Briefing note

Financing the end of extreme poverty

2019 update

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Key messages

- 430 million people will be living in extreme poverty by 2030, despite economic growth reducing poverty by a third. This is 30 million more people than last year's assessment, and means the world is significantly off track to achieve the first Sustainable Development Goal.
- Extreme poverty could be ended by investing in human development: education, health, nutrition and social protection.
- Most countries can afford this investment if they maximised their taxation and allocated 50% of public spending to human development. But 46 countries still cannot afford to end extreme poverty on their own, facing a funding gap of $222 billion per year.
- Nearly half the gap in these 46 countries could be filled by governments maximising taxation and better targeting spending. The other half could be filled by more and better-targeted aid.
- To close this gap, governments should increase taxation and allocate 50% of public spending to human development. Donors should fulfil their 0.7% ODA/gross national income commitment and allocate half their aid to the poorest countries. This could close the gap to meet SDG 1 and end extreme poverty by 2030.
- Global inequality does not have to increase. Some governments and donors are leading the way in prioritising human development in the poorest countries. But overall aid trends are going in the wrong direction. Leaders gathering in September 2019 for the UN High Level Meeting on Financing for Development and SDG Summit must act now to reverse the trend and end extreme poverty by 2030.

The financial challenge of ending extreme poverty

The latest United Nations (UN) report on progress towards the Sustainable Development Goals (SDGs) (UN, 2019), published at the High-level Political Forum in July 2019, was a stark reminder of the challenges the world faces in implementing the SDGs and tackling the current scale of inequalities, both within and between countries. Of the world's people, 1 in 12 are living in extreme poverty. One in nine go hungry. Half lack essential healthcare. Half are not covered by social protection. One in five children are not attending school.

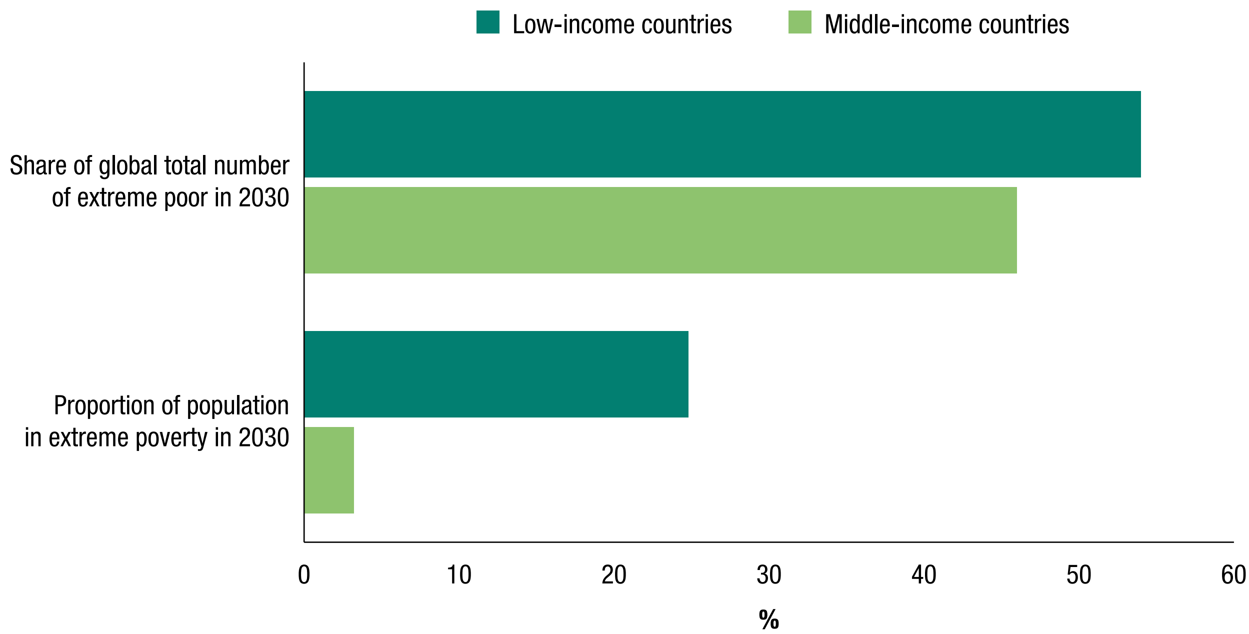
Progress towards the first SDG – ending extreme poverty everywhere by 2030 – is clearly off track. The projections in this note suggest that, while economic growth will cut poverty rates by one-third by 2030, 430 million people will still be trapped in extreme poverty. This is 30 million more than shown in the projections made in last year's full report on financing the end of extreme poverty (Manuel et al., 2018). UN projections suggest that the numbers could be even higher.

The updated projections in this note show that poverty will be concentrated in fragile states (86% of the total). Poverty will also be much more concentrated in low-incomes countries (LICs). While half of the extreme poor will still be in middle-income countries (MICs), they will account for a relatively small share of the population, leaving overall poverty rates as a proportion of the population much lower in MICs at 3% – eight times lower than the 25% projected for LICs (Figure 1).

As the analysis in last year's full report showed, additional investment in human development – in proven education, health, nutrition and social protection programmes – could end extreme poverty (and would also deliver on the education and health SDGs). This year's briefing note uses the same methodology but updates the financial estimates.

