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From Poverty Reduction to Mutual Interests?

The debate on differentiation in EU development policy

Svea Koch

From poverty reduction to mutual interests? The debate on differentiation in EU development policy

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Abstract

This paper looks into the issue of how European Union (EU) development policy can respond to a changing development landscape that is characterised by a different geography of power and wealth and a changing geography of global poverty. The question of how to differentiate its partnerships and how to best engage with middle-income countries (MICs) has been among the most discussed issues in the ongoing process of modernising EU development policy. The analysis in this paper puts the question of aid to MICs in the context of two interlinked challenges: (i) the need to reconceptualise dominant approaches to global poverty reduction that prioritise national income as a key guiding criterion to classify countries, and (ii) the growing range of global challenges that require development policy to diversify its objectives. With regards to the implications for EU development policy, the paper draws two main conclusions. First, tackling global poverty needs a better coordinated cross-country division of labour at the EU level to avoid marginalising countries that have become wealthier in per capita terms but that continue to experience internal development challenges. Second, addressing challenges related to complex global public goods requires EU development policy to continue its engagement with emerging economies and other increasingly powerful developing countries. Such diversification of objectives, however, will increase the coordination challenges of EU development policy and other European external policies substantially.

Svea Koch | Bonn, September 2012

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Abbreviations

ACP	African, Caribbean and Pacific Group of States
ALOP	Asociacion Latinoamericana de Organizaciones de Promocion / International Land Coalition
APRODEV	Association of World Council of Churches Related Development Organisations in Europe
BMZ	Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung / Federal Ministry for Economic Cooperation and Development
CIDSE	Coopération Internationale pour le Développement et la Solidarité / International Cooperation for Development and Solidarity
CIFCA	Iniciativa de Copenhague para Centroamérica y México
DAC	Development Assistance Committee
DCI	Development Cooperation Instrument
DIE	Deutsches Institut für Entwicklungspolitik / German Development Institute
DFID	Department for International Development
DGM	French Directorate-General of Global Affairs, Development and Partnerships
ECOSOC	United Nations Economic and Social Council
EDF	European Development Fund
ENPI	European Neighbourhood Policy Instrument
EU	European Union
FDI	Foreign Direct Investment
GNI	Gross National Income
GPG	Global Public Good
LDC	Least-developed Country
LMIC	Lower-middle-income Country
LIC	Low-income Country
MDG	Millennium Development Goal
MIC	Middle-income Country
MPI	Multi-dimensional Poverty Index

ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OLICs	Other Low-income Countries
UNDP	United Nations Development Programme
UNFPA	United Nations Population Fund
UNOFS	United Nations Organization for Food Security

1 Introduction

The global development landscape is changing tremendously and presents the challenge for European development[1] policy to change with it. The distinction between "developed" and "developing" countries, the transfer of aid from the world's wealthiest to the world's poorest countries and the perception that poverty is predominantly the problem of poor countries have long been central to development policy. However, separating the world into "poor" and "rich", "North" and "South", and "donors" and "recipients" has become increasingly ill-suited to capture the changing relationships among countries. Over the last two decades, many developing countries have seen considerable economic growth, which has resulted in a changing geography of wealth and power with geopolitical ramifications. In this increasingly heterogeneous and differentiated development landscape, only 36 countries remain classified as "low-income"[2] (the most widely used term for a poor country), while the number of countries with higher per capita incomes has increased significantly. As countries become richer in per capita terms, they are also becoming less dependent on aid; development assistance typically accounts for a marginal share of the national budget and a country's gross national income (GNI). Against this background, it is increasingly being questioned whether it is still appropriate to provide EU aid to countries that appear wealthy enough to fund their own development without external financial assistance.

But even if income disparities between developing countries and those in the Organisation for Economic Co-operation and Development (OECD) are on the decline, the challenges of poverty reduction and inequality remain unresolved. In many developing countries, rapid economic growth was accompanied by an increase in social inequalities and insufficient reductions in poverty. A widely read study of Sumner (2010b) highlighted that more than 70 per cent of the world's poorest people – what he calls a "new bottom billion" – do not live in low-income countries, but rather in middle-income countries (MICs). Development agencies in the EU and OECD countries that have committed themselves to global poverty reduction are still coming to terms with this new geography of wealth and power on the one hand, and the new geography of poverty on the other.

At the same time, global development challenges beyond poverty reduction have gained importance. Intensifying globalisation and the frequency and intensity of global crises in recent years have revealed the increasing interconnectedness of the world and the global nature of development challenges. In such a globalised world, major challenges such as climate change, food insecurity, financial instability, communicable diseases, migration, conflict and insecurity are not only challenges that potentially affect us all; they also ultimately depend on the development paths of developing and emerging countries and their commitments and cooperation in global governance processes. Development policy

1 For the purpose of this paper, the term "EU development policy" is used rather than solely referring to the European Commission. The degree of independence of a supranational actor such as the European Commission is limited due to the influence on decision-making of the member states (Tallberg 2002; Furness 2010). However, the focus of this paper does not include bilateral aid programmes of member states but refers to aid that is spent through Community Institutions in Brussels.

2 This is according to the latest World Bank classifications of 2012.

can play an important role in addressing these complex challenges. Its objectives, therefore, need to diversify and new forms of cooperation with influential non-OECD countries need to be sought.

For EU development policy, the concomitance of these developments poses significant challenges. On the policy level, the EU has so far emphasised the primacy of poverty reduction in its development programmes – an approach that has become increasingly incompatible with the large and increasingly heterogeneous partner country portfolio of the EU. Recognising the need to adapt its policies and objectives to a changing international environment, the EU is currently in the process of modernising its development policy. The need for greater differentiation between partner countries and the extent to which MICs should continue to receive EU aid are key points of the EU's new development policy agenda[3] and the negotiations on the next EU multi-annual financial framework.[4] According to the European Commission's Communication and the Council Conclusions of 14 May 2012,[5] the EU plans to withdraw its bilateral development cooperation programmes from 19 developing countries[6] that have either reached upper-middle-income status or account for 1 per cent of global GNI. On a more conceptual basis, the EU aims to better calibrate and target partner engagements and to include strategically-oriented policy objectives alongside a strict poverty reduction remit. In other words, the argument for differentiation is that development cooperation with more advanced countries should shift focus from poverty reduction to global challenges and mutual interests (Gavas et al. 2011).

So far, research has mainly focussed on analysing the changing distribution of wealth (e.g. Spence 2011; OECD 2010; Rodrik 2011), the increasingly global rationale of development policy (e.g. Severino / Ray 2009; van Lieshout et al. 2010) or the question of aid to MICs on a conceptual basis (e.g. Alonso et al. 2007; Kanbur 2010; Fenton 2008; Sumner 2011a; Kanbur / Sumner 2011). These discussions have not yet been combined and analysed from the specific perspective of EU development policy. This paper contributes towards filling this gap by synthesising existing debates and by outlining the implications of a changing development landscape for the EU's engagement with MICs. It does not attempt to provide an in-depth analysis of the restructuring of the global economy, geopolitical power shifts, global challenges or the changing patterns of global poverty. Rather, it aims to identify the main trends of a changing development landscape that need to be considered in the strategic reorganisation of EU development cooperation with MICs.

The remainder of this paper will outline the challenges of such a reorientation of EU development policy. The paper argues that the question of development cooperation with MICs needs to be answered in the context of two interlinked challenges: (i) the need to reconceptualise dominant approaches to global poverty reduction that prioritise national

3 "Increasing the impact of EU development policy: an agenda for change" (COM (2011) 637 final).

4 "Global Europe: a new approach to financing EU external action" (COM (2011) 865 final).

5 See: http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/130243.pdf.

6 Argentina, Brazil, Chile, China, Colombia, Costa Rica, Ecuador, Kazakhstan, India, Indonesia, Iran, Malaysia, the Maldives, Mexico, Panama, Peru, Thailand, Venezuela and Uruguay.

income as a key guiding criterion to classify countries and to design poverty-efficient aid allocations, and (ii) the growing range of global challenges that require development policy to diversify its objectives and to seek continued engagement with anchor countries and emerging economies.[7] It argues that both challenges are interrelated and that, even from a global governance perspective, the EU should remain concerned about a recipient country's internal development challenges. With regards to the implications for EU development policy, the paper derives two main conclusions. First, contributing to global poverty reduction will require a better coordinated cross-country division of labour at the EU level to ensure that countries with higher per capita incomes – but significant internal development challenges – are not left alone in their fight against poverty and social inequality. Second, addressing complex challenges relating to global public goods requires the EU to increasingly adopt a global development approach and to reorganise its development cooperation with anchor and emerging countries accordingly. This, however, will also increase the coordination challenges among European donor agencies and other European external policies substantially.

The paper starts off in Chapter 2 by analysing the past debate on aid to MICs at the EU level and the EU's current approach. In Chapter 3, it analyses the main trends of the changing geographies of growth and poverty that require the EU to rethink and adapt its approaches and strategies towards MICs. The fourth chapter analyses two resulting challenges that need to be considered in discussions about continued or discontinued development cooperation with MICs: (i) the need to reconceptualise the poverty focus, and (ii) the global rationale for development policy. The last chapter outlines the implications of both challenges for EU development policy.

