateral development banks. The criterion assesses the relative weights to be assigned according to countries' needs and performance. Poverty selectivity is earmarked through IDA's operational cut-off point in terms of per capita income. Performance is measured through the Country Performance Rating (CPR). Thus, poorer countries with the same level of CPR receive more assistance.

This notwithstanding, the existing literature highlights other non-objective criteria that are taken into account by how aid agencies upon deciding where to assign their aid allocations (Hoeffler and Outram, 2008). Mixed with developmental objectives, strategic economic and political goals are also mainstreamed by official donors. This behaviour is more pronounced in bilateral agencies than in multilaterals. The former tend to discriminate their allocations by giving more weight to ex-colonial ties, trade relationships or foreign policy issues. However, this trend has been progressively diminishing over the last decades (Claessens, Cassimon, van Campenhout, 2007).

The aforementioned criteria share some key features that are critical for their application in aid allocation decisions and which reflect, to a certain extent, some shortcomings of the decision processes themselves. First, they are all conceptualised within a context where poor people are concentrated in LDCs and LICs, not in MICs as it is the case nowadays. Hence, they do not capture the changing dynamics of the global geography of poverty. The benchmark criteria based on poor countries also suffer from a certain country bias. Per capita aid tends to be larger for less populated countries. Second, there is no international consensus on the standard criteria that should be used to decide bi- and multilateral aid allocations. This fact is a relevant sign that reflects the weak coordination amongst official donors. Under this principle, it is not surprising that aid orphans coexist with aid darlings. Indeed, insufficient aid depends on the preferred modality of aid allocation and the weight that individual allocation rules place on performance needs.

---

[13] The Poverty Gap (PG) or *intensity of poverty* measures how far below the poverty line the average income of the poor falls as a proportion of the poverty line itself. Thus, in the two extremes, PG = 0 (0%) if there are no poor and 1 (100%) if the poor have an average income equal to zero. A PG = 0.5 (50%) indicates that in average the poor have an income equal to half of the poverty line. This index provides crucial additional information to the percentage of poor people (Headcount Index). For instance, it helps to differentiate between two countries with the same percentage of poor but very different average income among them. A country where the poor have an average income just below the poverty line is much better off than another one where –even if their proportion of poor people were similar- the poor's average income is well below the poverty line.

Furthermore, these allocation criteria are based on the inherent assumption that development assistance must flow to the countries with a larger share of population living below the poverty line (higher headcount ratio). These countries are often aid dependent. Then, why should aid flow to countries that have enough home-grown resources but do not address their high levels of inequality?

2.2 Benchmark Criteria Based on Poor People

With the new global geography of poverty an uncontested reality, there is a robust development literature following a rationale that stresses the importance to continue development assistance to the MICs given the fact that these host most of the poor. Kanbur and Sumner (2011), Glennie (2011) and Carbonnier and Sumner (2012) forge a rationale that is compounded by a set of arguments that qualitatively provide some benchmark criteria. As a whole, they are conceived as a blueprint for adapting the official donors' aid agencies policies and aid allocations' decisions to the dynamics of an evolving development paradigm.

- **Pockets of poverty**: As most poor people live in MICs, any strategy aimed at addressing global poverty needs to target these countries, regardless of their per capita income. This view is grounded on the commitment to offer assistance to poor people, independently of whether they live in LICs or not. Indeed, the argument rests in the following principle: if wealthier income per capita MICs have not been able to eradicate their pockets of poverty is partly due to the ineffectiveness of development assistance in reaching the poor (either because of a lack of means or capacity for targeting the poor). Some of the recently graduated countries have shown weak signs of resistance towards external shocks and, in some cases, have even fallen back to LICs status, as discussed further down in section 4.
- **Spillover effects**: MICs are important regional hubs that act as 'poles for regional development' (Glennie, 2011). They foster cross-border and global spillovers and they play a decisive contribution to strengthen regional integration processes. Indeed, in the recent financial crisis, the decisive role that MICs played in supporting their surrounding poorer countries has been widely acknowledged. The benefits of the spillover effects have included debt relief, well-developed trade relations and remittances, technical assistance, public administration reform or humanitarian assistance (Glennie, 2011).
- **Knowledge transfers**: Related to the spillover effects, the synergetic cooperation of official donors with MICs entails substantial gains in knowledge that can be useful for the development process of LDCs and LICs. These gains are exemplified as some of the externalities generated as a result of triangular patterns of cooperation between official donors, MICs and LICs. The example of knowledge gains in the operation of safety nets in MICs is often held by the WB as useful for addressing poverty reduction in LICs. Furthermore, official donors can assist MICs in reducing inequality and thus poverty at home by the replication of successful experiences through knowledge sharing and the provision of expertise and technical cooperation in seeking new financial mechanisms, the design of social inclusion and redistributive policies (e.g. the EC with its comparative advantage in regional integration or its own social model).
- **Cooperation/Contribution towards the provision of GPGs**: A global commitment and decisive engagement of MICs in the design and implementation of Global Public Goods is one of the major innovations among the international development community to tackle global developmental challenges. In Busan, donors agreed to foster a global partnership aiming at improving effective development approaches beyond aid. Development cooperation with MICs represents for official donors a means to promote GPGs. Given the intertwined nature of global

challenges with poverty reduction, the design and implementation of GPGs can serve as (i) a policy framework between official donors and MICs; (ii) incentive alignment by meeting the interests of High Income Countries (HICs), MICs and LICs; and (iii) the conceptualisation of MICs as proactive stakeholders in a horizontal partnership relation rather than the classical conceptualisation of mere aid recipients in a paternalistic relationship. Official donors' cooperation with MICs in terms of promoting alliances to safeguard the provision of GPGs can significantly contribute to strengthen the increasingly relevant weight that MICs have in improving global governance in benefit of sustainable development.

– **Policy coherence for sustainable development (PCD)**: Making use of a broad range of policies within different areas is critical to address global development. Thus, policy coherence is subject of the interest of not only official donors –as it has been often conceived by aid agencies-, but for MICs themselves. PCD is highly relevant for the lattter both in terms of spurring domestic and international global public policies, and strengthening their foreign development assistance programs. The EC, a strong advocate of PCD within the EU, could play a catalytic role in assisting MICs in the development of their own policy coherence guidelines, as well as in jointly contributing to increased global policy coherence.

In practical terms, this study recommends that three key qualitative criteria be used to decide which countries should remain in the future DCI. Following the argument that combating inequality should be the main focus of a development cooperation strategy vis-à-vis MICs, it would seem plausible to establish that EU's development efforts with these countries takes place if and only if: i) they present high income inequality –which could be considered as a Gini coefficient above 45%; ii) they are willing to address inequalities issues; and iii) the EU retains certain potential for leverage. This set of three qualitative criteria can, in practice, help to complement quantitative criteria that remains, almost by definition, arbitrary.