This note updates the cost estimates for all 138 LICs and MICs, including all 47 least developed countries (LDCs). It draws on research by the United Nations Educational, Scientific and Cultural Organization research for education costs and on World Health Organization and World Bank research for universal healthcare and

Figure 1 Poverty will be much more concentrated in low-income countries



Source: authors' estimates

nutrition interventions. We also update the cost estimates for a set of social protection programmes, designed at the scale needed to lift everyone out of extreme poverty in each country. This set comprises employment on public work programmes for those able to work, and universal grants for children, elderly and those with disabilities.

Finally, this note updates estimates of the potential for each of the 138 countries to increase their tax revenues in line with the maximum amount that International Monetary Fund (IMF) and World Bank research suggests is feasible, given the economic circumstances in each country. Significant political barriers would have to be overcome and care would need to be taken so as not to impede investment or create a regressive tax system. Nevertheless, these estimates suggest that LICs and MICs could increase their revenues by $1.7 trillion a year.

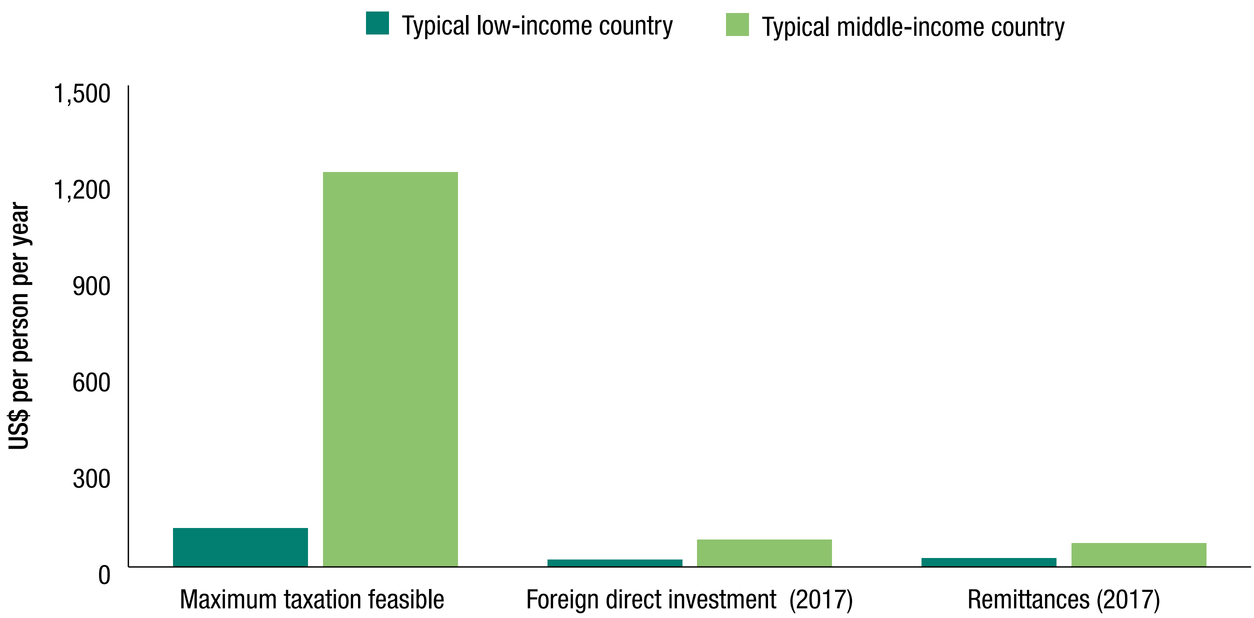
These additional revenues are not evenly distributed: 99% of the increase would be generated by MICs. On average the maximum revenue potential in MICs is $1,230 per person a year – more than 10 times the $120 average in LICs. This imbalance in taxation resources is even greater than for foreign direct investment and remittances, where MICs receive three times more per person (Figure 2).

Which countries can afford the investment needed for human development to end extreme poverty?

A combined analysis of the costs and the potential taxation revenues reveals that 91 of the 107 MICs could afford to make the needed investments in human development to end extreme poverty. There are 62 that are already spending at least the required amount (Figure 3). Most of these are upper middle-income countries, spending on average 47% of their budget on human development. Another 18 could afford the required amount if they increased the share allocated within their budgets from the current 28% to 50%, in line with the combined international spending targets for education, health and social protection (15%, 15% and 20% respectively). Finally, there are another 11 MICs (and one LIC) that could afford the needed investment if they increased their spending on human development to 50% and maximised their tax effort in line with what IMF and World Bank research suggests is feasible.

At present, however, 30 of the 31 LICs cannot afford the investments needed to end extreme poverty, even if they maximised their tax revenues and increased the share they allocated for such investments from an average of 32% to

Figure 2 Low-income countries have 10 times less revenue potential – and receive three times less foreign direct investment and remittances