2 The debate on differentiation in the EU context so far

The question of how to best adapt development policy to the specific needs of countries with advanced development and higher levels of average income is not entirely new.[8] Thus far, the reactions and strategies of European donors basically have fallen into two categories based on different rationales for providing aid: a narrow definition of development policy, which prioritises poverty reduction as the overarching objective for

7 In this paper, a distinction is made between anchor countries and emerging economies. Even though most anchor countries fall within the group of emerging economies, this is not necessarily the case. Emerging economies are characterised by increasing per capita income, high growth rates and growing weight in global governance processes. Anchor countries, on the other hand, are characterised according to their economic and political weight in their respective regions (Stamm 2004).

8 In 2003, for example, DFID and the Spanish Agency for International Cooperation commissioned a study with the objective to outline the rationale for aid to MICs (Eyben et al. 2004). In 2005, DFID published a special strategy for their engagement in MICs titled "Achieving the Millennium Development Goals: the middle-income countries" (DFID 2005). The UN held a series of international conferences on development cooperation with middle-income countries between 2007 and 2009 and published a number of reports and resolutions exclusively dedicated to the question of how to undertake development cooperation with MICs (UN 2007, 2009). In 2007, the World Bank issued a special evaluation of its role in MICs (World Bank IEG 2007). In 2008 Oxfam commissioned a study with the aim to rethink the role of MICs in the development process, as it became clear that income status graduation cannot be considered as an endpoint to development (Fenton 2008).

development programmes and aid allocation to the poorest countries. By focussing mainly on the poorest countries, these donor agencies expect to have the greatest impact on poverty alleviation. The United Kingdom's Department for International Development (DFID) and its 90/10 rule (90 per cent of aid resources for low-income countries (LICs) and 10 per cent for MICs) is the most prominent example of this approach. It is based on the dominant thinking at that time that there is less concentration of poverty in countries with higher average per capita incomes, and that poverty is predominantly a problem of poor countries. MICs, on the other hand, are expected to have greater access to international capital markets due to their better developed institutions and sound policies (Dollar / Pritchett 1998; Dollar / Levin 2004). As a consequence, these donors markedly reduced – or even withdrew – their aid to MICs.[9]

Other European donors have emphasised the need to conceptualise development policy beyond the narrow poverty reduction remit towards a global outlook on development. In this view, accelerating globalisation processes and the increasing interconnectedness of the world require development policy to focus on global challenges and key issues of global governance (Messner 2001; Faust / Messner 2006). Such a broad definition of development policy aims to contribute towards solving regional and global challenges in cooperation with non-OECD countries. For some EU donors, this has led to a diversification of the objectives of development policy: Germany and Sweden, for example, have increasingly shifted their strategies from "traditional" development policy and a focus on poverty reduction towards global structural policy or policy for global development.[10]

The latter shift of principles and objectives has also led to a different approach towards MICs and emerging economies. Rather than withdrawing from these countries, it was considered important to continue development cooperation but in a different manner (Altenburg / Stamm 2005). Germany's "anchor country concept"[11] (BMZ 2004) can be seen as a pioneering element in this respect and shaped the discussion at an early stage. It highlighted the external capacities of countries to create regional and global spillover

9 DFID's 2011 bilateral aid review has led to a further concentration of aid in 27 partner countries and to a decision to end the bilateral relationship with 16 countries, of which 12 are MICs; see: http://www.dfid.gov.uk/Media-Room/News-Stories/2011/The-future-of-UK-aid/. This process has been accompanied by a controversial debate about the continuation of UK aid to India (House of Commons 2011) and by a discussion about new partnerships with emerging economies; see: http://www.chathamhouse.org.uk/files/18611_150211mitchell.pdf. In the Netherlands, a recent revision of Dutch development cooperation has led to a reduction in the number of partner countries from 33 to 15, of which only four are MICs. Upper-middle-income countries, for example, were excluded from the partner country selection from the beginning.

10 In Germany, the term "global structural policy" was introduced in the coalition treaty under the chancellorship of Gerhard Schröder in 1998. The objective of global structural policy was to take development policy out of its niche of project aid and interventions at the local level and to aim at working towards structural changes at the national and global levels. In 2003, Sweden announced a bill to introduce its "policy for global development", which required not only the development ministry but all Swedish ministries to take due account of sustainable global development in all their policies and actions.

11 According to the updated definition of Leininger et al. (2009), "anchor countries are developing countries which, due to their economic weight in regional terms and due to their international role have the potential to create far-reaching spill-over effects and the state capacity to pro-actively influence regional and global processes" (ibid., 3).

effects as well as their central importance in global governance processes. A new cooperation approach was developed that was aimed at recognising the countries' increased self-confidence, their economic and political roles in regional and global terms, and the importance of moving towards mutual interests in solving global development challenges. Internal development challenges and poverty reduction, on the other hand, received less attention and were considered to be the country's own responsibility.

The EU can be considered a latecomer in these debates and has only started to address the issue of differentiation in its recent modernisation process. The EU's current approach can thus best be described as a mismatch between policy objectives and partner country portfolio. The European Consensus on Development[12] clearly states that the eradication of poverty is the primary and overarching objective of EU development cooperation, benchmarked against the Millennium Development Goals (MDGs). On a legal basis, this is also enshrined in the Lisbon Treaty (Art. 208), which has narrowed the focus and objective of EU development policy by making poverty reduction the central goal (Art. 208).[13] The European Consensus furthermore states that official development assistance (ODA) allocations should prioritise support to least-developed countries (LDCs) and low-income countries (LICs). At the same time, it is also made clear that "[d]evelopment aid will continue to support poor people in all developing countries, including both low-income and middle-income countries (MICs)" (Article 10) and that "the EU also remains committed to supporting the pro-poor development of middle-income countries (MICs), especially the lower MICs […]" (Article 24).

Unlike those EU donors for whom a clear focus on poverty reduction has been accompanied by a strong concentration of aid to the poorest countries, the EU has so far not adapted its partner country portfolio or aid allocations. For the time being, the EU's partner country portfolio includes 145 countries.[14] In 2009, the European Commission allocated more of its aid budget (incl. the European Development Fund, EDF) to MICs (EC 54 per cent, DAC average 41 per cent) and less to LICs than the Development Assistance Committee (DAC) average (EC 46 per cent, DAC average 59 per cent). While spending in LDCs does not differ greatly from the DAC average (EC 39 per cent, DAC average 43 per cent), the biggest contrast relates to spending in upper-middle-income countries (EC 19 per cent, DAC average 9 per cent) (see Figure 1).

12 The 2005 "European Consensus on Development", as a successor to the 2000 policy statement "The European Community's development policy", for the first time sets out a common vision and objectives that guide both the member states' and the EU's development policies.

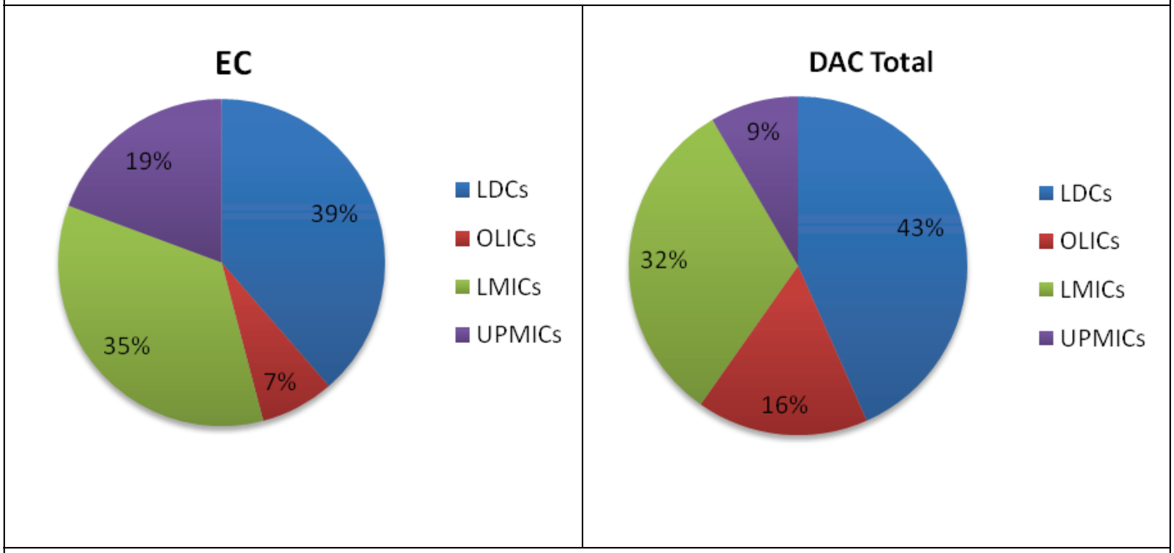
13 This clear focus is a significant change to the language of the preceding Treaty of Nice (Art. 177), which mentioned three objectives on equal footing: the sustainable economic and social development of the developing countries, the smooth and gradual integration of the developing countries into the world economy and the campaign against poverty reduction in the developing countries.