These arguments provide a relevant, consistent and a robust rationale for supporting an adapted EU development assistance to newly graduated countries in the frame of the future 2014-2020 DCI 2014-2020. The following section offers an assessment of the prospects for impact of cutting-off EU bilateral aid to the proposed 'graduated' countries.

3. POTENTIAL IMPACT OF CUTTING EU AID TO GRADUATED MIC

Undoubtedly, development aid in MICs represents a very small share of the overall public resources needed to finance their own development. Most of them have recently experienced an economic growth expansion era, whereby generating substantial financial resources that could potentially be allocated for development purposes. Arguably, EC assistance allocated to MICs has a marginal effect, particularly if one takes into account the economic impasse and perspective of development financing. This is precisely the argument that Commissioner Piebalgs has defended: "some countries can now afford to fight poverty themselves and, as a result, this will allow us to focus on places that need more of our help."

Beyond this debate, and against the envisaged scenario of substantially cutting bilateral aid to 'graduated' countries from 2014, there are relevant potential impacts that should be taken into account in order to better decide suitable criteria to guide the future allocations of aid under the forthcoming EU's MFF 2014-2020. These potential impacts may affect both 'graduated' MICs as well as the European Union, a distinction that is accounted for in the following.

3.1 Prospected Impacts in "graduated" MICs

Currently, some of the people who find themselves in MIC's poverty pockets arguably suffer from a similar extent of deprivation than other poor people living in LCDs and LICs do. A recent study (Alkire and Santos, 2010) found that 8 states of India, for example, accumulate more poor people than the whole Sub-Saharan Africa as per the Oxford/UNDP Multidimensional Poverty Index[14] (MPI). They are facing serious problems in the provision of basic public services (health, water, sanitation, food, education, among others). Indeed, Jha and Negre (2007) point out that it may well be the case that the total number of those who are at the bottom of the pit in India is larger than the total population suffering from comparable deprivations in Sub-Saharan Africa.

The bulk of more recent literature on the relation between growth, poverty and inequality appear to point to the fact that such countries' most pressing developmental constraint is their high inequality levels (Carbonnier and Sumner, 2012). Large income disparities seriously challenge the social cohesion within their territories, a critical factor for achieving institutional capacity to design and implement effective policies aimed at poverty reduction (Easterly, 2006). Thus, policies aimed at addressing this structural issue may require significant support from the development community. In this regard, a potential cut of EU aid could weaken the capacity of MICs in raising public awareness and political support for the design and implementation of redistributive and inclusive development policies and measures targeting the afflicted poor as a top priority (Melamed, 2010). That is, if the EU was to adopt a more assertive role in promoting social cohesion and pro-poor policy interventions within the framework of its development cooperation, particularly with MICs. By introducing differentiated partnerships, CONCORD (2012) points out the risk of turning away from the fight against poverty and inequality.

In the same vein, the proposed aid-cut to the aforementioned MICs endows the assumption that the EU has found new alternatives to cooperate with them in tackling global and regional challenges. However, the Partnership Instrument, an update for the re-branded Instrument for Industrialised Countries, is rather targeted at fostering cooperation -in the areas of climate change, growth, finance and trade- to promote 'mutual interests and give the Europe 2020 strategy a global reach' (Gavas, 2012). In this regard, it appears difficult to envisage the sustainability of a graduation approach whereby there is no monitoring period after graduation to make sure countries do not experience reverse developments. This is particularly so for many MICs whose present good economic performances might be the product of short- or medium-lived growth spells, as it has historically been the case for many a developing country in the past. In fact, the World Bank has already projected lower growth for the immediate future due to the present financial crisis, whose effects are expected to impact developing countries.[15]

On the other hand, the EU often positions itself as a donor with a particular comparative advantage in specific areas. Thus, MICs may miss a key partner to work toward regional integration, Policy Coherence for Development, official aid donor coordination and systematic approaches to GPGs -such as environment conservation, climate change or food security- would yield more consistent results in the frame of a strategic development partnership between the EU and MICs.

---

[14] The MPI developed by the Oxford Poverty and Human Development Initiative is the product of two numbers: the headcount ratio (income poverty) and the average intensity of deprivation (non-income poverty). It was featured in the United Nations Development Programme 2011 Human Development Report.

[15] World Bank (2012).

For some of the MICs, particularly Lower MICs, the EU's halt to bilateral development cooperation will imply a significant loss as it is a relevant donor with proven expertise and value added in certain fields. Its absence may not go unnoticed as in many cases EU's contribution made a difference. Additionally, given that the EU is a key player and not simply one more donor, its withdrawal from graduated countries in the area of poverty reduction may have an important impact as this may encourage other countries to take similar steps, particularly among EU Member States.

3.2 Prospected Impacts for the European Union

The aforementioned impacts on MICs, although relevant in the context and content, are limited by the relatively small financial contribution of EU's aid flows to MICs in absolute terms. However, the likely impacts of cutting EU aid to 'graduated' countries are more relevant and meaningful for the EU itself. These impacts have implications for the Union from both a development-centred and a broader foreign policy perspective.

Through a developmental lens, a reduced implication with MICs would likely involve substantial prospects for a diminished global field presence of the EU, weakening one of the most prominent comparative advantages of the EU at global level. This is especially apparent in Latin America, the most affected area if the new criteria are adopted with 11 countries falling off EU's DCI partners. For the EU, lacking a permanent focal point in large MICs, with a fast-increasing global presence, can hamper the implementation of strong development, poverty-oriented partnerships. It may also potentially weaken prospects of promoting EU values such as democracy, good governance and human rights that are intrinsically linked to development. In light of the Busan Partnership for Effective Development, the new situation can represent a significant shift on the nature and consistency of development partnerships between the EU and large-populated MICs.

Bearing in mind the issue of aid effectiveness (Paris, Accra, Busan), the possibility of weakening permanent development focal points on the ground undermines the improvement on effective development, the Achilles' heel for the EU - and other official donors. This fact, along with the lack of concrete development focus of the proposed PI, can generate an aid gap affecting vulnerable poverty pockets in 'graduated' countries. The extent of such prospect is obviously related to the poverty-situation of the given country, which largely differs upon UMICs and LMICs.

It is widely acknowledged in the development community that the effect of aid is positively correlated to the quality of policy. As a consequence, 'aid would be more effective if it were either more systematically targeted to poor countries with sound economic reform programs or used to promote good policies' (Santiso, 2001). Research by World Bank economists Burnside and Dollar (2000) on the impact of aid, policy and growth thoroughly argues that aid has substantially contributed in reducing poverty and promoting growth in developing countries with 'sound economic management and robust government institutions' (Santiso, 2001).