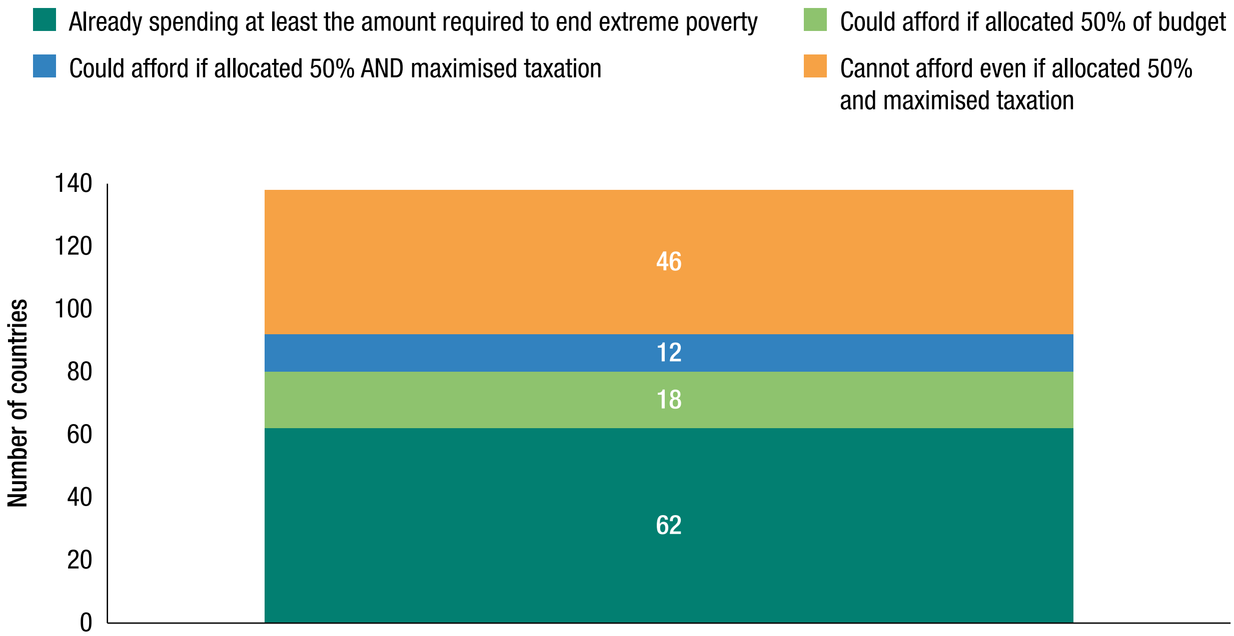


Source: authors' estimates and Development Initiatives

50%. There are also 16 MICs that cannot afford such investments.

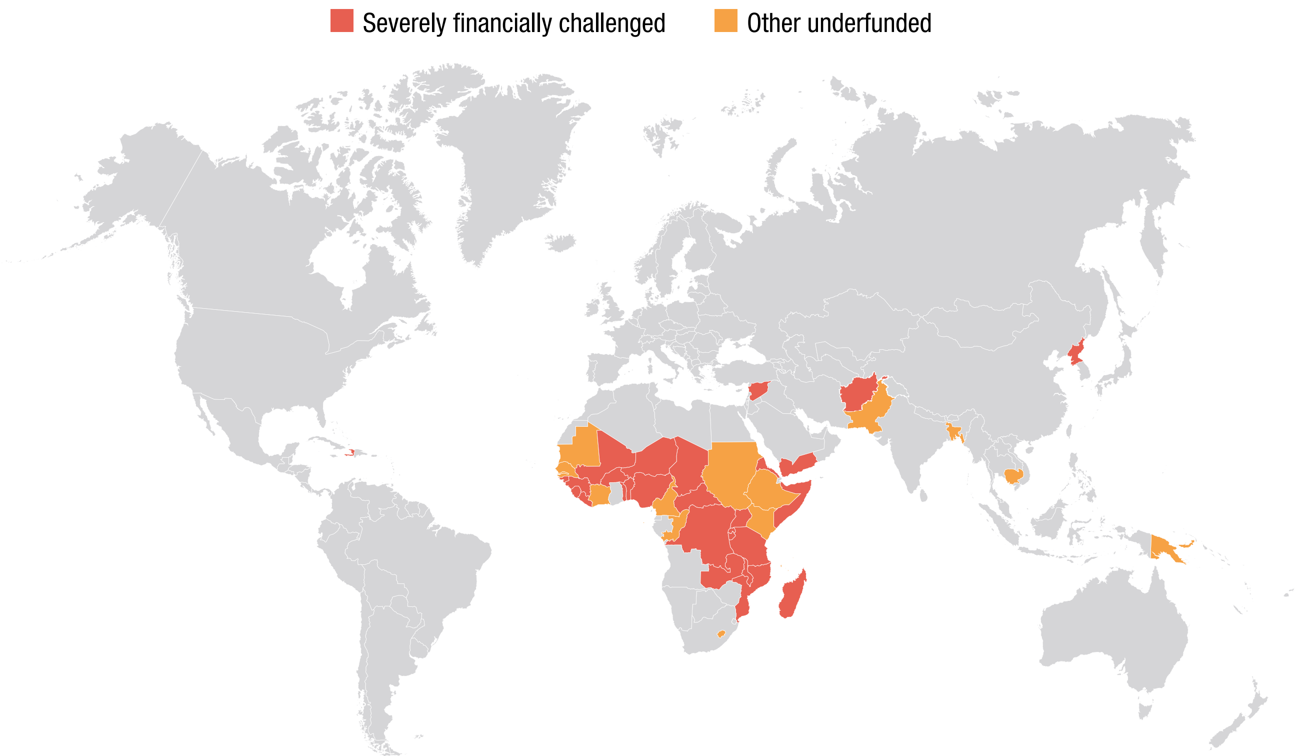
Taken together, these 46 countries face a total financing gap of $222 billion a year on the basis of current spending by governments and aid from donors (Figure 4). Most of the 46 are in sub-Saharan Africa and most are also LDCs and fragile states. They include 29 countries that

Figure 3 Most countries could afford investment in human development needed to end extreme poverty



Source: authors' estimates

Figure 4 Most countries that cannot afford to end extreme poverty are in sub-Saharan Africa



Source: authors' estimates

are severely financially challenged – they cannot afford even half of the spending that is needed. All but two of these are LICs. All 29 are expected to have high poverty rates in 2030, with the median rate standing at 31%.