14 There are 124 countries that receive ODA from the DCI and the EDF. Apart from the DCI and the EDF, the ENPI covers Europe's 16 closest neighbours in Eastern Europe, the Mediterranean and the Caucasus, while the Instrument for Pre-Accession covers both candidate and potential candidate countries in the Western Balkans, Turkey and Iceland. The funds within both instruments are to a large extent ODA eligible. However, the rationale for "aid" to these countries is based on the EU's own strategic interests rather than pure developmental outcomes. The ENPI and the Instrument for Pre-Accession can be considered as "the most strategically refined aid instruments that are most precisely attuned to EU interests" (Holden 2009, 183).

This above-average funding for MICs is one of the most frequent criticisms of EU development policy and is considered as a lack of focus on poverty (Booth / Herbert 2011; Orbie / Versluys 2009; Dollar / Levin 2004). The 2007 DAC / Peer Review of the European Community echoes this criticism and states that "the Community has been under pressure from some Member States to increasingly concentrate on LDCs and other low-income countries, partly as a way to retain the poverty focus of its assistance" (OECD / DAC 2007, 40). One key challenge for the EU is therefore to concentrate its aid funds in better accordance with its overall objective of poverty reduction, but to do so based on a thorough understanding of changing patterns of poverty (see Section 3.1).

In doing so, the EU is confronting different obligations and framework conditions than member states. This relates particularly to a potential reduction of its partner country portfolio. The Cotonou Agreement provides the legal framework for governing the EU's partnership with the African, Caribbean and Pacific (ACP) group of states. Due to the contractual nature of the Cotonou Agreement, any cuts in aid or stalling of bilateral development cooperation will have to pass the dialogue principle and be mutually agreed by the EU and the ACP. This is the main reason why the debate on differentiation has so far mainly focussed on countries in Latin America, Asia and Central Asia, the Gulf region and South Africa that are funded by the Development Cooperation Instrument (DCI). In addition, the EU is expected to act in complementarity vis-à-vis member states' bilateral programmes, and one of its identified comparative advantages is to maintain global presence: "The Commission is present as a development partner in more countries than even the largest of the Member States, and in some cases is the only EU partner substantially present […] covering practically every developing country and region […]" (European Parliament / Council / Commission 2006, 8). Thus, a potential partner country reduction has to include a discussion about the EU's role vis-à-vis member states' programmes and the extent to which the mandate of a global presence requires an adaptation of the strategic orientation of EU development policy.

Figure 1: Comparison of aid flows by income group: EC and DAC totals for 2009



Source: Own based on http://stats.oecd.org/Index.aspx?DatasetCode=ODA_DONOR

The central mismatch that has evolved in EU development policy relates to its formal adoption of one overarching policy objective in its policies and programmes on the one hand, and its global presence on the other. In order to respond to an increasingly heterogeneous and differentiated development landscape, the narrow focus on poverty reduction has proven to be too limited. This became particularly evident with the example of the DCI. Many countries that are covered by the DCI have achieved higher per-capita income, meaning that the instrument now has a strong MIC focus.[15] Yet, its regulation requires all programmes to be consistent with the overall objective of poverty reduction. The limitations of this approach became particularly visible during the mid-term review of the DCI. During this process, the European Parliament raised concerns that some of the actions programmed under the DCI's geographic programmes would not meet ODA criteria. They added that the actions programmed were not sufficiently oriented towards the poverty eradication objective and the pursuit of the MDGs before they called for the withdrawal of these measures. The Commission, on the other hand, argued that it is becoming increasingly important to have the scope to fund measures beyond ODA in emerging economies such as China, Brazil and India and in several dynamic developing countries.[16]

Looking at country programming, one can see that in most emerging economies and countries with higher levels of development, the EU is currently in a transition phase. While maintaining the traditional focus on poverty reduction, most Country Strategy Papers of emerging economies increasingly include a more strategic orientation towards areas of mutual interest. In India, the EU follows a "two-pronged approach". While still committed to fighting poverty, the EU's objectives have become more strategic, moving "away from the aid rhetoric that had no objective beyond poverty reduction" (Coulon 2008). Traditional development assistance is thus increasingly moving towards trade, economic and cultural cooperation, and areas of mutual interest such as energy, transport and the environment (ibid.). The Country Strategy Paper for China 2007–2013 notes that China is moving away from being a traditional ODA recipient and that the cooperation programme is an important mechanism to support the EU's own major economic and political interests in China's development. Poverty reduction objectives (mostly by supporting social protection mechanisms and the decent work agenda) are therefore combined with mutual interests such as climate change, the improvement of financial services and trade cooperation. The Country Strategy Paper for Brazil 2007–2013 acknowledges the limited impact that the EU can have on poverty reduction – given the low aid dependency of Brazil – and emphasises that ODA is not the key to Brazil's development. Moreover, the 2009 Communication of the Commission "The European Union and Latin America: Global Players in Partnership" highlights the need to increasingly integrate activities of mutual interest alongside activities aimed at poverty reduction, in particular in emerging economies and MICs in the region:

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15 According to the list of countries in the amended regulation of 14 October 2009 and comparing this list with the 2011 World Bank classifications, most countries receiving funds from the DCI are either lower-middle-income countries (LMICs) (47 per cent) or upper-middle-income countries (UPMICs) (33 per cent), while low-income countries account for only 20 per cent.

16 "Mid-term review of the financial instruments for external actions" (COM (2009) 196 final).

„The merits of significantly diversifying the instruments and targets of EC cooperation should be explored. While concentrating financial resources on the poorest countries, the EU should look for new forms of cooperation with countries with higher levels of development. For all countries, this may entail putting more emphasis on cooperation in areas such as climate change (mitigation and adaptation), higher education, multi-lingualism research, science and technology, including energy efficiency and renewable energy, to complement joint efforts" (European Commission 2009b, 9)

A second challenge for the EU therefore relates to reconceptualising its development cooperation, increasingly targeting a portfolio of strategic objectives and refocusing its assistance to countries with higher levels of development. So far, a gradual shift in individual partner countries has not been accompanied by a strategy for global development and a coherent strategy on how to work with more advanced countries to this end. Moreover, discussions thus far have not included a clear strategy on how to shape a gradual transition from a focus on poverty to areas of mutual interest or how to potentially combine both strategic objectives.

Approaches to tackling both challenges – concentrating EU aid funds where there are likely to have the greatest impact on poverty reduction, and reconceptualising development cooperation with emerging economies and countries with higher levels of development – need to be based on a thorough understanding of the key changes in the development landscape.

3 The changing development landscape

One could rightly argue that there has been nothing more constant than change in the international development landscape. The fundamental nature of the current transformation, however, indicates that the developments over the last decade or two have been of historical significance and have created an international environment that is significantly different from the post–Second World War or post–Cold War period.

3.1 The changing geography of growth

From a development perspective, the world had been viewed for a long time as a two-polar, binary order with a few rich countries surrounded by a majority of poor countries.[17] The distribution of income was mainly divided according to these two poles: most of the world's population lived either in rich or in poor countries, with few in between (Harris et al. 2009).[18] This dividing line between high-income and low-income countries also mirrored the distribution of global poverty. According to estimates, in 1990, 93 per cent of

17 The most prominent theoretical foundation for dividing the world into a dichotomist structure are the dependency theories first developed in the late 1950s by Paul Prebisch (then Director of the UN Economic Commission for Latin America, CEPAL), and further developed by Andre Gudrun Frank (1966). Dependency theories were an attempt to explain the underdevelopment and persistent poverty of many nations as a direct consequence of the interactions and economic activities of developed countries.

18 This distinction into "developed" and "developing" does not neglect the tripartite division of the world into first, second and third world during the Cold War. The reference to a two-polar world-order relates in particular to the distribution of wealth and the distribution of global poverty without drawing on political criteria that have shaped the relations between countries at that time.

the global poor lived in LICs (Sumner 2010b). Poverty was thus predominantly a low-income-country problem – aid transfers from the world's wealthiest countries to the world's poorest ones were a key element of the development agenda. This, in turn, has characterised the relationship between countries and distinguished them as either "donors" or "recipients", while the approaches and actions of the development business became "aid-centric" (Harris et al. 2009, 7).