It is also true that aid cannot buy reform and automatically induce policy change. However, when reforms have been initiated, foreign assistance helps accompany reform and assuages social costs of adjustment. This why the World Bank's 1998 report 'Assessing Aid: What Works, What Doesn't and Why' recommends a more systematic targeting of aid to poor countries with sound policies and effective institutions.

In sum, incrementing the impact of aid by concentrating it in the poorer countries does not happen mechanically. The very fact that sound policies are mostly to be found in MICs may appear to contradict the Commission's approach, seeking to increase the impact aid by allocating it to poorer countries.

This aspect is closely intertwined with the possibilities that EU development assistance to MICs offer in fostering PCD. In the progressive transformation of the aid system to the global public polices' framework, it may appear sensible to maintain development assistance for poverty reduction as part of the overall attempt to address global challenges through the provision of GPGs. As a result, it is likely that the EU may weaken its potential to foster coherence amongst global developmental polices (environment, climate change, migration, security, trade), which are all closely linked to poverty issues. In fact, cutting off EU bilateral aid with MICs could hamper the generation of synergies and weaken the flow of leverage effects between the wide-range of developmental programs and actions implemented through thematic and regional budget lines and the PI, especially taking into account low poverty profile of the new instrument.

Along these lines, the fact of withdrawing bilateral development assistance to MICs may weaken the chances of attaining the global targets for achieving the MDGs if crucial support to social programmes is withdrawn. In fact, the EU has been fully committed to this endeavour, with an explicitly acknowledgement in the ECD. This states that "support to middle-income countries also remains important to attaining the MDGs." Regarding the close 2015 deadline for meeting the MDGs, EU's development policies may arguably be exposed to a higher risk of failure with the proposed allocation criteria expected to apply from 2014.

Last but not least, the proposed scenario is likely to weaken the EU role in the world. From a foreign policy perspective, the rise of MICs in the South is rapidly altering the geopolitical landscape. Considering the strategic role of EU's development cooperation as part of its foreign policy outreach, the fact of terminating its bilateral development cooperation scope with MICs to 19 countries would imply decreased opportunities to strengthen the links with South Asia and Latin America. Less leverage power on development-related issues (e.g. security, trade, migration) would be detrimental to the successful addressing of these issues.

4. ADAPTING THE TYPES OF DEVELOPMENT ASSISTANCE TO MICS

The new reality of aid, as mentioned in section 1, hinges upon two inexorable dynamics. First, the rapid evolution of a new aid landscape and second, the shift in the new global geography of poverty. The international aid architecture is moving from a traditional system characterised by paternalistic relations of aid to a global development partnership geared toward the provision of GPGs. As such, aid and poverty reduction are part of the global overall attempt to attain sustainable development.

Against this background, the global effort to eradicate poverty would appear to suggest the convenience to not discontinue EU's development assistance to 'graduated' MICs with poverty ratios or large absolute number of poor. However, the extension of such cooperation should reflect the new aid reality and therefore might be targeted at adapting development cooperation policies and schemes to this new paradigm. The transitional component of this assistance could thus be extended so as to ensure that prospective negative impacts regarding a potential exclusion are avoided. The 'raison d'être' of a phasing-out period (POP) is to pave the way for a smooth transition from aid to non-aid support to increasingly wealthier, self-financed countries, in accordance with the gradual nature of the growth process itself –in per capita terms. Thus, the setting up of a strategic adaptation period rather than a phasing out would maintain development cooperation with MICs, but transforming its development approach to better capture the dynamics of the new development paradigm.

4.1 Structure of a Strategic Adaptation Period

A transitional period should necessarily depend on the poverty context and the quality of the policy framework of the MIC under consideration. A potential strategic adaptation period (SAP) is advised in a multi-level, sequential, and non-excluding phase. This means that the three levels mentioned below can all be taken into account simultaneously –multi-level, while giving more priority to the initial levels related to the mitigation of the vulnerability of the given country -sequential. The fact that the assistance concentrates in one level needs not necessarily imply the exclusion of assistance to the other levels of cooperation –non-excluding.

Thus, firstly the SAP should be aimed at minimising the risks of the MIC falling back to LIC status, especially regarding its high vulnerability to external shocks[16]. Would then EU's development cooperation in this country automatically restart? Secondly, a SAP might avoid the risk of aid crowd-out, i.e donors flight from a given country. It should be aimed at guaranteeing an efficient allocation of budget resources by the 'graduated' country to poverty reduction and addressing other social deprivations be the neediest. Thirdly, a SAP should support redistributive development policies that are fully owned and currently addressed by the given country and encourage or foster them there where they are insufficient.

MICs face the overarching challenge of improving their mostly unequal distribution of resources throughout inclusive development and growth policies aimed at addressing high inequality and poverty, while activating excluded sectors from the growth dynamics. With this primary objective, a SAP could serve as a channel to adapt the role of the EU as official donor with an updated development aid function. Thus, development assistance in 'graduated' countries should play a catalytic, non-financially essential role (Glennie, 2011) for incentivising social inclusiveness and pro-poor growth at domestic level. Depending on the development status of the country, it could act as a driver for change and/or consolidation of sustainable progress.

Concretely, the EU could tailor the content and structure of MICs' Country Strategy Papers and Multi-Annual Indicative Programs by including specific objectives for a potential SAP during 2014-2020. First, it might reflect the increased commitment of the EU in supporting inclusive development through the assistance in the design and implementation of inclusive and redistributive policies, particularly bearing in mind that the most negatively affected continent by the proposed DCI allocation exclusions is also the most unequal one. Second, the EU has the opportunity to strengthen development partnerships with MICs beyond the scope of traditional aid schemes and towards the promotion of effective development. Third, it can reinforce the engagement of the EU in strengthening development triangulation with LDCs and LICs with a special focus on regional integration. Fourth, the EU can assist MICs, at a strategic level, in the provision of policy advise focused on improving policy coherence for sustainable development (Glennie, 2011; Carbonnier and Sumner, 2012).

[16] Between 1978 and 2003, 25 countries fell back from MIC to LIC status (WB country classifications in Glennie, 2011).

