USAID's Approach to Poverty Reduction

Synthesis of Studies in Honduras, Mali, Romania, and Uganda

EVALUATION BRIEF NUMBER 9

Summary

TO WHAT EXTENT IS USAID's "sustainable development" goal similar to or different from the poverty reduction approach adopted by many other donors and development banks? USAID's Center for Development Information and Evaluation examined this question by looking in detail at four mission programs: Honduras, Mali, Uganda, and Romania. Honduras, Mali, and Uganda are highly indebted poor countries (HIPCs) that have developed national poverty reduction strategy papers (PRSPs) to qualify for debt relief. Romania is a middle-income country that has not developed a PRSP.

The assessment found the following:

- In HIPCs, most of USAID's resources are allocated to direct delivery of services that are highly focused on poor people in the areas of health, nutrition, population, humanitarian assistance, education, microenterprise, and agricultural extension.
- USAID's support for economic growth by means of policy, legal, and institutional reform has declined dramatically in HIPCs. The Agency's programs in Romania were significantly more growth oriented than those in HIPCs.
- In HIPCs, insufficient resources and attention have been devoted to economic growth programs and policy reform that could contribute to sustainable development and an enabling environment for poverty reduction. Though the task of promoting economic growth in very poor countries is formidable, without growth, poor countries will remain poor.

KEY IDEAS

1. In highly indebted poor countries, USAID allocates most resources to direct provision of social services to the poor and has greatly decreased support for programs that create economic growth through policy, legal, and institutional reforms.
2. Economic growth programs could promote the sustainable development necessary to permanently reduce poverty in such countries.
3. Two main factors have influenced USAID's resource shifts away from economic growth programs—the Agency's reporting requirements and congressional earmarks and directives.
4. The assessment recommends that more attention be paid to removing obstacles to economic growth, including distorted exchange rates, inappropriate fiscal policy, weak banking sector, and distorted price and regulatory regimes.
5. USAID should continue to exert influence in the PRSP process to increase attention to economic growth and poverty reduction issues.

- Reporting practices required by USAID's "management for results" system and congressionally mandated soft earmarks have influenced the shift from economic growth to social services.

- PRSPs generally encourage donors to support social services to relieve the symptoms of poverty rather than supporting economic growth to address the fundamental causes of poverty.

The assessment findings raise key policy questions:

- Has USAID found the right balance between economic growth programs and social expenditures in HIPCs?

- Are PRSPs neglecting economic growth? Should USAID work with other donors to increase the attention to growth objectives in PRSPs and encourage private sector participation in PRSP processes?

Background

The assessment team examined how missions have balanced service delivery priorities and economic growth programs and what their involvement has been in PRSP processes. Although the sample is small, the findings may be instructive for USAID policymakers endeavoring to meet the Millennium Development Goal of cutting the incidence of extreme poverty in half by 2015.

Synthesis Findings

Shifting from Economic Growth to Direct Delivery of Social Services

In the HIPC missions studied, funding to support economic growth and policy reform has declined dramatically. In Honduras, Mali, and Uganda, economic growth programming fell from 60 percent of mission portfolios in the mid-1990s to less than 20 per cent in 2002. Romania did not experience such a decline: over 50 percent of USAID funds in Romania went to economic growth in fiscal years 1996–2001. This decline of growth-oriented aid in HIPCs is worrying because economic growth is the most effective way to reduce poverty and improve social conditions over the long term. Growth encourages investment, creates jobs, reduces unrest and an exodus of skilled workers, and creates an enabling environment that permits the poor to be more productive. Growth is also necessary for social services to be sustainable.

Today, the Agency's programs in HIPCs are heavily weighted toward direct delivery of services. In the three HIPCs studied, population, health, nutrition, and education (PHNE) programs grew from 14 percent of USAID portfolios in 1995 to 53 percent in 2002. This proportion substantially exceeds the UNDP guideline that 20 percent of donor country assistance be allocated to social services. In Mali and Uganda, population, health, and nutrition programs may be receiving more money than can be effectively absorbed.

This pattern is repeated in other HIPC USAID programs. In 2003, nearly half the portfolio of 21 HIPC missions was devoted to PHNE services (see table). In these countries, total USAID allocations for economic growth declined from about $441 million in 1995 to $152 million in 2003, while PHNE allocations grew from about $93 million in 1995 to over $400 million in 2003. The lion's share of PHNE funding was devoted to health (including HIV/AIDS), population, and nutrition. Education accounted for only one-fifth of PHNE funding between 1999 and 2001. (This was the average; the share of PHNE funds going to education varied greatly by mission.)