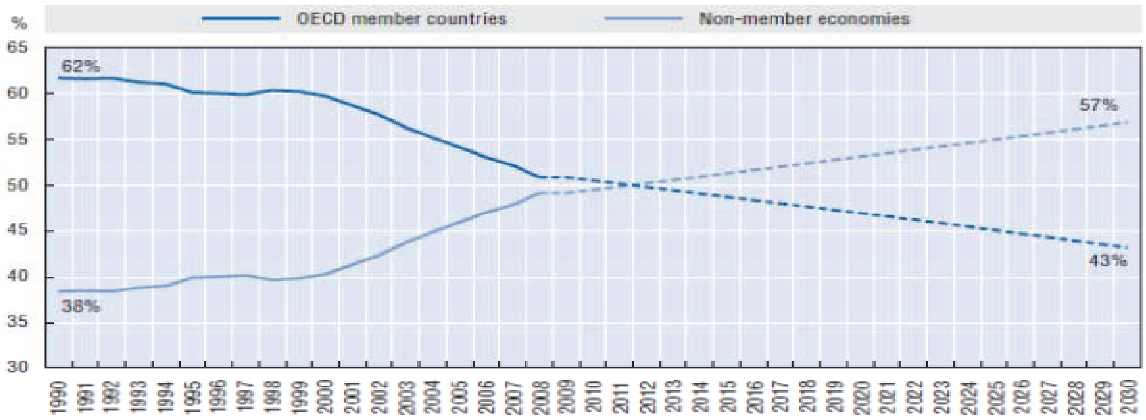
However, the perception that the world can, from a development perspective, be explained by a dichotomous distinction into "developed" and "developing", "donor" and "recipient", "North" and "South" is today even more debatable than it was in the mid 1990s. With the exception of the rise of the Asian Tigers, the 1980s represented a "lost decade" triggered by financial crises and instability for mainly two regions: Latin America and sub-Saharan Africa. However, starting in the 1990s and accelerating in the 2000s, much of the developing world has seen strong economic growth, resulting in tremendous changes in the geography of growth and wealth distribution (Rodrik 2011; Spence 2011). For the first time in the post–Second World War period, growth in developing countries has outpaced that of industrialised countries; by 2010 developing countries (including former socialist countries) accounted for half of the world economy (Rodrik 2011). The 2010 OECD report interprets these dynamics as "shifting wealth" (OECD 2010) and points out that the world's economic centre of power has gradually shifted away from the OECD and towards the emerging economies. According to the report, the number of converging countries – countries with double the average per capita growth than the high-income OECD countries – more than quintupled, while the number of poor countries more than halved.[19]

While this does not mean that the gap between developing countries and industrialised countries has closed or that growth was equally distributed among developing countries, it shows a clear trend towards convergence: "[T]he huge asymmetries between advanced and developing countries have not disappeared, but they are declining, and the pattern for the first time in 250 years is convergence rather than divergence" (Spence 2011, 4). This is also confirmed by the OECD report. Acknowledging that economic growth occurred in varying degrees and with widely disparate outcomes, the report clearly states that "[t]his re-alignment of the world economy is not a transitory phenomenon, but represents a structural change of historical significance" (OECD 2010, 2).

Will this trend towards convergence continue? The OECD report is positive and estimates that the situation in 1990 – when OECD countries had a 62 per cent share of the world economy – is likely to be reversed by 2030, with developing countries' share projected to rise to 57 per cent (see Figure 2).

19 This analysis of the OECD is based on a classification that categorises the world economy into four speeds and into four groups of countries accordingly: (i) "affluent": high-income countries according to the World Bank's grouping; (ii) "converging": countries with double the GDP per capita growth of high-income OECD countries; (iii) "struggling": middle-income countries whose GDP per capita growth is less than double than that of high-income OECD countries; (iv) "poor": low-income countries whose GDP per capita growth is less than double than that of high-income OECD countries (OECD 2010, 33).

Figure 2: Share of the global economy 1990–2030



Note: These data apply Maddison's long-term growth projections to his historical PPP-based estimates for 29 OECD member countries and 129 non-member economies. Dotted lines indicate projections.
Source: OECD (2010)

Others are more cautious. They point towards previous experiences with fast economic growth that – in most developing countries – has hardly ever been sustained. Rodrik (2011), for example, expects that many countries are unlikely to sustain current growth rates and that rapid convergence is possible in theory but unlikely to happen in practice. The main reasons he identifies are the failure to promote economic diversification and to initiate structural change from low-productivity sectors (e.g. agriculture and other informal sectors) to higher-productivity sectors. In the same vein, Page (2009) refers to the expected unsustainability of current growth rates. He argues that recent growth, especially in Africa, has largely been driven by commodity booms and better macroeconomic policies; it has hardly been accompanied by increased productivity, export diversification or investment.

But even if large income disparities prevail, it is important to acknowledge that the dividing line between the "developed" and the "developing" world has become increasingly blurred and that the current development landscape is considerably different from the landscape of just one or two decades ago. Not only has the group of countries with higher per capita income averages increased steadily since the 2000s (see Section 3.2), the characteristic differences attributed to the former demarcation line between developed and developing countries have also become increasingly redundant. This relates as much to the "internal attributes of nations (political and economic systems, rates of economic growth)" as to their "external relationships" (Harris et al. 2009). In fact, many countries are now considered "intermediate" – in between the old categories of "developed" and "developing". A particular set of countries within this group combine characteristics formerly attributed to either developing or developed countries. Despite having large numbers of poor people, these countries have experienced fast economic growth and gained significant geopolitical influence. Harris et al. (2009) describe this as a mismatch of relational and income characteristics. Schmitz and Messner (2008) refer to these countries (mainly China and India) as "poor but powerful" and argue that these are increasingly distinct from other low- and middle-income countries as well as OECD countries.

Another key element of changing growth patterns is the fact that South-South economic, trade and aid flows have gained significant importance vis-à-vis North-South flows. South-South foreign direct investment (FDI) flows (largely from Brazil, China, India, South Africa and the East Asian Tigers) have risen faster than North-South flows (OECD 2010). Aid flows from non-DAC members rose by 63 per cent between 2006 and 2008, reaching a 10 per cent share of global aid flows in 2008[20] (ECOSOC 2008). Many countries that were formerly considered "aid recipients" have thus become important "donors" themselves and are currently both recipients and providers of aid (Grimm et al. 2009). These changing patterns of financial flows have important repercussions for the current aid system, making new financial opportunities available for developing countries, creating new actors on the scene and providing an increasingly diverse marketplace of ideas and approaches.

Even more important for the analysis in this paper is the fact that "shifting wealth" and the growing economic weight of anchor and emerging countries has led to geopolitical ramifications and an increasingly multi-polar world order with new demands for global decision-making. In this increasingly globalised, interconnected and multi-polar world, global challenges such as climate change and reducing CO_2 emissions; security and stability; migration; financial stability; and communicable diseases cannot be addressed without the involvement of emerging and developing countries (Zoellick 2010). As the (re-) emergence of the G20 suggests, this is not only about China and India, but increasingly about countries such as Brazil, Mexico, Indonesia, Turkey, Argentina, Russia and South Africa. The evolving international roles of these dynamic players are particularly important in the areas of global governance reform and for the provision of global public goods (GPGs). In fact, these power shifts provide an "important impetus for a new understanding of development policy as global public policy," which would shift "development interests beyond ODA and the alleviation of absolute poverty to include other instruments such as trade, technology and investment transfer, protection and valorisation of national resources in a more coherent manner" (Gleichmann / Kloke-Lesch 2010, 13) (see Section 4.2).

The challenge many donors – and in particular the EU – are now facing is to adapt their development policies to a development landscape that has become much more differentiated, heterogeneous and complex. On the one hand, many countries have seen rapid economic growth, gained significant political and regional influence and are now indispensable for global and regional problem-solving. Economically and politically, they are increasingly meeting European countries on equal terms – or have at least recognised their common interests and mutual dependence. In times of scarce ODA resources, it is being questioned more often – and rightly so – whether or not it is appropriate and

20 Non-OECD donors do not provide "aid" in the classical sense as defined by OECD/DAC criteria. The UN Economic and Social Council's calculations are therefore defined to the greatest extent possible on the same terms as OECD/DAC ODA.

legitimate to continue to provide EU aid to countries that appear wealthy enough to fund their own development.

Any rethink of this approach, however, has to consider more than just the dramatic shifts in the patterns of growth and geopolitical power shifts. Looking only at growth rates and increasing average income levels provides a rather incomplete picture of the changing development landscape. Most importantly, it overlooks social and human development and the extent to which countries have reduced poverty as they have climbed the ladder of economic development and gained influence on the global political stage. Any new strategy involving middle-income or emerging countries therefore needs to take account of another trend that has accompanied shifting patterns of wealth: the changing geography of poverty.

3.2 The changing geography of poverty

Since poverty has been considered predominantly a low-income-country problem for a long time, the decision for donors about where to prioritise assistance in order to reduce poverty was significantly less complex. Evidently, aid has always served other purposes besides poverty reduction; commercial, strategic and political reasons have been – and still are – just as decisive for aid allocations (Holden 2009; Barder 2009). But if donors prioritised poverty reduction – a paradigm that gained ground in the development community throughout the 1990s – a focus on poor countries was the logical consequence.

In 2007, Paul Collier's widely read book *The Bottom Billion* re-emphasised this focus on prioritising aid for poor countries (Collier 2007). Collier acknowledged that the world can no longer be portrayed as "5 billion poor" and "1 billion rich", so he divided the world roughly into 1-4-1: 1 billion people living in affluent, developed countries; 4 billion people living in countries experiencing rapid economic growth whose living standards are converging with those of the rich; and 1 billion poor people living in mostly fragile countries suffering from stagnating economic growth. Economic growth plays a key role in Collier's concept and the lack thereof is considered a decisive factor for these countries to be stuck in poverty: "The problem of the bottom billion has not been that they had the wrong type of growth, it is that they have not had any growth" (ibid., 11).

As pointed out before, Collier's viewpoint – to focus aid on low-income and mostly fragile countries and to phase it out for those countries in the "middle" – has been influential with a number of donors, most notably DFID,[21] which has set funding priorities and programmes accordingly. It has also reinforced the view that aid spending in MICs is perceived as aid that is poorly targeted at poverty reduction.