4.2 Types of Development Assistance to MICs

In case an adaptation period was to be included for the graduating MICs in the next Multiannual Financial Framework, the EU should opt for a type of development assistance that accommodate the aforementioned innovations taking place within the international development system in line with the main trends that were discussed in Busan and the EU's regulatory development framework. As presently conceived and to a certain extent, there is consensus in the need to adapt traditional aid-based approaches to new forms of cooperation with MICs. Aligned with the pursuit of social protection floor policies[17] (ILO, 2011), these may include the following:

- **Progressive Tax Reform**: official donors can assist MICs in building the capacity for orienting fiscal policies towards a better distribution of resources for poverty reduction purposes, with the particular aim of expanding MICs historically narrow fiscal bases. A recent work led by Ravallion (2010) estimates a marginal tax rate required to end poverty in MICs,[18] although such approach is dependant on each country's poverty context and public management capacity. The UN (2009) notes that technical cooperation could be provided in three main areas: (i) design of reforms, (ii) technical and institutional strengthening of tax administration system and (iii) cooperation in double taxation and tax fraud. All in all, a strong support to more progressive tax policies might entail a thorough assessment of the possibilities to involve the new middle classes. The alignment of their preferences with tax reform's goals is critical for the success of redistributive policies (ILO, 2011).
- **Conditional Cash Transfer Programs**: despite the novelty of this kind of programs, cash transfers to poor people are rendering substantial positive impacts in MICs. Soares et al. (2009) find that such schemes have cost less that 1% of GDP and contributed to reduce inequality by 15-21% in Brazil, Mexico and Chile, as in most of Latin America. An appropriate targeting of potential beneficiaries and the right complementary provision of basic social services are outlined as the critical factor of success for these programs. They can be approached as part of MICs' social safety net policy (López Calva and Lustig, 2010).
- **Strengthening International-Domestic PCD**: the EU can play a relevant role in fostering the positioning of PCD at the top of MICs' political agenda. Specifically, it could provide technical cooperation and policy advise in increasing the focus of the developmental content of those poverty-related areas: structural and regulatory issues, ensuring closer synergies between trade and development, adapting intellectual property rights, increasing the voice of MICs in multilateral development banks or improving the management of migration and remittances.
- **Crowding-in Public-Private Resources**: in most MICs, stable political environments and prosperous macroeconomic frameworks are prominent features. Within them, aid can play a catalytic role for incentivising private funds to crowd-in through pro-poor growth projects with a pattern of collaboration based on public-private partnerships. Fitting this category, blending of grants and loans, despite the limited empirical evidence of its effectiveness in practice so far (Gavas et al. 2011), it is increasingly recognised as a financial mechanism that can contribute to leverage large-scale infrastructures, institutions and services geared to development. In the same

[17] The Bachelet's report defines that social protection floors 'aim at facilitating effective access to essential goods and services, promote productive economic activity and be implemented in close coordination with other policies enhancing employability, reducing informality and precariousness, creating decent jobs and promotion entrepreneurship' (ILO, 2011).

[18] Ravallion (2010) argues that most countries with an average per capita income over USD4000 would require small additional taxation to end poverty.

vein, it can foster the involvement of the private sector in a more systematic approach to support entrepreneurial schemes oriented to the development of the poorest.

– **Boosting the role of Civil Society Organizations (CSOs)**: addressing inequality, reducing exclusion and promoting social cohesion requires the decisive participation of CSOs (Carbonnier and Sumner, 2012). Official donors could strengthen a decentralised approach of cooperation aimed at empowering CSOs that drive the change in domestic political processes towards poverty reduction and inclusive development. Such cooperation might be fostered by co-funding schemes in order to secure ownership and incentives alignment.

More generally and as stressed in a recent European Parliament study commissioned by its Development Committee[19], a new paradigm may be needed for development cooperation vis-à-vis MICs which does not betray the principle of poverty reduction. Contributing author Sanahuja outlines the four core elements of a development cooperation agenda toward MICs, namely i) institutional strengthening for social cohesion; ii) financial stability and counter-cyclical policies; iii) policies to improve access to international markets through higher competitiveness and secured access; and iv) cooperation and incentives to promote the engagement and participation of MICs in the provision of global public goods.[20] These could be taken as the very general guiding principles to adapt EU's development cooperation to countries that are now proposed for immediate graduation.

Although regional and thematic programmes are foreseen in the DCI proposal, their contribution will be rather limited given their low relative allocations and the geographical extension they are to cover. Funding for programmes like EUROsocial[21] (€40 million for the period 2010-2013) supporting social cohesion in Latin America are underfunded considering the importance and extent of the problem they tackle.

During the proposed Strategic Adaption Period, previous geographical funds could be earmarked to strengthen specific thematic support, thus addressing issues at the core of social cohesion such as fiscal reform, social expenditure criteria and attention to specific excluded sectors. Additionally, regional geographic programmes, in particular, arguably focus in excess on support for regional integration process with little regard to the asymmetries present within some of these regions.

5. RECOMMENDATIONS

5.1 Setting up Objective Criteria for Differentiation

All in all, the proposed formula is poorly articulated if it purports to provide criteria that aspire to become a standard and objective benchmark to define EU's aid allocations. The current approach based mainly on per capita income should be replaced by one geared instead at targeting poverty pockets in highly heterogeneous countries. The Alkire-Santos (2010) Multidimensional Poverty Index (MPI) offers a more horizontal assessment of poverty localisation beyond national per capita income. This conceptualisation allows for better addressing the issue of insufficient aid by changing the approach from 'aid orphan countries' to 'orphan poverty pockets'. Such index offers a more holistic take on political decisions of aid allocations.

[19] Morazán et al (2012).

[20] Sanahuja, J.A. Presentation of the study by Morazán et al (2012) at Eurolat in Strasbourg on 19 April 2012.

[21] See http://www.programaeurosocial.eu/eurosocial-II/tiki-index.php for more information.

A caveat of using the MPI, however, is the fact that it is extremely complex to capture different deprivations linked to poverty in one single index, despite its multidimensional nature. Indeed, there is still no consensus on which dimensions might be included and how they might be weighted (Ravallion, 2011).

In sum, the present briefing does not directly suggest the use of the MPI. It rather argues that the MPI is a more objective criterion as it is based on the presence of poverty pockets instead of national per capita income when it comes to comparing composite indices. Conceptually, the MPI offers a more multidimensional description of the poverty context at local level, by including poverty dimensions beyond income. However, this index, as it is counter argued by Ravallion (2011), has two important caveats that deserve close attention. First, the aggregation of a bunch of indicators into a single index disregards the inter relations that do exist among the several interdependent poverty dimensions. Second, the choice of weight for such an index is highly arbitrary, and thus inherently problematic as it can detract the reality. An additional methodological caveat is the need to take the data from different non-standard household surveys, which has substantial implications on the quality of the data and the wide range of methodological approaches used.

Against the premises discussed, and regarding specific country differentiation for the proposed future DCI, this study recommends that instead of 'graduating' Upper Middle Income Countries (UMICs) from it, previous country allocations from the current DCI remain and are earmarked for inequality-reducing interventions with those partners who wish to collaborate on these grounds. This briefing argues that there are good reasons to continue to cooperate on poverty reduction if this is done by addressing inequality, particularly with those MICs with highly unequal income distributions by international standards. One arbitrary threshold could be established at those with Gini coefficient above 45%.

If, however, a set of criteria for differentiation is required, the recommendation is to not base it solely on per capita GDP. Instead, and given the much argued importance of inequality, other measures like the Gini coefficient, the different FGT indices (poverty rate, gap and severity), a multidimensional poverty measure like the MPI and the HDI be considered. An example is proposed in the following box, providing a possible –although highly arbitrary- categorization of countries that should or should not be in the next DCI.