How to meet the financial challenge

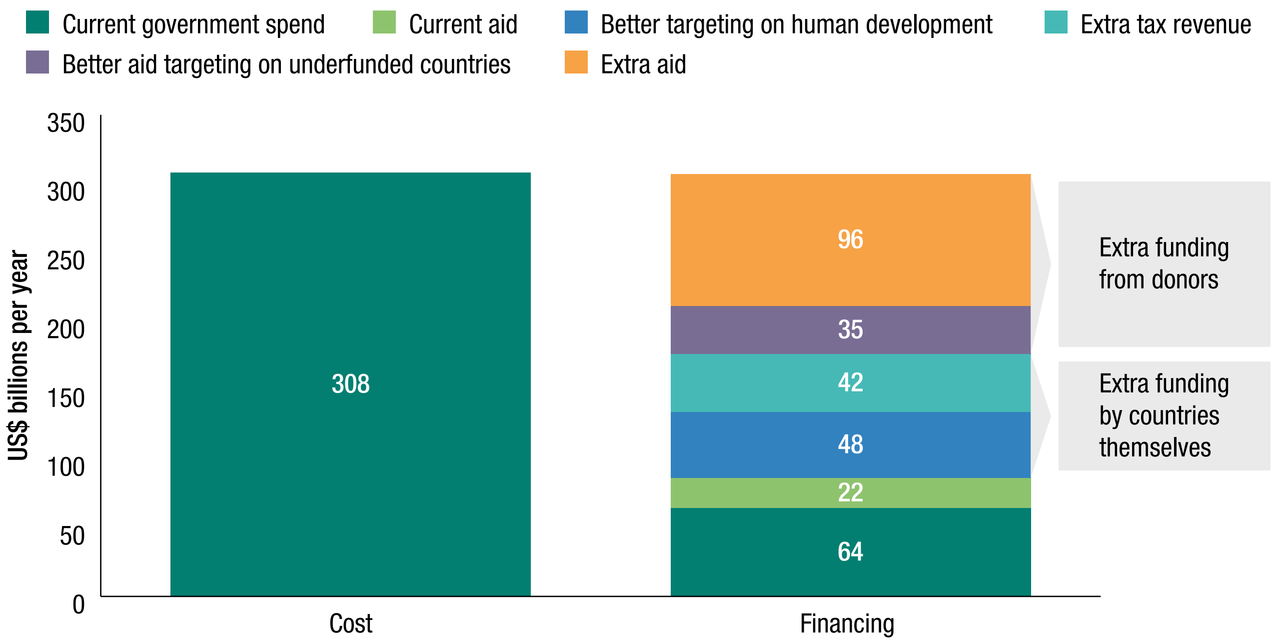
Nearly half (41%) of the $222 billion a year funding gap in the 46 countries could be filled by the countries themselves. They could, on average, increase their tax revenues by a quarter. And they could increase the share they allocate to human development from 28% to 50% (some have already been allocating over 40%, including Ethiopia and Tanzania). If they maximised their tax revenues and allocated half of their revenues to human development they could fill half the gap. But they would still need additional aid financing of $131 billion a year – six times the $22 billion a year of aid that is currently given for human development in these countries.

The other half of the funding gap, which needs to be aid financed, could be filled if all donors met the UN target for official development assistance (ODA) as a proportion of gross national income (GNI) of 0.7% and ensured that half of their aid went to the poorest countries. This would involve giving all the increase in aid to underfunded countries (with half allocated for human development and the rest available for infrastructure and other investments). It would also require donors to scale back by three-quarters over time their existing funding to countries that can already fully afford the costs and to channel all of the resulting resource to human development in the 46 underfunded countries.

Figure 5 sets out how the 46 underfunded countries could afford the investment needed to end extreme poverty. The precise mechanisms for providing the finance would need to be matched to the context. In some countries this might involve additional financial controls (as has been done in Afghanistan and Somalia) and new funding modalities (such as the Education Cannot Wait fund), as well as scaling up the provision of services by UN agencies and non-governmental organisations.

Even without any increase in global aid, all countries could afford at least half of the costs of the investment needed if current aid flows were better prioritised. Over half of the aid disbursed at country level is directed to countries that can fully afford the costs of ending extreme poverty. If over time donors scaled back aid to these countries by 39%, and re-allocated every dollar of this aid to human development in the 29 countries that are severely financially challenged, all of these countries could afford half the costs.