However, the redistribution of global growth has had important repercussions on the global geography of poverty and challenges the view that poverty is predominantly a low-income-country problem. First of all, there is the success story. The share of the population living in extreme income-poverty (below US$ 1.25 a day) fell tremendously

21 According to a 2009 DFID White Paper, half of all new bilateral funding would be allocated to fragile states. This was reconfirmed during the bilateral aid review in 2011.

between 1981 and 2008 from 52 to 22 per cent. This progress, however, has been very uneven between regions. The sharp decline in global income poverty is mainly attributed to progress in China and East and South-East Asia, while sub-Saharan Africa has only seen a modest decline in income poverty (World Bank 2012).

Moreover, not all countries that have seen fast economic growth rates over the last century have combated poverty with urgency. Many countries have become wealthier in per capita terms and crossed the middle-income threshold, while large parts of the population continue to live below the poverty line. This has now led to a situation in which the majority of extreme income-poor, or a "new bottom billion" (Sumner 2010b), live in MICs. Sumner estimates that 72 per cent of the world's income-poor[22] do not live in the poorest countries that Collier terms the "Bottom Billion" but in countries that have generated significant economic growth and crossed the MIC threshold. Of this 72 per cent, 61 per cent live in stable MICs and only 28 per cent of the world's poor live in LICs, whereas fragile low-income countries account for only 12 per cent (see Table 1).

Table 1: Distribution of the global poor in 2007/2008 by country type (%)

	Fragile and conflict-affected	Not fragile or conflict-affected	Total
Low-income	12	16	28
Middle-income	11	61	72
Total	23	77	100

Source: Sumner (2010b)

At the same time, this recent shift in the global geography of poverty has to be treated with some caution. A closer look at how this change came about reveals that it is closely related to the transition of five populous countries to MIC status: China (graduated in 1999), Indonesia (2003), India (2007), Nigeria (2008) and Pakistan (2008). If China and India are removed, the figure decreases from 72 per cent of poor people living in MICs to 22 per cent (while Nigeria, Pakistan and Indonesia account for much of the remaining 22 per cent). Yet, it is a significant increase compared to 1990, when only 9 per cent of the global poor lived in MICs (Sumner 2010b).

Sumner's findings are nonetheless relevant, in particular since they point towards an important trend in the changing nature of poverty. One of the key differences between Collier's and Sumner's findings relates to the emphasis given to inequality and poverty and income disparities within countries. Collier calculated the billion poor people by counting the total population of his 58 Bottom Billion countries and not only the countries' poor populations. Sumner, on the other hand, puts the emphasis on poor people in non-poor countries, and thus on distributional challenges within – rather than between – countries. So whereas the key challenge identified by Collier relates to how LICs can generate growth in order to reduce poverty, Sumner draws attention to the fact that many

22 The calculations of Sumner refer to absolute poverty and the US$ 1.25 poverty line using data from 2007/2008 World Development Indicators.

countries have taken off economically, while at the same time large proportions of their populations continue to live below the poverty line.

This shift has sparked a new discussion about where to focus development assistance in order to tackle global poverty. In particular, it has raised questions regarding the viability of the prevailing paradigm that aid has a strong poverty focus if it is spent exclusively in the poorest countries. The challenges of Collier's Bottom Billion – mainly badly governed, fragile and conflict-affected poor countries – have been widely documented and researched (see e.g. Chauvet / Collier 2004; Chauvet et al. 2007; Collier 2009; Torres / Anderson 2004; Duffield 2005; Picciotto 2004), as these challenges have dominated the debate on poverty reduction for the last decade. This discourse obviously remains very important, as development progress proves particularly challenging in conflict-affected countries. According to the World Bank, no fragile country has yet achieved a single MDG (World Bank 2011b).

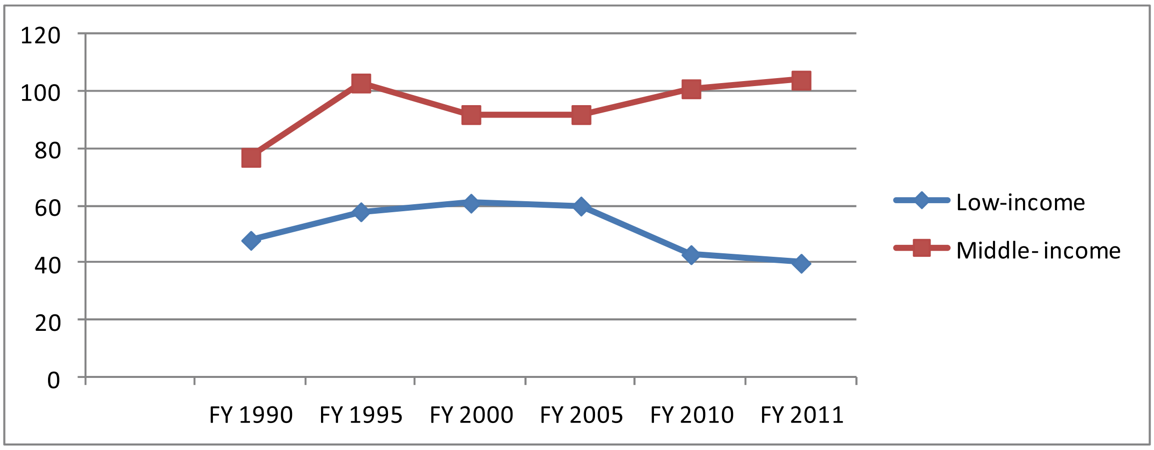
However, according to current figures, the challenges of the Bottom Billion countries apply to a decreasing number of developing countries and to a limited share of the world's poor population. Sumner (2010b) estimates that the number of poor people living in fragile and conflict-affected countries accounts for around 300 million people, a 23 per cent share of the world's poor population. Moreover, a number of countries that were considered "trapped and falling behind" at the beginning of the 2000s have generated significant economic growth in recent years. Of Collier's 58 Bottom Billion countries, 11 were considered as "converging" by the 2011 OECD report, meaning that they are currently generating GDP per capita growth rates that are twice as high as those of high-income OECD countries. The shift in global poverty – namely the people who make up the 77 per cent share of the world's poor population, who do not live in fragile or conflict-affected countries, and the 61 per cent of these who live in stable MICs – thus confronts development practitioners and researchers with new challenges and requires a fresh look on poverty and social inequality in economically thriving countries.

A key question in these discussions is therefore whether or not Sumner describes a situation that only results from the transition of five populous countries to MIC status. In other words, is the continuation of poverty and rising inequality in countries that have generated fast economic growth a trend that characterises a significant change in the poverty problem that is likely to continue in the mid-term, if not over the long-term?

Any estimation of whether or not the majority of poor people will continue to live in MICs is complex.[23] However, there are two important factors to consider. The first is to look at the extent to which we can expect the number of MICs to either rise or decrease over the next years. In 1988, there were only 77 MICs, whereas this number increased to 104 in 2009. On the contrary, while the number of LICs increased significantly during the 1990s

23 According to Kanbur / Sumner (2011) these factors include "growth projections for individual countries; assumptions on exchange rate evolution; assumptions on international inflation and other aspects of the Atlas methodology for classifying countries as LICs or MICs; the evolution of income distribution within each country; any re-evaluation of PPPs in each country (and influence on $ 1.25 poverty) and population growth in individual countries" (ibid.).

Figure 3: The increase of MICs from 1990 to 2011



Source: World Bank: http://data.worldbank.org/about/country-classifications/country-and-lending-groups#Low_income

– from 48 in 1988 to 63 in 2000 – the latest World Bank classification data indicate that this number fell to 35 in 2011.

Recent projections indicate that this trend is indeed likely to continue and that the number of LICs might continue to fall significantly. Calculating the World Bank's International Development Association[24] future client base, Moss and Leo (2011) estimate that the International Development Association will probably lose half of its client countries by 2025 because countries will become too wealthy to qualify. According to these estimates, only 31 countries will remain eligible for International Development Association assistance in 2025 and the total population covered by the lending facility will be reduced by two-thirds.

The second important factor is to look at the extent to which countries have reduced poverty as they have reached MIC status. In general, leaving distributional issues aside, countries should have made remarkable progress in reducing poverty by the time they reach MIC status. The average income threshold a country must exceed in order to be classified "middle income" by the World Bank roughly corresponds to US$ 2.70 per capita per day,[25] which is above the two commonly used income poverty lines of US$ 1.25 and $ 2 (Kanbur / Sumner 2011). Overall, findings suggest that the incidence of extreme income poverty in MICs is generally lower than in LICs.[26] Including other aspects of social and human development beyond income poverty, MICs, by and large, seem to be

24 According to Moss / Leo (2011), the International Development Association follows two objectives: (i) to provide finance to countries that cannot borrow because of low-income or lack of creditworthiness, and (ii) to help countries grow wealthier and improve their policies so that they can turn to commercial markets or the World Bank's hard window for their capital needs (ibid., 2).

