Middle Income Countries and Innovative Financing for Agricultural Development

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The report of the UN Department of Economic and Social Affairs (UNDESA) for 2014 raises a number of issues related to Middle Income Countries and the changing Official development Architecture. In particular, the emergence of Middle-Income Countries (MICs) and the increasing role that domestic resource mobilization may play.

This implies a reflection on which type of aid will go to MICs (e.g. more loans) and which type will go to the poorest countries. It also raises questions on how financing institutions will review their aid policies when more and more countries graduate from poor to middle income status. As a consequence, the complementary role of innovative financing for development can be to a way unlock private funding, in particular through Public - Private partnerships . This article briefly describes these the three subject matters

The AID landscape provides mixed signals

Official development assistance (ODA) grew by 6.1% in 2013. However, the share of aid going to some of the world's least developed countries is falling, despite the overall increase in spending[1]. More donors are focusing on middle income countries, giving aid in forms other than grants, (equity investments and loans, guarantees) which developing countries must pay back as ODA.

The OECD's development assistance committee (DAC) is undertaking negotiations on the future of foreign aid polices. Under one proposal presently being debated, countries with a per-capita national income of more than $7,115 would be removed from the list of eligible recipients. Separately, the World Bank is also considering how it will categorize countries into income groups, with a new system likely to be introduced next year. Similar considerations will also shape the future of the largest multilateral financial institutions, such as the European Development Fund (EDF) the International Development Association, (IDA), the African Development Fund (AfDF) and their parent bodies.

As to Low income countries, estimates suggest that ODA still accounts for 40% of fiscal revenues in low-income countries and 70% of their external finance. Some donors are already reducing their list of aid recipients. The EU aid in the 2014-20 period will prioritize the poorest countries, though middle-income states will remain eligible for some thematic and regional funding.

The implications

Domestic resource mobilization will therefore be key to address poverty problems in many countries.

The global poverty 'problem' is changing. New research shows that *there is a new 'bottom billion' of 960m poor people or 72 per cent of the world's poor who live not in poor countries but in middle-*

[1] OECDE 2013 Report. In 2013,aid to Africa fell by 5.6% to $28.9bn

income countries (MICs[2]). This is a dramatic change from just two decades ago, when 93 per cent of poor people lived in low-income countries (LICs).

This is not just about India and China and the findings are consistent across monetary, nutritional and multi-dimensional poverty measures. Contrary to earlier estimates that a third of the poor live in fragile states, the estimate is about 23 per cent, and they are split fairly evenly between fragile LICs and fragile MICs.

One read of the data is that poverty is increasingly turning from an international to a national distribution problem, and that governance and domestic taxation and redistribution policies become of more importance in many countries than ODA. "*The perseverance of poverty is more a distribution question than a question of lack of resources*"[3].

Domestic resource mobilization may therefore be of help based on different lines of argument:

- countries where there are financial resources but not enough technical expertise for agricultural development;
- countries where there are both financial and technical resources but what is needed is social engineering, know-how transfer, how to put together resources and existing technical expertise.

Where ODA is still necessary

As to Low income countries, estimates suggest that ODA still accounts for 40% of fiscal revenues and 70% of their external finance[4]. Some donors are already reducing their list of aid recipients. The EU said its aid in the 2014-20 period will prioritize the poorest countries, though middle-income states will remain eligible for some thematic and regional funding.

In any case, in both middle income and low income countries the issue of introducing innovation in the way funding is channeled will be key to efforts to obtain sustainable development.

Innovative Financing for development in addition to ODA and the role of the private sector

It is commonly agreed upon that there is need to better and more fully spend what is already available; too often, focusing on advocating for the allocation of more resources leads to a neglect of spending entirely what is already available. This calls for ways and means to progressively introduce *innovation* in the way existing financial and technical resources are channelled into the agricultural sector (ODA, national budgets, private investment).

The private sector is increasingly becoming the driving force behind rural economies in many developing countries, particularly in Africa. But the general move towards market economies does not necessarily reach poor rural people. **Blending of public and private resources** in the poorest regions of the world are necessary because it is increasingly clear that no one sector in society can deliver the complexities of sustainable development alone.

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[2] Institute for International Development 2013 , DANIDA 2013, OECD 2013

[3] Danish NGO Forum (2012)

[4] OCDE 2013 report

In the area of agriculture and food security, **Public-private partnerships** are therefore an innovative means to raise more resources. **Cost and risk** are the two major bottlenecks limiting agricultural finance[5]. For this reason, **Value-Chain Financing** opens up the potential for much investment to agriculture. For example: **risk management and warehouse receipts, advance market mechanisms and migrants' remittances:**

1. **Risk Management Tools such as Farmers' Weather-Index Insurance Schemes -** Farmers face a variety of market and production risks that make their incomes unpredictable from year to year. Index insurance, is a financial product that is linked to an index highly correlated to local yields. Pay-outs on the insurance policy are triggered by pre-specified patterns of the weather index, as opposed to the actual yields of the crops (very costly to be verified through field visits) . Given the consequences of global climate change, weather index insurance may also play a role in supporting adaptation strategies in developing countries.

2. **In *Warehouse Receipts*,** Producers and/or traders deposit their produce at the warehouse and are, in turn, issued a receipt certifying secure and safe storage of the goods for a specified period of time. The warehouse receipts serve as collateral or pledge for securing loans from banks or other lenders with the condition that proceeds from the sale of the produce should first be used to repay the loan. If public money **(national budgets and ODA**) are used to trigger off and support the above (private) two value chain financing schemes, the multiplier effect on agricultural production and food security may be very important, particularly in countries with a fragile agriculture.

3. **Advance market mechanisms** A third example of public-private partnerships to catalyze private investment is provided by **Advance market mechanisms** through which donors commit money to guarantee minimum prices and markets for agricultural and nutritional innovative products (e.g. animal vaccines, improved seeds, local ready-to-use food) that could be developed by the private sector.

4. **Migrants'remittances.** As a final example, the promotion of the investment of migrants' remittances in agriculture. In other words, matching each dollar sent by migrants home with ODA resources and appropriate national credit and fiscal policies, in order to encourage collective investments in agriculture instead of the present fragmentation whereby out of the over USD 500 billion per year that migrants send home, not more than 10-20 per cent goes to saving and investment (and even less to agriculture).

Development agents, such as the UN, can act as catalysts to enhance private and public sector investments, adding value from a development perspective. Support to boost private and public

[5] As mentioned in the UNDESA report, policies to facilitate investment need to address: (i) reducing risks by creating an enabling environment (ii) sharing risks to leverage private resources with public funds; (iii) restructuring investor incentives to reduce short-term oriented behaviour; and (iv) balancing regulations to ensure financial sector stability with access to credit and financial services.

sector initiatives, might include policy advice, pilot projects, technical assistance ,training and capacity building.