Box 1: Potentialities and Limitations of Differentiation Criteria: an Illustrative Example

Table 3 and Table 4 in the Annex respectively list the MICs that are to remain in the proposed DCI and those who are to graduate from it. Several indicators are displayed for each of these countries. As can be seen, the Multidimensional Poverty Index does not have much sensitivity as most graduated MICs fall very close to each other, with some exceptions. Since the country's share of word GDP does not account for population, inequality or poverty, this indicator is not deemed to be a good quantitative criterion. Since high inequality and the presence of poverty pockets is proposed as the main criteria for differentiation, the DCI could maintain allocations for those countries with, say, **Human Development Index below 0.750, Gini coefficient above 45%, poverty rate above 10% and poverty gap above 4%** (using the US$ 2 poverty line because this has higher sensitivity for MICs). **This necessarily arbitrary selection would lead to the future DCI continuing cooperation with the following MICs currently excluded from the proposal, in addition to those already included: Brazil, China, Colombia, Ecuador, Peru, India and Indonesia**. Under these criteria, **DCI cooperation with Argentina, Chile, Costa Rica, Kazakhstan, Malaysia, Mexico, Panama, Thailand and Uruguay would be discontinued.** Three countries, Iran, Maldives and Venezuela do not present sufficient data to be categorized following these criteria. Using Table 3 and 4, different differentiation results can be obtained by modifying the indices' thresholds proposed above.

As regards qualitative criteria for differentiation, it must be noted that internationally comparable poverty indices are based on very low poverty lines indeed (PPP US$ 1.25 and 2.0 for the extreme and moderate poverty lines, respectively). This means that for middle income countries the indices become very little sensitive and are rendered of limited use for differentiation. In many MICs the poor are not much above this international poverty line and therefore do not show in the statistics. This why it is suggested that the extent of inequality is used, in combination with poverty indices, to determine which countries could opt for DCI support on poverty reduction by targeting inequality. Also for this reason, the previous quantitative differentiation example for the DCI uses relatively low poverty rate (10%) and gap (4%) as threshold.

Having said this, if some MICs are to be graduated from the DCI, qualitative criteria should be used complementarily to the quantitative criteria set forth above. It is strongly suggested that qualitative rather than quantitative criteria are used to cut development aid to large MICs. Using the share of GDP to exclude countries does not account for the total population or the extent of poverty. In this case, it would be better to adopt qualitative criteria like respect for Human Rights, democracy, willingness to cooperate on addressing inequality issues, governance issues and the actual potential for leverage by the EU in a given country. Through these, the exclusion of China and other large players like Brazil, India and Indonesia, with large poor populations could be better argued if necessary.

One particularly defining criterion, although ex-post, is the above-mentioned willingness by the partner country to engage EU's development cooperation in tackling income inequality. Many MICs, particularly in Latin America, present Gini coefficients above 45%, whereas the EU has an average 30.5% and ranges between 24 and 37%. A key feature of these is the urgent need for i) tax reforms that address their regressive and ineffective tax systems and ii) a better pro-poor focus of social expenditures – of which conditional cash transfer can play, as they are doing, a major role.

Beyond this, a good possibility would be the complementary combination of quantitative criteria with other qualitative criteria –poverty pockets, spillover effects, knowledge transfers, cooperation to GPGs, PCD- that offer thorough country-specific benchmarks concerning needs, context, capacities and performance/impact on a case-by-case basis.

However, the measuring of qualitative criteria in highly complex policy constructs such as PCD or GPGs entails a more comprehensive and systematic approach. In such cases, the development of a portfolio of indicators is more suitable than the composite of indicators into a single aggregate index. Initially, composite indicators may present some advantages to a portfolio of individual indicators. Composite can be more easily understood compared to a portfolio that can result in information overload. But the disadvantages are structural in this case. Composite indicators' standardization and aggregation processes can hide information and can serve to dumb down the contribution of the individual indicator to the policy-making. Furthermore, these processes carry out high risks of asymmetries in the over simplified task of subjective value weighting (King and Matthews, 2012).

Instead, the use of a balanced portfolio of indicators can allow policy-makers to define allocation criteria based on a detailed understanding of the indicators and their relative importance and interplay (with higher sensitivity to heterogeneous cross-country contexts). The objective of this approach is to develop a comprehensive information system that deeply captures and shows the complex nature of poverty and its incidence for development policy. To this endeavour, which is still in a largely experimental stage, there are some processes worth taking into account. Building upon the first EC's Policy Coherence for Development Report in 2007, Dutch (Haver Droeze, 2008) and Irish (King and

Matthews, 2012) PCD frameworks offer a wide overview of using the portfolio of indicators' approach. In the same line, but in a different topic, the EC's Results-Oriented Monitoring System, set up in 1999, is an evaluation tool that sets five qualitative criteria (quality of design, effectiveness, efficiency, impact and sustainability) and a sample of indicators under each criterion that are aimed at providing an in-depth assessment of EC's development programs and projects.

All in all, it is recommended herein the definition of a set of 'multiple indices' –portfolio of indicators approach- instead of a 'single multidimensional index' –a single composite index. A set of indicators could be identified for measuring the qualitative benchmarks in a per country basis[22]. This would provide a comprehensive and coherent approach against which base aid allocation decisions could be adopted. The EP could potentially endorse this approach, thus contributing to address the current contradiction: the EU aims at setting differentiation criteria to benefit those countries who need it the most but in effect the proposed criteria will not (necessarily) be targeting the people most in need.

5.2 Defining a Research Roadmap

The prospected impacts of cutting EU bilateral aid to 'graduated' countries can only be assessed, at the moment, at the theoretical level based on assumed cause-effect relations. They are purposeful in drawing the first potential impacts scenarios. However, their consistent valuation would entail the compilation of empirical-based evidence on the potential effects/impact that cutting EU bilateral aid in some MICs might imply. This notwithstanding, there is an inherent difficulty in assessing potential impacts given that there are different alternatives to halting aid to MICs. In this regard, the latter would not carry the same implications if EU development aid to MICs were to be maintained and managed as usual or be adapted to the particular needs of MICs as discussed earlier in the briefing.

In particular, the EP could request the Commission to (i) adopt new criteria for differentiation based on some of the aforementioned requirements or a combination of them; (ii) assess new forms of development cooperation for low and upper middle-income countries based on proposed assistance in section 4; and (iii) a tailored EU approach to address poverty and inequality in a differentiated manner vis-à-vis graduated countries.