25 Using 2008 exchange rates.

26 According to Sumner (2011b), the average incidence of income poverty in low-income countries for 2002–2007 is almost twice as high (52.4 per cent) as in lower-middle-income countries (27.1 per cent) and 10 times higher than in upper-middle-income countries (5.2 per cent).

better off than LICs (Sumner 2011b). This general positive correlation is also confirmed if multi-dimensional poverty is considered. According to Alkire (2010), there is an encouraging disconnect between higher average income levels per capita and the multi-dimensional poverty index (MPI).[27]

However, what those aggregate figures mask is the fact that there are tremendous differences across countries and that the group of MICs and the progress made is actually significantly more disparate than these overall findings indicate. The argument that all MICs achieve broader human development can easily be rejected by the fact that 12 LMICs are still considered least-developed countries.[28] This incongruent development progress is also reflected in the varying poverty rates of MICs. As emphasised by a recent UN report, the incidence of poverty in MICs ranges from 2 per cent to more than 60 per cent of a country's population (UNDP / UNFPA / UNOFS 2011, 3). Comparing the poverty reduction efforts of the 23 countries[29] that have achieved MIC status since 2000, it becomes obvious that there are countries that have even seen rising poverty levels as their average GNIs per capita increased (Sumner 2011b). Some countries, e.g. Botswana, have seen substantial income increases but poverty reduction rates that are falling only slowly. Others such as Ghana have translated comparatively modest economic growth into a significant decline in poverty (Fosu 2011). There are countries that continue to have higher levels of poverty than LICs, despite achieving MIC status. Zambia, for example, (which has only very recently been granted LMIC status) has a higher extreme poverty per capita ratio (64.3 per cent) than a poor LIC such as Mali (51.4 per cent).[30] And there are extreme examples such as Equatorial Guinea, a high-income country where 76.8 per cent of the population continues to live below the national poverty line.[31] Even India, which has had impressive annual GDP growth rates, has not matched its good economic performance with equally high rates of poverty reduction (Fosu 2011) and continues to account for more of the world's extreme income-poor (450 million) than the entire African continent (377 million).[32]

The relationship between growth and poverty reduction is thus more complex. While there is an overall agreement that growth is a necessary precondition for poverty reduction (Lopez 2010), the assumption that the incomes of the poor increase one-for-one if a country generates economic growth (Dollar / Kraay 2002) is difficult to sustain against the backdrop of persistent poverty in MICs. In fact, there seems to be little correlation

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27 The MPI is a new international measure that goes beyond measuring income poverty by taking into account the multi-dimensionality of poverty. It identifies overlapping deprivations that members of a household experience based on three dimensions: health, education and standard of living. A household is considered as multi-dimensionally poor if it is deprived of an equivalent of 30 per cent of the weighted indicators (Alkire / Santos 2010).

28 See: http://www.unctad.org/Templates/Page.asp?intItemID=3641&lang=1.

29 Angola (2006), Armenia (2004), Azerbaijan (2005), Bhutan (2008), Cameroon (2007), Congo (2007), Cote d'Ivoire (2010), Georgia (2005), India (2009), Indonesia (2005), Lesotho (2007), Moldova (2007), Mongolia (2009), Nicaragua (2007), Nigeria (2010), Pakistan (2010), Sao Tome and Principe (2010), Senegal (2011), Sudan (2009), Ukraine (2004), Uzbekistan (2011), Vietnam (2011), Yemen (2011).

30 Data processed from the Demographic Health Survey 2007.

31 According to World Bank data from 2006.

32 According to the Demographic Health Survey 2005.

between a country's progress towards reducing poverty and its economic growth (Lopez / Page 2003; Fosu 2009, 2011).[33] While the OECD report highlights the general positive correlation of growth and poverty reduction,[34] it explicitly states that there are tremendous differences across countries, and that countries with rapidly growing economies were not necessarily the ones to achieve the greatest poverty reductions.[35] Some countries have translated relatively strong economic growth into a significant decline in poverty, while others have generated more GDP growth but only achieved modest poverty reduction rates (Fosu 2011). The same can be said for the link between growth performance and wider social and human development. Bourguignon et al. (2008), for example, found that "the correlation between GDP per capita growth and non-income MDGs is practically zero," which led them to conclude that "these results do not invalidate the argument that growth is necessary to achieve the MDGs, for instance by generating needed budget resources, they suggest that growth alone is not enough" (ibid., 9).

Rising inequality and distributional challenges are therefore crucial in explaining the diverse outcomes related to poverty reduction. In a broad range of countries, economic growth has been accompanied by increasing inequality (OECD 2010; Lopez / Page 2003; Saith 2006). According to the OECD report, since 1990 the decrease in income inequalities between countries – due to the strong growth performance of many developing countries – has occurred at the same time that income inequalities within many countries have been steadily increasing. The Gini coefficient – the most commonly used index to measure inequality – has risen in most developing countries across all world regions except Latin America. In particular in Asia, Gini coefficients have been rising significantly during the last 20 years (e.g. by 10 percentage points in China).

This does not invalidate Collier's viewpoint that poor countries need sustained growth in order to reduce poverty. However, it reaffirms Sumner's assumption that distributional issues are as significant in characterising the poverty problem as the total lack of resources. National progress and national aggregates such as average income per capita can be misleading as entire regions and social groups have been de-linked from the positive developments in the same country.

This is also the case if multi-dimensional poverty is considered. Assessing an MPI sample of 28 countries, Rippin[36] identifies tremendous differences across regions within the same country. The Callao region in Peru, for instance, ranks third with an MPI of close to zero, while the Huancavelica and Huánuco regions rank 230 and 232, respectively, with an MPI

33 Looking in particular into the long-term relationship between economic growth and poverty reduction, Lopez / Page (2003) found that the impact of economic growth on poverty outcomes differs significantly across countries and regions. Of a sample of 54 countries, the poor failed to achieve income growth in 21 countries, and in a number of countries, long-term growth even led to increases in poverty.

34 According to the report, a 1 per cent rise in real per capita GDP is, on average, equivalent to a 1.1 per cent reduction in the absolute poverty rate (OECD 2010).

35 Taking a set of 24 countries, out of which 16 are converging countries, the report found that, by and large, the growth elasticity of poverty reduction in converging countries is rather modest compared to countries with less economic growth (OECD 2010).

36 Data not yet published by Nicole Rippin (mimeo).

of more than 0.23. LICs are no exception to unequal distribution of wealth within the same country. Nairobi in Kenya, for example, has one of the lowest MPIs (0.04), while the north-eastern region accounts for one of the highest MPIs (0.68) of the sample. India, known for its regional poverty disparities, has regions where multi-dimensional poverty is relatively low (Kerala (0.05) and Delhi (0.06)), while other regions such as Jharkhand (0.44) and Bihar (0.48) are in the bottom quintile of the sample. This challenge of widening gaps in income and social development distribution within countries is also acknowledged by Vandemoortele (2011), one of the main architects of the MDGs, who emphasises that "the world is off-track, not because of insufficient economic growth but mostly because people in the bottom quintiles have benefited disproportionately little from national progress. As long as the world continues to turn a blind eye to the growing inequities within countries, the MDGs will be mission impossible" (Vandemoortele 2011, 1).

What these findings clearly show is that poverty can no longer be seen as a problem only of LICs and that economic growth, even though important, is not a sufficient condition for countries to reduce poverty. It is therefore important to acknowledge that countries have made very uneven progress in reducing poverty as they climbed the ladder of economic development. The increase in average per capita income and the transition to middle-income status can therefore not be considered as end points to development or equated with reduced levels of poverty or higher human development.

This, of course, raises the question whether or not the EU has the right strategies to respond to this changing development landscape. The concomitance of the resulting challenges – the changing geography of growth, geopolitical ramifications and the increasingly global nature of development challenges on the one hand, and the changing nature of poverty and increasing inequities within countries on the other – further complicates the question of how to undertake development cooperation in an ever more heterogeneous and differentiated development landscape.

4 Two evolving challenges

Both shifting wealth and changing patterns of poverty have given new momentum to the debate on aid to MICs and emerging economies. The growing number of MICs; the fact that the majority of poor people currently live in MICs; geopolitical power shifts and the re-emergence of the G20; the succession of global crises; and the growing consciousness about the need to find joint solutions to global challenges have sparked new debates among scholars (Sumner 2010a, 2011a; Kanbur / Sumner 2011; Glennie 2011; van Lieshout et al. 2010) and donors (DGM 2011; DFID 2011; BMZ 2011).

On the one hand, the changing geography of poverty has provoked a new discussion on the rationale of aid in tackling national development challenges and supporting poverty reduction efforts in countries that have surpassed a certain income threshold. On the other, the trend and need to expand the objectives of development policy beyond poverty reduction and the classical "aid relationship" has increased markedly due to the frequency and intensity of the global crisis and the continuing trend of global interdependencies and challenges (Faust / Messner 2012; van Lieshout et al. 2010). This has also caused an increasing number of EU and non-EU donors to seek new partnerships and forms of cooperation with MICs and emerging economies that reflect the mutual responsibility for global development.[37]

The remainder of this section tackles (the debate around) these challenges and proceeds as follows. In a first step, it analyses those challenges that arise even if donors decide to adopt a narrow definition of development policy, namely the need to understand the poverty problem and capacities of a country beyond its average income and to adapt aid allocations or cut-offs accordingly. In a second step, it analyses the trend towards a broad definition of development policy and the implications for development cooperation with influential MICs in the context of global challenges.