Direct provision of services (such as in health, nutrition, and education) can make people more productive and improve the lives of the poor, especially if such services are targeted at low-income people. However, improved services today often beg the question of how to sustain them tomorrow.

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Clearly, improved provision of social services is not sufficient to produce economic growth.

Growth requires good policies, strong institutions, and favorable business climates. These have to be built by local leaders dedicated to improving their economies; they cannot be produced by foreign aid. However, aid programs can help internal efforts to improve growth conditions achieve results. Where local political commitment is strong, such assistance can bring long-term benefits to national economies.

The case studies found that USAID missions rely heavily on local NGOs and U.S.-based PVOs to deliver social services in many HIPCs. This practice may be necessary where governments are weak or corrupt, but it raises questions about long-term sustainability. Some donors believe that aid should support capacity building in governments—to improve their effectiveness to provide social services.

Finally, the case studies found that USAID programs in the HIPCs often favor decentralized regional or municipal programs as a way of avoiding centralized inefficiencies and giving voice to local populations in their own affairs. However, such programs have to avoid the pitfalls of empowering local elites.

Earmarks and Management for Results

What drove the shift in Agency programs from economic growth toward social services? The case studies found two factors to be most important. First, congressional earmarks and directives in population, child survival and disease, nutrition, education, and agriculture favored the social sectors. Economic growth is not included in the functional accounts, and the demand for funds for growth programs has far exceeded what Congress has appropriated.

Second, USAID's results-based reporting system encourages missions to favor social service programs because the outputs, beneficiaries, and national impacts of these programs are more easily measured than those for economic growth programs. Progress in improving central bank transparency or reform of exchange rate policies is difficult to measure, especially on a short-term basis.

Special Challenges

The case studies found widespread obstacles to private investment and growth in HIPCs.

In all three HIPCs, insufficient attention has been given to the following:

- exchange rate policies that penalize exports
- fiscal deficits that put a drag on growth
- incomplete privatization agendas and outdated regulatory structures

Requested USAID Program Levels in 21 HIPCs
($ millions)

	1995	1996	1997	1998	1999	2000	2001	2002	2003
Economic Growth	441	438	219	228	160	151	144	168	152
PHNE	93	118	198	196	253	251	324	334	410
Democratic Governance	45	40	56	46	65	57	58	54	90
Environment	65	65	82	60	66	68	75	36	34
Humanitarian Assistance	75	85	224	233	119	158	164	168	154
Total	**720**	**746**	**779**	**763**	**663**	**685**	**765**	**761**	**840**

Source: USAID congressional presentations. Totals reflect rounded numbers.

- weak or risk-averse banking sectors that fail to finance domestic investment

- chaotic transport and freight regimes that make it difficult to export

Other problems vary by country. In Uganda, an appreciating local currency (in 2001–02) has hurt exports and private investment. Mali suffers from poor physical infrastructure and governmental mismanagement. In Honduras, inadequate rule of law is a major obstacle to increased investment. Honduras also has higher than average income inequality in a region with the highest level of income inequality in the world. This suggests that more activities are needed to strengthen the human capital of poor households, increase their access to productive assets, and provide infrastructure that expands their access to markets.

In Romania, evaluators noted stubborn pockets of poverty in spite of recent gains in national growth rates, and noted that the mission's strategic plan for 2002–06 calls for increased attention to vulnerable groups.

Involvement of USAID Missions in PRSPs

In Mali, Honduras, and Uganda, PRSP processes did not involve the business community. They did involve civil society (mainly local NGOs), but the extent of civil society participation varied. Civil society participation was relatively strong in Honduras, weak in Mali, and nonexistent in Uganda.

USAID's participation in PRSP processes was mixed. In Mali it was limited to facilitating contacts between government and civil society and encouraging a gender component in the PRSP's governance sector. In Uganda and Honduras USAID participation was strong: missions were fully engaged in policy dialogue and implementation discussions. In Uganda, the USAID mission played a key role in developing education and health policies. In Honduras, the mission pushed for the adoption of many USAID programming goals and incorporation of transparency and anti-corruption objectives in the PRSP. As part of IMF and World Bank adjustment programs, USAID also provided technical assistance to the Honduran Government to assess the effects of macroeconomic and sectoral policies on economic growth and poverty reduction.

In general, USAID participation in PRSPs had the effect of strengthening attention to economic growth issues. Most PRSPs tend to focus on poverty alleviation and improving social services. USAID missions encouraged PRSPs to also address broader issues that can affect long-term growth and poverty reduction, such as policy reforms, institutional improvements, and improvements in transparency and control of corruption. Mission participation also contributed to improved donor coordination.

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