5.3 Globalising Policy Coherence for Development

The EU, arguably the main global advocate of policy coherence for development, has put this issue at the top of its Development Agenda. Nonetheless, the debate has centred on how to effectively improve the coherence of developed countries' policies, with an implicit donor-bias. Against the new aid paradigm, which hinges upon the implementation of strategic global development partnerships among developed and developing countries, the principles of PCD should also flow to LICs and MICs. The EP could play an active role, along with the EC, in ensuring the mainstreaming of PCD as part of its support strategy within the frame of the proposed forms of cooperation with MICs mentioned in section 4.2.

[22] It therefore allows assessing the poverty-problem analysis by country, thus limiting the impact of generalizations in a highly heterogeneous scenario. Furthermore, the qualitative nature of the criteria does not disregard the assignment of ex-post value weighting for the indicators of the portfolio. This fact can substantially contribute to compare the results at cross-country level and therefore to make decisions on aid allocations.

5.4 Towards a Strategic Adaptation Period

The development community widely acknowledges the prioritisation of aid allocations where they are most needed. However, the abrupt cut of EU bilateral aid through non-objective criteria in the forthcoming MFF may not be the most coherent response. There are two important trade-offs to take into account. The EU risks to loose a key focal point on poverty reduction in 19 'graduated' countries with overall large pockets of deprivation. The Commission proposes to address this potential 'gap' with funding allocated under the new Partnership Instrument (PI) –which is not poverty-focused- and via thematic DCI budget lines. As it appears, the Commission does not plan to apply the same criteria to other MICs in Africa or the Middle East, thus reflecting inconsistencies in its allocation policy. The trade-off may no be all that good in swapping geographic for thematic aid allocations to MICs in view of the potential outcomes, namely a diminished development focus and a weaker EU presence in the proposed scenario.

Furthermore, the new demanding global dynamics require an adaptive strategy for matching EU's development policy to the new global development landscape and geography. The proposed SAP seeks to address the need for framework focusing on new forms of development cooperation and the core elements of MICs development agenda aimed at addressing their main challenges of inequality and social cohesion (section 4.2).

To this purpose, the EP could request the revision of the differentiation criteria to accommodate some of the concerns expressed here or, at least, considering the setting of a strategic adaptation period within the next Multiannual Financial Framework whose discussion is underway. It would represent a good opportunity for addressing actual inconsistencies and for drawing a coherent EU development policy that really responds to global trends while fosters the EU's comparative advantage as a prominent global player.

6. REFERENCES

Alkire, S. and Santos, M.E. (2010). "Acute Multidimensional Poverty: A New Index for Developing Countries". Oxford Poverty and Human Development Initiative. Working Paper 38.

Burnside, C. and Dollar, D. (2000). "Aid, Policies, and Growth". American Economic Review. American Economic Association. Vol. 90(4) pages 847-868.

Carbonnier, G. and Sumner, A. (2012). "Reframing Aid in a World Where the Poor Live in Emerging Economies". Revue internationale de politique de développement [En ligne], 3/2012, mis en ligne le 16 avril 2012, consulté le 16 avril 2012. URL : http://poldev.revues.org/977 ; DOI : 10.4000/poldev.977.

Claessens, S., Cassimon, D., and van Camenhout, B. (2007). "Empirical Evidence on the New International Aid Architecture". World Economy & Finance Research Programme.

Collier, P. and Dollar, D. (1999). "Aid Allocation and Poverty Reduction". World Bank Policy Research Working Paper No. 2041.

Collier, P. and Dollar, D. (2001). "Can the World Cut Poverty in Half? How Policy Reform and Effective Aid Can Meet International Development Goals". World Development. Vol. 29(11) pp. 1787-1802.

Easterly, W. (2006). "Social Cohesion, Institutions, and Growth". Center for Global Development. Working Paper no. 94.

Gavas, M. (2012). "The European Commission's Legislative Proposals for Financing European Union Development Cooperation". Overseas Development Institute. Background Note.

Gavas, M., Geddes, M., Massa, I., and Te Velde, D. (2011). "European Union Blending Facilities: Implications for Future Governance Options". Overseas Development Institute. Research Reports and Studies.

Glennie, J. (2011). "The Role of Aid to Middle-Income Countries: A Contribution to Evolving EU Development Policy". Working paper no. 33 (London: ODI).

Haver Droeze, F. (2008). "Policy Coherence for Development: the World Beyond Aid". Dutch Ministry of Foreign Affairs. Policy Coherence Unit.

Hoeffler, A. and Outram, V. (2008). "Need, Merit, or Self Interest – What Determines the Allocation of Aid". Centre for the Study of African Economies. WBP 2008-19.

ILO (2011). "Social Protection Floor: For an Inclusive Globalization". Report of the Advisory Group Chaired by Michelle Bachelet convened by the International Labour Organisation with the collaboration of the World Health Organisation. Geneva.

Jha, P. and Negre, M. (2007). "Indian Economy in the Era of Contemporary Globalisation: Some Core Elements of the Balance Sheet". Macroscan. In: www.macroscan.net - 16 April 2012.

Kanbur, R. and Sumner, A. (2011). "Poor Countries or Poor People? Development Assistance and the New Geography of Global Poverty". Charles H. Dyson School of Applied Economics and Management. Working paper (Ithaca: Cornell University).

King, M. and Matthews, A. (2012). "Policy Coherence for Development: Indicators for Ireland". Institute for International Integration Studies. Trinity College Dublin.

López-Calva, L.F. and Lustig, N. (2010). "Declining Inequality in Latin America: A Decade of Progress?". Brookings Institution and United Nations Development Programme.

Melamed, C. (2010). "Economic Growth and the MDGs". Overseas Development Institute. Briefing Paper No. 60.

Morazán, P., Sanahuja, J.A Ayllón, B. and FIIAPP (2012). "A New European Union Development Cooperation Policy with Latin America". Development Committee. European Parliament. Study. January.

Ravallion, M. (2010). "Do Poorer Countries Have Less Capacity for Redistribution?". Journal of Globalization and Development. 1(2), doi: 10.2202/1948-1837.1105.

Ravallion, M. (2011). "On Multidimensional Indices of Poverty". World Bank Group. Policy Research Working Paper No. 5580.

Santiso, C. (2001). "Good Governance and Aid Effectiveness: the World Bank and Conditionality". The Georgetown Public Policy Review. Vol. 7, No. 1. Pp. 1-22.

Soares, S., Guerreiro Osorio, R., Veras Soares, F., Medeiros, M. and Zepeda, E. (2009). "Conditional Cash Transfers in Brazil, Chile and Mexico: Impacts upon Inequality", Estudios Economicos, no. extra 1, pp. 207–24.

Sumner, A. (2011). "The New Bottom Billion: What if Most of the World's Poor Live in Middle-Income Countries?". Center for Global Development. Policy Brief (Washington, DC: CGD).

UN (2009). "Development Cooperation with Middle-Income Countries: Report of the Secretary-General". United Nations: New York.

Utz, R. (2010). "Will Countries with Insufficient Aid Please Stand Up?". Concessional Finance and Global Partnerships Vice Presidency (CFP). Working paper series No. 7.