Figure 5 How 46 underfunded countries could afford the investment they need to end extreme poverty



Source: authors' estimates

Aid flows to the poorest countries

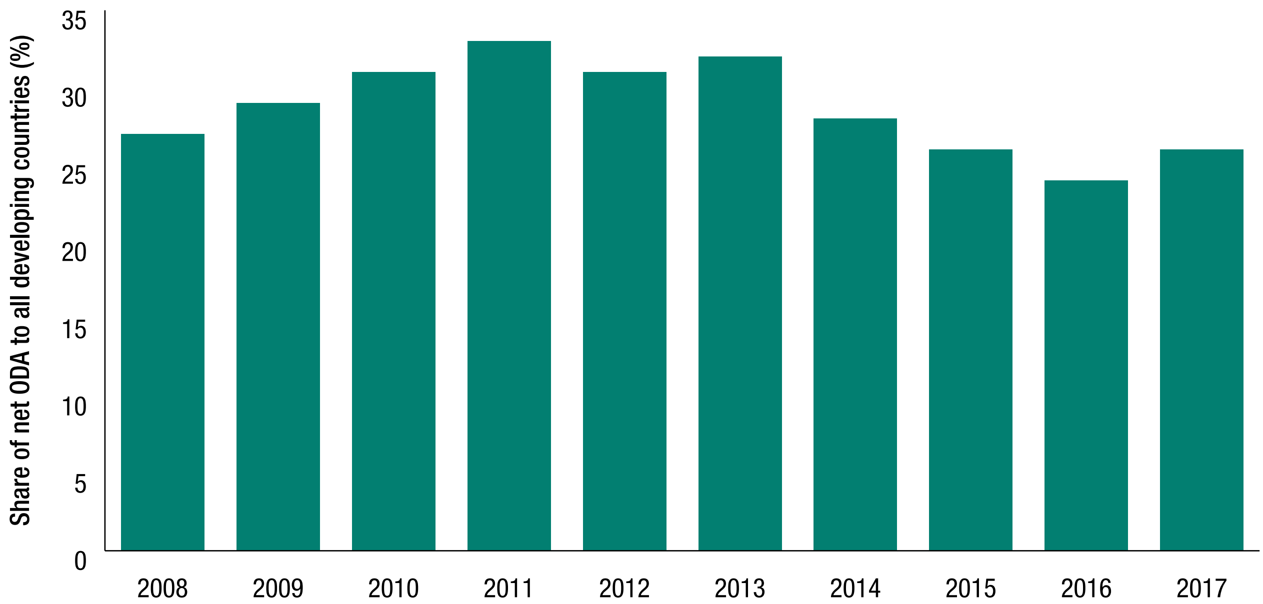
Over the past year, many commentators have noted the need for more and better prioritised aid for the poorest countries, including the Managing Director of the IMF, the previous chair of the Organisation for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC), Professor Jeffrey Sachs, Masood Ahmed from the Center for Global Development and Homi Kharas from the Brookings Institution (Lagarde and Gaspar, 2018; ODI, 2018; Move Humanity, 2018; Ahmed, 2019; Kharas and McArthur, 2019). In the latest UN SDG report, the UN Secretary-General called for 'a much deeper, faster and more ambitious response' to achieve the goals, noting that financing is the first of several areas that are crucial to drive progress (UN, 2019).

As the OECD DAC noted this year, however, recent trends in aid are going the wrong way: 'Development aid drops in 2018, especially to neediest countries' (OECD, 2019). OECD DAC figures show that on average:

- DAC donors give less than half the ODA/GNI target of 0.7%. This average masks a wide range of effort among the major DAC donors (those that have provided more than $450 million in ODA over the past three years). While four major DAC donors meet or exceed the ODA/GNI target of 0.7%, three major donors achieve just a quarter of that target.[1]
- DAC donors target the poorest countries poorly. Despite the international target of increasing aid to LDCs (SDG 17.2.1), their share of aid from DAC donors actually fell from one third in 2011 to just over a quarter in 2017 (Figure 6).

Aid is also poorly targeted relative to countries' own abilities to reduce extreme poverty. At present, there is no reduction in the amount of aid a country receives as the potential of its own taxation revenue per person in extreme poverty grows. Indeed, if anything, the more tax a country has that could be used to reduce its own extreme poverty, the more aid it receives (Figure 7). Donors might want to provide more aid to countries that raise more

Figure 6 Proportion of aid from the Development Assistance Committee to least developed countries



Source: OECD DAC

1 The major DAC donors that meet or exceed the target are Sweden, Norway, Denmark and UK (most generous listed first). The major DAC donors that achieve a quarter are South Korea (21%), US (24%) and Spain (29%) (OECD, 2019).

tax – as an incentive. But there is no rationale to provide more aid to countries whose fundamental economic characteristics mean that they have greater potential to raise tax. And while the ending of extreme poverty is not the only purpose of aid, the poverty rate is a useful indicator of overall need.