4.1 Poor countries or poor people?

The question whether MICs should continue to receive aid is given renewed urgency in light of the persistent pockets of poverty that exist in these countries and the fact that the transition to MIC status cannot necessarily be equated with reduced levels of poverty.

So far, the dominant thinking in the aid literature has considered aid to MICs as aid poorly targeted at poverty reduction. Accordingly, it was advocated to assess the poverty focus of donors' aid programmes against their spending in poor countries (Dollar / Pritchett 1998; Collier / Dollar 2002; Dollar / Levin 2004). This is echoed in the aid allocation literature that says two criteria need to be considered for poverty-efficient aid allocations: first, the "neediness" of countries, which reflects the principle that countries with higher levels of poverty should receive more aid; second, the country's institutional environment, which embodies the evidence that countries with sound institutional performance are more likely to make effective use of aid (Svensson 1999; Kosack 2003; Burnside / Dollar 2004). What has followed from the generally applied model is the view that aid should primarily be allocated to poor countries with relatively "good" political institutions.

Until recently, there has been considerably less debate on whether donors should focus on average per capita income or on the absolute numbers of poor people in assessing the

37 The new strategy of French development cooperation, adopted in 2011, centres around the need to better manage globalisation processes as it becomes clear that the benefits of globalisation are accompanied by a lack of global governance and collective action. The focus is therefore put on moving beyond development assistance and asymmetrical donor-beneficiary relationships towards global co-responsibility. In this context, four objectives are adopted: sustainable shared growth; the fight against poverty and inequality; the preservation of global public goods; and stability and the rule of law. Part of this new strategy is the formulation of differentiated partnerships and a new approach towards emerging economies on the basis of managing global balances (DGM 2011). Recognising that the importance of global challenges other than poverty reduction has increased in recent years, Switzerland has also adopted a wider set of strategic objectives. The new direction for Swiss development policy, adopted in 2008, includes human security and development-promoting globalisation as being objectives on equal footing (Lammers 2011). After a change of government in 2009, BMZ published a new "concept for development cooperation" with "global development partners" in 2011, which builds on the initial anchor country concepts in many ways. In its new strategy, BMZ identified three areas for strategic engagement with these partners: mitigating climate change and preserving the environment; promoting sustainable economic development; and shaping global development agendas.

neediness of a country, as both categories were given almost equal weight: “Aid is widely believed to have greater development impact where it is needed most – that is, where there are large numbers of poor people […]” (Knack et al. 2010, 6). Even though some donors started to include criteria other than average income to measure the needs of a country (e.g. the Human Development Index), for the majority of donor agencies, the World Bank’s country classifications continued to be a key determinant for the types and levels of development assistance. Since poverty – from a development policy point of view – has for a long time been considered predominantly a problem of poor countries, the focus on GDP per capita and poor countries was considerably less problematic. However, against the backdrop of changing patterns of poverty, a particular challenge emerged on how to best assess the neediness of a developing country. Both categories – average per capita income and total amount of poor people – are now increasingly used as two distinct categories. Barder (2009), for example, describes this as a trade-off that donors face in their efforts to reduce poverty: either help as many people as possible out of poverty or target the poorest countries. Kanbur and Sumner (2011) use the term “poor countries or poor people?” in their analysis about whether MICs should continue to receive aid.

Among scholars, two general lines of argumentation seem to have evolved as a response to this evolving trade-off. The first is closely related to Collier’s work on the Bottom Billion and calls on donors to concentrate aid to support poverty reduction in the poorest countries. While persistent poverty in MICs is acknowledged in this line of argumentation, it is argued that these countries have the resources and the capacities to resolve the poverty problem on their own and that “the international community basically doesn’t have a role in the MICs.”[38] In contrast, others argue that in order to maximise global poverty reduction, donors need to focus on poor people instead of poor countries and therefore continue to support MICs in their poverty reduction efforts (Eyben et al. 2004; Alonso et al. 2007; Kanbur 2010; Kanbur / Sumner 2011). In this latter view, of the heterogeneous group of MICs, many countries are still in need of financial and technical support from donors in order to overcome widespread poverty.

Deciding for one of these strategies also poses a challenge for donors, who are still coming to terms with the implications of this evolving trade-off. In its recent bilateral and multilateral aid review, DFID appears to have moved away from its focus on poor countries by stating that “aid will have the most impact on poverty reduction if it is spent in countries with large numbers of poor people and low human development indicators […] ” (DFID 2011, 26). It is also argued that “a country with higher numbers of poor people will need more aid than one with lower numbers of poor people” (ibid., 133). Accordingly, three out of the top five countries of the first quartile – where, according to DFID’s model, aid will have the most impact on poverty reduction – are LMICs (i.e. India, Nigeria and Pakistan), with China and Indonesia following on ranks in the first quartile. On the other hand, the review does not follow this line in a coherent manner and assesses and criticises the poverty focus of multilateral organisations based on their “focus on poor countries” (ibid., 9).

38 Stated by Paul Collier in 2010 in an interview with IDS; see: http://www.mixcloud.com/ids/paul-collier-and-andy-sumner-in-discussion-on-the-ids-paper-the-new-bottom-billion/.

This example shows quite well the challenges that both categories present for reconceptualising poverty-efficient aid allocations. Both categories (poor people and poor countries) have specific shortcomings. Focussing on income as the key determinant for the needs of a country and for selective aid allocations overlooks the fact that national aggregates – and in particular national per capita income – have become insufficient criteria for assessing the poverty levels and development challenges of a country. The advantage of average per capita income is that it allows, to a certain extent, for the accounting of the financial and redistribution capacities of a given country. Prioritising the total amount of poor people allows for capturing the poverty problem of a country, but fails to include the country's own poverty reduction capacity – in particular the financial and domestic redistribution capacities. It furthermore discriminates against smaller developing countries, where the incidence of poverty and other human development indicators may be high, but the absolute numbers of poor people are low compared to populous countries such as India, China and Indonesia. Prioritising a focus on poor people could easily lead to an undesirable selection of MICs that are sufficiently able to tackle poverty without international support; it could also lead to disadvantaging smaller MICs that continue to experience high incidences of poverty and below-average human development.

The argument made in this paper is thus to move from a focus on either "poor countries or poor people" towards a multi-dimensional view of developing countries that better captures the heterogeneity of MICs and the varying development challenges they face. When the World Bank originally created its country classification system, it intended to set income thresholds that allowed for the creation of a link between a country's economic and social development: "The process of setting per capita income thresholds started with finding a stable relationship between a summary measure of well-being such as poverty incidence and infant mortality on the one hand and economic variables including per capita GNI estimated based on the Bank's Atlas method on the other."[39] However, given the non-linear relationship between economic growth, poverty reduction and other human development indicators, the resulting classification system is currently grouping together countries where such a stable relationship does not necessarily exist.

Moreover, the classification system does not adequately reflect the nature of development challenges and the varying degrees to which the passing of the (rather arbitrary) income threshold was accompanied by a reduction of poverty, structural change and effective institution-building. For instance, in the group of LMICs, there are countries such as Sudan, Iraq and Timor-Leste, where issues of fragility, state-building and security are among the primary concerns for overcoming widespread poverty. There are countries such as India and Indonesia – both consolidated democracies and members of the G20 – where inclusive growth across all regions and cultural groupings remains challenging. And there are countries such as Ghana and Zambia, where commodity-based economic growth needs to be followed by economic diversification. In these latter types of countries, the process of building up effective institutions that are able to design and implement pro-poor policies has yet to keep pace with rapid economic growth. The same problem

39 See: http://data.worldbank.org/about/country-classifications/a-short-history.

constellations apply to upper-middle-income countries. There are countries on the upper third of the income range (US$ 3,976 to $ 12,275), such as Uruguay and Chile, whose main challenge is to consolidate economic progress and to catch up with the group of high-income OECD countries. Then there are countries in the bottom third, such as Ecuador, Peru, Botswana and Namibia, where high levels of poverty and inequality remain key development challenges.

Grouping these countries under one term fails to recognise these various development challenges. An adequate response to the changing geography of poverty thus requires a more nuanced view towards developing countries' needs and capacities and moving beyond GDP per capita as the single determining factor to group countries and to decide on aid cut-offs. This is also echoed by the UN General Assembly's resolution of 2009 on development cooperation with MICs that highlighted the disparateness of MICs: "national averages based on criteria such as per capita income do not always reflect the actual particularities and development needs of the middle income countries" (UN 2009, 1).

Donors are understandably disinclined to provide aid to countries that have sufficient capacity to tackle their poverty problem without international assistance. To get a more differentiated picture of these countries, it is thus important to develop a country classification system that carefully balances a country's needs against its own capacities in order to better distinguish between countries that can wipe out absolute poverty based on own resources and institutional capacities and those that cannot. Given the shortcomings of both categories (poor countries and poor people) in adequately assessing the neediness of a developing country, a more suitable approach would be to focus on the incidence of poverty and other non-income development indicators, while including a special focus on income inequality. Since these indicators do not allow capturing a country's own potential for supporting its populations without development aid, it is important to balance these needs against a country's (i) financial capacity (its redistribution capacity as well as its access to external private capital) and (ii) its institutional environment.