World Bank (2012). Global Economic Prospects: Uncertainties and Vulnerabilities. January.

ANNEX

Table 1: Income categories in 2011

Least Developed countries	Other Low Income Countries (LICs) (GNI per capita ≤ USD 1005 in 2010)	Low Middle Income Countries (LMICs) (GNI per capita USD 1006 - 3975 in 2010)	Upper Middle Income Countries (LMICs) (GNI per capita USD 3976 - 12275 in 2010)

Source: World Bank

Table 2: Income per capita/status and poverty gap in 'graduated' MICs

'Graduated' country	Income-Status	Per capita GNI, 2010 (USD)	Poverty Gap Index*
Argentina	UMIC	8620	0.7 (2010)
Brazil	UMIC	9390	3.6 (2009)
Chile	UMIC	10120	0.7 (2009)
China	UMIC	4270	3.2 (2008)
Colombia	UMIC	5510	3.8 (2010)
Costa Rica	UMIC	6810	1.8 (2009)
Ecuador	UMIC	3850	2.1 (2010)
Iran	UMIC	4520 (2009)	-
Kazakhstan	UMIC	7580	0.0 (2009)
Malaysia	UMIC	7760	0.0 (2009)
Maldives	UMIC	5750	-
Mexico	UMIC	8930	0.3 (2008)
Panama	UMIC	6970	2.1 (2010)
Peru	UMIC	4700	1.3 (2010)
Thailand	UMIC	4150	28.1 (2007)
Uruguay	UMIC	10230	0.1 (2010)
Venezuela	UMIC	11590	-
India	LMIC	1270	7.5 (2010)
Indonesia	LMIC	2500	3.3 (2010)

Note: South Africa and Cuba, although qualifying countries, will be maintained in DCI.
*Poverty gap at $1.25 a day (PPP) (%)
Source: World Bank

Table 3: Quantitative indicators** related to the measure of poverty in "graduated" countries under EC's DCI proposal										
	HDI	**GDP x cap. PPP $**	**MPI** (year)	**Gini* (%)**	**Poverty Rate* (%)**		**Poverty Gap* (%)**		**Pov. Sev. - $1.25**	**Share of world's GDP (2010)**
					$2	**$1.25**	**$2**	**$1.25**		
Argentina	0.797	14,538	0.011 (05)	45.8	1.9	0.9	0.9	0.7	0.58u	0.58
Brazil	0.718	10,367	0.011 (06)	53.9	10.8	6.1	5.4	3.6	2.88	3.30
Chile	0.805	14,311	-	52.1	2.7	1.4	1.2	0.7	0.49	0.34
China	0.687	6,828	0.056 (03)	41.5	29.8	13.1	10.1	3.2	1.44	9.37
Colombia	0.710	8,959	0.022 (10)	58.5	15.8	8.2	6.8	3.8	2.62	0.46
Costa Rica	0.744	11,106	-	50.3	6.0	3.1	2.7	1.8	1.45	0.06
Ecuador	0.720	8,268	0.009 (03)	49.0	10.6	4.6	4.1	2.1	1.45	0.09
Iran	0.707	11,558	-	38.3	-	-	-	-	0.16	0.52
Kazakhstan	0.745	11,510	0.002 (06)	30.9	1.1	0.1	0.2	0.0	0.02	0.24
Malaysia	0.761	14,012	-	46.2	2.3	0.0	0.2	0.0	-	0.38
Maldives	0.661	5,476	0.018 (09)	37.4	-	-	-	-	0.02	0.00
Mexico	0.770	14,258	0.015 (06)	51.7	5.2	1.2	1.3	0.3	1.42	1.64
Panama	0.768	13,057	-	52.3	13.8	6.6	5.1	2.1	0.96	0.04
Peru	0.725	8,629	0.086 (04)	48.0	12.7	4.9	4.1	1.3	0.54	0.25
Thailand	0.682	7,995	-	53.6	4.6	0.4	0.8	0.1	0.01	0.50
Uruguay	0.783	13,189	0.006 (03)	42.4	1.2	0.2	0.3	0.1	0.04	0.06
Venezuela	0.735	12,323	-	43.5	-	-	-	-	3.04	0.62
India	0.547	3,296	0.283 (05)	36.8	68.7	32.7	24.5	7.5	3.69	2.73
Indonesia	0.617	4,199	0.095 (07)	36.8	46.1	18.1	14.3	3.3	1.46	1.12
Germany	0.905	36,338	-	28.3	-	-	-	-	-	5.19
Hungary	0.816	20,312	0.016 (03)	31.2	0.4	0.17	0.2	0.16	0.32	0.20

Source: Human Development Index (HDI), Gross Domestic Product (GDP) per Capita, Multidimensional Poverty Index (MPI) and Income Gini Coefficient are taken from the UNDP Human Development Report 2011. Poverty Rate (headcount ratio), Poverty Gap (%) at $2 and $1.25 a day (PPP), Poverty Severity (Squared Poverty Gap) and Share of World's GDP indices are taken from World Bank Indicators (PovcalNet).

*Numbers show data recently available.

**The objective of tables 3 and 4 is to offer a comparative overview of the main quantitative indices at hand among the "graduated" 19 countries and the remaining MICs under the EC's DCI proposal. A characteristic disadvantage of quantitative indices is their low sensitivity to reflect the high heterogeneity among developing countries and the complexity (multidimensionality) of poverty as phenomenon. Especially if very low poverty lines are used, as this reduces the ability of poverty indices to help discern the different realities of middle income countries by consistently showing very low rates.

u: Only calculated for Argentina urban.

Table 4: Quantitative indicators related to the measure of poverty in remaining MICs under EC's DCI proposal (14 LMICs + 2 UMICs)

	HDI	GDP x cap. PPP $	MPI (year)	Gini* (%)	Poverty Rate* (%)		Poverty Gap* (%)		Pov. Sev. - $1.25	Share of world's GDP (2010)
					$2	$1.25	$2	$1.25		
Bolivia	0.663	4,419	0.089 (08)	57.3	24.9	15.61	13.1	8.64	6.30	0.03
Cuba (UMIC)	0.776	-	-	-	-	-	-	-	-	0.10
El Salvador	0.674	6,629	-	46.9	16.9	8.97	7.6	4.44	3.02	0.03
Guatemala	0.574	4,720	0.127 (03)	53.7	-	13.53	-	4.72	2.39	0.07
Honduras	0.625	3,842	0.159 (06)	57.7	29.8	17.92	14.9	9.35	6.86	0.02
Iraq	0.573	3,548	0.059 (06)	-	21.4	2.82	4.4	0.42	0.12	0.13
Mongolia	0.653	3,522	0.065 (05)	36.5	-	-	-	-	-	0.01
Nicaragua	0.589	2,641	0.128 (06)	52.3	-	11.91	-	2.36	0.67	0.01
Pakistan	0.504	2,609	0.264 (07)	32.7	60.2	21.04	17.9	3.49	0.87	0.28
Paraguay	0.665	4,523	0.064 (03)	52.0	13.2	7.16	5.7	3.02	1.92	0.03
Philippines	0.644	3,542	0.064 (08)	44.0	41.5	18.42	13.8	3.72	1.00	0.32
S. Afri. (UMIC)	0.619	10,278	0.057 (08)	57.8	31.3	13.77	10.2	2.30	0.50	0.58
Sri Lanka	0.691	4,772	0.021 (03)	40.3	29.1	7.04	7.4	0.98	0.22	0.08
Turkmenis.	0.686	7,242	-	-	-	24.82	-	6.97	2.71	0.03
Uzbekistan	0.641	2,875	0.008 (06)	36.7	-	-	-	-	-	0.06
Vietnam	0.593	2,953	0.084 (02)	37.6	43.4	16.85	13.5	3.75	1.24	0.17