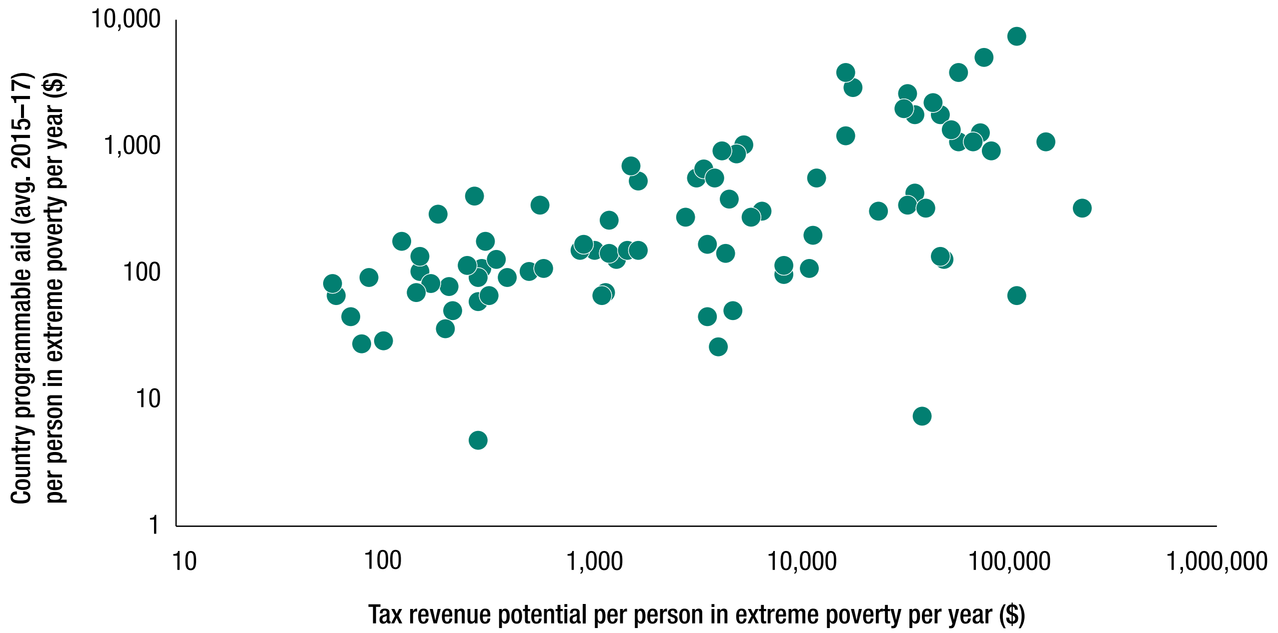
Last year's report introduced a donor efficiency index to measure just how efficient donors are in their efforts to target extreme poverty. This index measures not only the proportion of aid given to the poorest countries but also how well that aid matches the individual needs of the poorest countries, given that some LDCs have much greater ability than others to contribute their own resources. The index also focuses on the countries facing the greatest financial challenge: the 29 countries that cannot afford even half the costs.

The index is more demanding than previous measures, where high scores can be achieved simply by funding a few of the richer LDCs. This year's updated index reveals that the three best donors continue to be eight times better than the worst three at targeting their aid to those countries that are least able to finance ending extreme poverty (Figure 8).

There is also a wide variation in efficiency among the major multilateral agencies that support the poorest countries, with the best three agencies three times better than the worst three at targeting their support to the countries that need it the most (Figure 9). The IMF concessional trust fund achieves the highest score. The EU's European Development Fund (EDF) also scores highly while its other main financing instrument, the Development Cooperation Instrument (DCI), is close to DAC average. Others with high scores include the United Nations Development Programme (UNDP), the African Development Bank concessional fund (AfDF), the Global Health Fund and the United Nations Children's Fund (UNICEF).

Other multilaterals achieve scores that are much closer to the average for DAC bilateral donors: the Global Alliance for Vaccines and Immunizations (GAVI), the International Fund for Agricultural Development (IFAD), the International Development Association (IDA) (the World Bank's concessional fund), the World Health Organization (WHO), the Islamic Development Bank (IsDB), the Organization of the Petroleum Exporting Countries (OPEC) Fund

Figure 7 As tax potential rises, aid increases

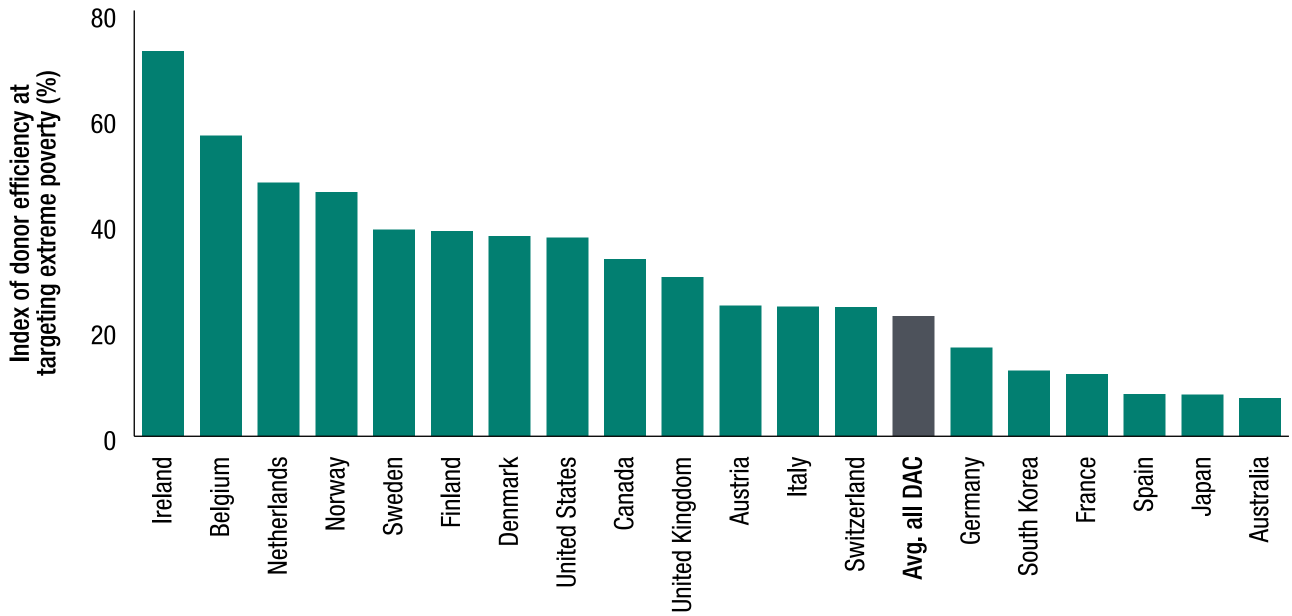


Note: figure includes all LIC and MICs that receive aid and have populations of more than one million and poverty rates of more than 1%
Source: authors' estimates

for International Development and the Global Environment Facility (GEF).