Source: Human Development Index (HDI), Gross Domestic Product (GDP) per Capita, Multidimensional Poverty Index (MPI) and Income Gini Coefficient are taken from the UNDP Human Development Report 2011. Poverty Rate (headcount ratio), Poverty Gap (%) at $2 and $1.25 a day (PPP), Poverty Severity (Squared Poverty Gap) and Share of World's GDP indices are taken from World Bank Indicators (PovcalNet).

*Numbers show data recently available.

Table 5: Percentage of people below USD1.25 poverty line		
	1988-90 or nearest year	**2007-08 or nearest year**
Low income, stable (e.g. Tanzania, Zambia)	80%	**16%**
Low income, fragile conflict-affected (e.g DRC, Burundi)	13%	12%
Middle income, stable (e.g India, Indonesia)	6%	**61%**
Middle income, fragile conflict-affected (Pakistan, Nigeria)	1%	11%

Source: Sumner (2010) in Glennie (2011)

Table 6: Global distribution of world's poor (%) by various measures, 2007-08					
	USD1.25	**Children out of primary school**	**Children below height**	**Children below weight**	**MPI**
Middle-income (MIC)	72	56	71	71	70
Low-income (LIC)	28	39	28	28	29
Fragile and conflict-affected states (43)	23	61	31	30	29
Sub-Saharan Africa	27	54	27	24	28
Least Developed Countries (50)	25	40	27	27	27
China and India	50	-	43	48	-

Source: Adapted from Sumner (2010) in Kanbur and Sumner (2010)

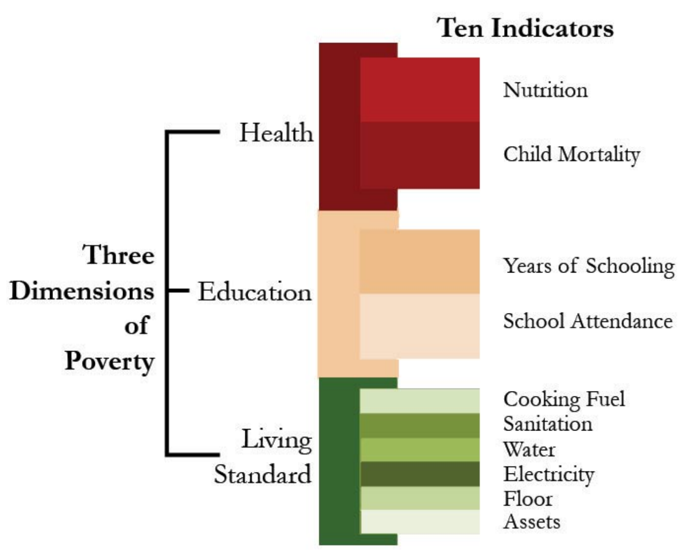
Table 7: Income status transitions from 1980-2003

Between 1980-2003, 38 countries fell back from MIC to LIC status, with only 10 managing to return to MIC status in subsequent years

Change in income status	Number of countries	Examples
Fell back to LIC, and did not managed to return to MIC	21	Angola, Azerbaijan, Ghana, Kenya, Yemen, Nicaragua, Tajikistan, Nigeria, Moldova
Fell back to LIC, but bounced back to MIC	9	China, Egypt, Guyana, Maldives, Turkmenistan, Armenia
Fell back to LIC, bounced back to MIC, but fell back to LIC	6	Georgia, Indonesia, Lesotho, Togo, Senegal
Fell back to LIC, bounced back to MIC, fell back to LIC, but bounced back to MIC	1	Albania
Fell back to LIC, bounced back to MIC, fell back to LIC, bounced back to MIC, but fell back to LIC	1	Sudan

Source: World Bank

Figure 1: Alkire-Santos Multidimensional Poverty Index



Source: Oxford Poverty and Human Development Initiative (2010)

Table 8: EC proposals for external action instruments			
Instrument	**Proposed total budget 2014-20 (2011 prices)**	**Proposed total budget 2014-20 (current prices)**	**Coverage**
European Development Fund (off-budget)	€30.32 bn	€34.275 bn	Africa, Caribbean and Pacific
Heading 4 (Global Europe)			
Geographic			
Development Cooperation Instrument	€20.597 bn	€23.295 bn	Asia, Central Asia, Latin America and the Middle-East Two thematic programmes: (i) GPGs and challenges; (ii) CSOs and Local Authorities Pan-African Programme
European Neighbourhood Instrument	€16.097 bn	€18.182 bn	Neighbouring countries in the eastern and southern Mediterranean
Pre-accession Instrument	€12.52 bn	€14.11 bn	Southern Balkans, Turkey, Iceland
Partnership Instrument	€1 bn	€1.131 bn	Global reach but with a focus on strategic partners and emerging economies
EU-Greenland Partnership	€0.193 bn	€0.218 bn	Greenland
Thematic			
European Instrument for Democracy and Human Rights	€1.4 bn	€1.578 bn	Human rights protection and promotion, democratisation, elections monitoring
Instrument for Stability	€2.51 bn	€2.829 bn	Crisis response, crisis preparedness, conflict prevention, global and trans-regional security threats
Nuclear Safety	€0.56 bn	€0.631 bn	All third countries, but priority for pre-accession and neighbouring countries

Source: European Commission

EUROPEAN PARLIAMENT

BB-31-12-689-EN-N

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES

POLICY DEPARTMENT

Role

Policy departments are research units that provide specialised advice
to committees, inter-parliamentary delegations and other parliamentary bodies.

Policy Areas

Foreign Affairs

- Human Rights
- Security and Defence

Development

International Trade

Documents

Visit the European Parliament website: **http://www.europarl.europa.eu/studies**

ISBN 978-92-823-3741-7

ISBN 978-92-823-3741-7
doi: 10.2861/81545

Publications Office