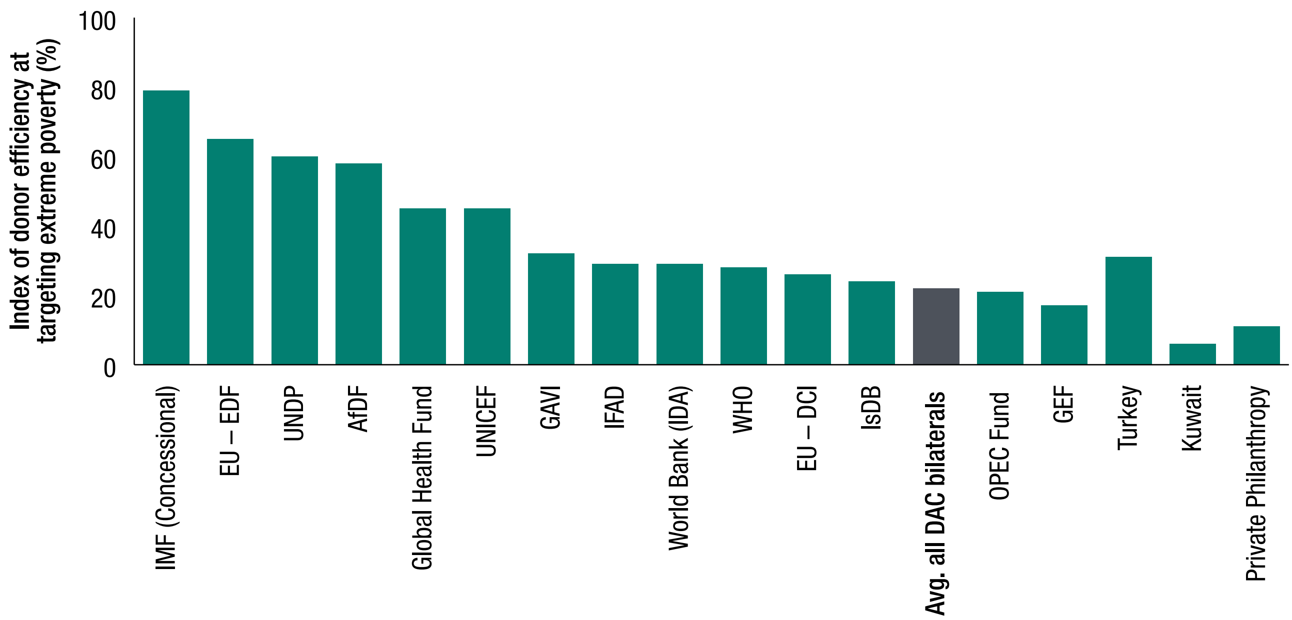
Only two non-DAC donors, Turkey and Kuwait, reported their aid in 2017 to the DAC, with Turkey achieving the higher score. The private philanthropic organisations that reported to DAC in 2017 provided $6 billion a year of aid, close to the total provided by all the regional development banks together, but their aggregate efficiency score is below the DAC average. Some small organisations do score highly, however, including Comic Relief (which achieves an efficiency score that is nearly twice that of the UK).

Figure 8 The best major bilateral DAC donors are eight times better at targeting extreme poverty than the worst



Source: authors' estimates

Figure 9 There is wide range in the efficiency of multilateral agencies and other donors

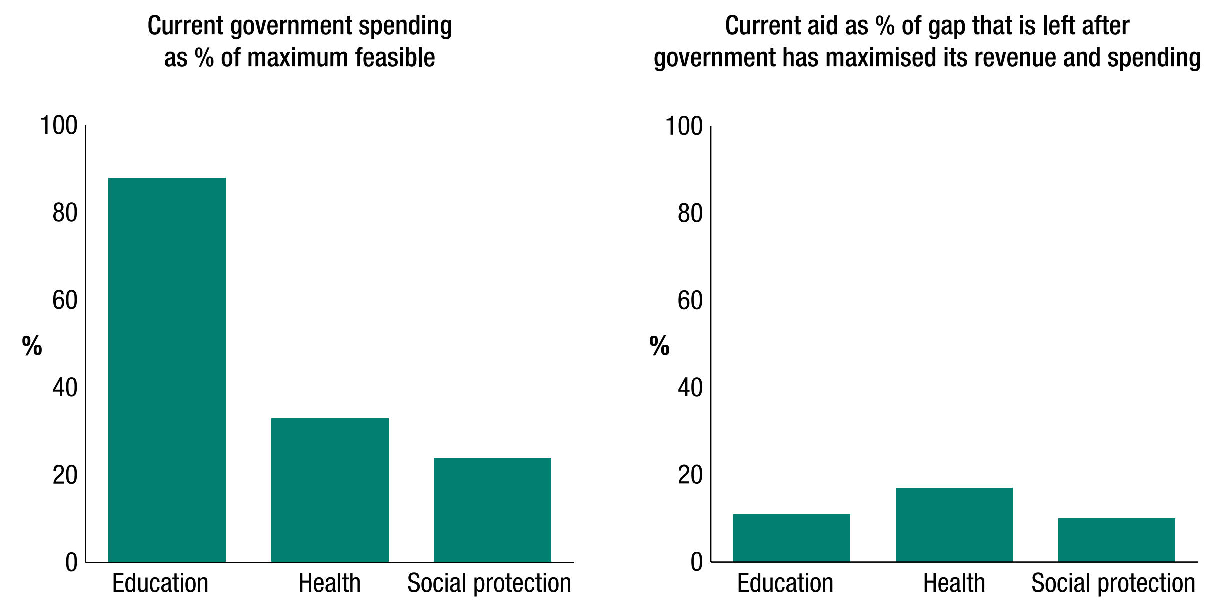


Source: authors' estimates

Box 1 Social protection – the sector that needs the most urgent support

While education and health sectors are severely underfunded, social protection fares the worst. Governments currently prioritise education, while donors prioritise health. Our analysis shows that donors provide only 8% of the funding needed to fill the social protection aid funding gap (the gap left after governments have maximised their tax and funded each sector in line with international spending targets).

Figure 10 Social protection is the least funded sector



Source: authors' estimates

One result of this underfunding for social protection is the delay in scaling up (and in some cases creating) coordinated national cash transfer programmes to support those trapped in extreme poverty. Globally, over a third of the people who escape from extreme poverty are able to do so because they receive such transfers. Greater investment in social protection also facilitates 'growth from below', with most people who escape poverty doing so through small, usually informal investments from individuals and households (CPAN, 2019).

Yet the latest figures from the World Bank note that only one-fifth of the poorest people in LICs are currently covered by a social safety net programme (World Bank, 2018). As a result, few LICs have national programmes that match the scale of Ethiopia's highly successful Productive Safety Net programme. This programme offers the poorest households paid employment through small-scale investments in agriculture, such as irrigation canal and tree-planting schemes (see photo). The programme also includes training in nutrition and livelihood skills. Such investments not only enable households to lift themselves out of poverty, but also make them more resilient in the face of climate change.

Small-scale irrigation canal, Ethiopia Productive Safety Net © Photo by Nena Terrell/USAID

While this index is more rigorous than previous measures, a similar ranking emerges from simpler measures, such as the proportion of aid given to LDCs. Among the major DAC donors, Ireland also scores the highest (providing 50% of its bilateral aid to LDCs). And most of the higher scoring multilateral agencies provide more than half their aid to LDCs – as does IsDB, GAVI, IFAD and the World Bank's IDA. The largest notable exception is EU institutions, which collectively only provided a quarter of their aid to LDCs.

Conclusions and recommendations

Global leaders have committed to ending extreme poverty. But the prospects of delivering on this commitment are dwindling as we fall further and further behind. The latest projections in this note are that 430 million people will be living in extreme poverty by 2030 – 30 million more than last year's projection.

More investment in effective education, health and nutrition and social protection programmes could end extreme poverty. Most countries can afford this investment if they better target their spending and maximise their taxes. But that leaves 46 countries that still cannot meet the costs. These countries face a $222 billion a year funding shortfall in ending extreme poverty. Almost half of this gap can be filled by the countries themselves, the other half through more and better targeted aid.

The focus of this analysis is on public finance – tax and aid – as private finance is rarely used as a major source of finance for the provision of basic social services. There is much greater potential for mobilising private sector finance for infrastructure. However the private sector can play an important role in the delivery of social services. While the focus of this analysis is on ensuring there is sufficient finance available, it will also be crucial to ensure that the finance is well spent.

The key challenge for leaders as they gather in September for UN High-level Political Forum on Sustainable Development and the high-level dialogue on financing for development is whether donor countries, in partnership with the poorest countries, will make the affordable changes to their public financing priorities that are needed to end extreme poverty. If they do, they could ensure that no-one is left behind. They could enable all countries to mobilise the resources needed to lift everyone out of extreme poverty by 2030, and to ensure that everyone has the chance to attend school, access essential healthcare, receive high-impact nutrition interventions and be covered by social protection.

Recommendations

The poorest countries (LDCs) should:

1. increase their tax revenues by a quarter (to the maximum level that is economically feasible)
2. allocate half of their public spending to health, education and social protection (as Ethiopia and Tanzania have come close to doing).

DAC donors should:

1. double their collective aid, with all donors meeting the UN target for ODA (following the example of four major DAC donors)
2. double the share of their collective aid given to LDCs from one-quarter to a half (following the example of Ireland)
3. press all multilateral agencies with a global reach to provide at least half of their support to the poorest countries (as most already do).

Financing the end of extreme poverty

odi.org/end-poverty

430 million people

will be living in extreme poverty by 2030.

That's 30 million more than last year's projection.

+7.5%

More investment in these areas could end extreme poverty:

- Effective education
- Health and nutrition
- Social protection programmes

Most countries can afford this investment if they better target their spending and maximise their taxes.

But there are still 46 countries that cannot.

- **$86bn:** Existing funding in those 46 countries
- **$222bn:** Funding shortfall in ending extreme poverty

Almost half of this gap can be filled by the 46 countries themselves, the other half through more and better-targeted aid.

COUNTRIES

DONORS

We could finance the end of extreme poverty by 2030 if…

Current Target

COUNTRIES
maximise their tax revenue

+25%

and

allocate half of public spending to education, health and social protection.

DONORS
meet the UN 0.7% ODA/GNI target*

and

target half their aid at the poorest countries.

Poorest countries

*United Nations Official Development Assistance/Gross national income target

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