Including a specific focus on the financial capacity of countries is important to counter two specific risks. The first is that too much aid goes to wealthier countries that are sufficiently able to tackle poverty without financial assistance (DFID 2005). The second is the overgeneralisation that MICs – even if they meet the "neediness criteria" due to high incidence of poverty and large amounts of poor people – by and large have sufficient domestic (and external private capital) resources available and only need to redistribute funds more efficiently.

Regarding the redistribution capacity of developing countries, a study of Ravallion (2009) is of particular interest. Based on the assumption that governments in donor countries are disinclined to provide aid to a country that has sufficient internal capacity to tackle poverty through redistribution, Ravallion (2009) estimates this internal redistribution capacity for 90 countries.[40] Calculating the marginal tax rate needed (income tax rate on

40 The capacity for redistribution is measured by the marginal tax rate (on those who are not poor, by rich-country standards) that is needed to cover the poverty gap or to provide a poverty-level basic income, judged by developing-country standards.

individuals who are not poor by US standards) to cover the poverty gap for the US$ 1.25 as well as the US$ 2 line, Ravallion concludes that, in general, alleviating poverty through redistribution is more feasible in MICs. However, a more nuanced view reveals that this is by far not applicable to all countries. Taking the examples of China, India and Brazil, Ravallion finds that the capacity for redistribution is considerably more constrained in India than in China or, in particular, in Brazil. But even in China, the tax rate needed to address the US$ 2 poverty gap would require a prohibitive rate of 100 per cent. The same holds true for countries such as Vietnam, Pakistan and Nigeria, where for both poverty lines, prohibitively high tax rates of 100 per cent would be required.[41]

Beyond taxing individuals, governments obviously have alternative taxation instruments and other sources of non-tax revenues as well as access to international financial markets, which could provide them with sufficient revenues to implement redistributive policies in order to alleviate poverty. Altenburg (2010) therefore argues that donors should carefully assess whether or not a country is able to tackle its poverty problem without international support by using its own resources or through access to bonds on the international capital market. Therefore, it is important to carefully assess a country's financing gap for effectively eradicating income poverty and not to simply assume that MIC status is a sufficient proxy for such a calculation. This is echoed by Sumner (2011a), who calls for a new aid allocation model based on a formula that takes into account "the needs to end poverty", "the potentially available domestic and global resources" as well as the "commitment to poverty reduction" and the "capacity for poverty reduction".

In addition to assessing the financing capacity, the institutional capacity and quality of public services need to receive particular attention. In general, one could expect that MICs have greater institutional capacities than their poorer counterparts and that rising average income levels have been accompanied by a strengthening of a country's institutional performance and public service delivery (Dollar / Pritchett 1998; World Bank Independent Evaluation Group 2007). The heterogeneity of MICs, however, is also reflected in the varying levels of institutional capacity and the varying degrees to which economic growth has been accompanied by structural change and institutional capacity-building. Achieving MIC status based on a development-oriented strategy requires a certain level of institutional capacity-building. However, given that many MICs have experienced resource-based growth, the transition to MIC status has in many cases not been accompanied by a strengthening of the country's institutional performance, nor by an improvement in the inclusiveness of governance systems or the accountability of governments to its citizens. Effective institutions, however, are a key prerequisite for a country's capacity to design and implement pro-poor policies.

The main challenge in many MICs might not be an absolute lack of capital but rather overcoming social inequalities and designing pro-poor and redistribution policies in order

41 However, what Ravallion (2009) also finds is that economic growth does have a direct effect on a country's redistribution capacity. At a certain point, when a country has experienced "sufficient economic growth" (ibid., 20), the tax rates required to fill the poverty gap start to drop significantly. According to his calculations, this refers to countries with roughly more than US$ 4,000 in consumption per capita per year.

to spend available resources to benefit the poor population. In addition to assessing the financial capacity of MICs, it is thus also important to focus on the extent to which economic growth has been accompanied by institutional capacity development, which enables a country to effectively manage policy reforms. Donors can play a crucial role in this regard, not merely by providing cash, but by providing support to institutional reform processes and by designing and supporting the implementation of pro-poor growth policies. This is also reflected in the "Consensus on development cooperation with MICs", which resulted from UN conferences in Madrid and El Salvador in 2007: "[T]he development of middle-income countries is hindered by disparities existing within them; redressing such disparities is the primary responsibility of their governments with the support of bilateral and multilateral cooperation donors, which represents an important component of their development."

Getting involved in internal development and redistribution processes might prove to be a difficult political endeavour. Ravallion (2009) rightly recommends not only assessing the redistribution capacity but also the redistributive efforts of governments, which, to a large extent, depend on political will. In addition to assessing the financing and institutional capacities of countries, it is equally important to focus on the development-orientation and commitment of a recipient government. Mechanisms such as policy dialogue with the respective partner country government and support for civil society organisations are crucial in this respect. A focus on institution-building, however, is equally important, since the political will of a government is at least partly determined by a country's political institutions, which work as different kinds of incentives for economic redistribution (e.g. Olsen 2000; Blaydes / Kayser 2011).

Finally, any decision to continue or discontinue the provision of aid needs to consider the extent to which concerned countries are interested in an ongoing aid relationship. When their economies continue to grow, many MICs do not favour a continuation of or an increase in aid, largely due to the demands and conditionality that accompany its provision (Eyben et al. 2004; Sumner 2011b). Taking these arguments together, one can see that the question of whether donors should focus their support on poor countries or poor people is less clear-cut and requires a better understanding of the nature of a country's development challenges and its internal capacity to tackle these without international assistance.

Thinking about global poverty reduction is currently in a transition phase – future concepts have yet to be developed to meet the challenges of changing patterns of poverty. Poverty in poor and especially fragile countries will remain on the agenda and continue to pose a particular challenge for the development community (see e.g. Kharas / Rogerson 2012). Nonetheless, the sharp reduction in the number of LICs and the fact that the graduation process has in many cases been accompanied by stagnating poverty levels and increasing inequality requires a better understanding of the specific characteristics and development challenges of the countries "in the middle". It also requires donors to rethink their poverty reduction strategies and policies (Carbonnier / Sumner 2012). An important contribution to addressing this challenging task is to conceptualise and group countries differently in order to derive a better understanding about when donors can still (potentially) contribute to a country's poverty reduction efforts and when it is time for a country to graduate from aid. Such a multi-dimensional approach towards country classifications would go beyond economic development and include factors that provide a more accurate picture of a country's social and political development. Proposals for different country classifications are already underway, for instance with regard to the internal and external capacities of countries (e.g. Harris et al. 2009) or with regard to a multi-dimensional approach towards fragile states (Grävingholt et al. 2012). However, given the dominant, widespread practice of classifying countries according to GDP per capita, more research and efforts are needed to further develop such classifications and to establish them among development researchers and practitioners.[42]

4.2 A global rationale for development policy

While it is important not to exclude countries from development assistance on the basis of their average income, it is important to acknowledge that global development challenges beyond poverty reduction have increased in importance. In the late 1990s, the UNDP's seminal work on global public goods[43] highlighted that minimising the negative consequences of globalisation requires the adequate provision of GPGs, "concerted cross-border public policy action" (Kaul et al. 1999, 3) and a new paradigm for international cooperation (Kaul et al. 1999). Such a global approach to development acknowledges that major global challenges such as climate change, food insecurity, financial instability, communicable diseases, migration, conflict and insecurity have increased along with accelerating globalisation and are problems that not only potentially affect us all but that also require interventions beyond the national level. The concept of GPGs has become one of the key themes in international cooperation and created discussions among donor agencies from the outset (see Chapter 2). Yet, there are two main factors that distinguish the current discourse on a GPG approach to development from earlier discussions. The first relates to the extent to which the concept is supported and implemented by European development agencies and the corresponding changing nature and purpose of aid. The second relates to the focus and interest that is attributed to GPGs from a development policy perspective and the increasingly blurring lines between "developing country interests" and "EU interests".

Over recent years, the extent to which European donors support and embrace a GPG approach to development and a broad definition of development policy has increased markedly. Initially, when the concept started to be widely discussed in international

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42 As part of the research process of this paper, the author presented previous versions at academic conferences and in public discussions. While the issue of aid to MICs continues to be a controversial topic for discussion, there was a wide consensus among all discussants that the problem with the MIC category is that everybody agrees that it is increasingly ill-suited, but that everybody – including development researchers – keep using it. Classifying countries differently thus also includes overcoming path dependency.

43 According to Kaul et al. (1999): "A global public good is a public good with benefits that are strongly universal in terms of countries (covering more than one group of countries), people (accruing to several, preferably all, population groups), and generations (extending to both current and future generations, or at least meeting the needs of the current generation without foreclosing development options for future generations)" (ibid., 2).

forums[44] in the early 2000s, some donors subscribed to this new global approach to development (e.g. France, Sweden and Germany) while others (e.g. the United Kingdom) contested it. Critics of the approach were concerned that the concept of GPGs was too fuzzy, that it would divert scarce resources away from original development purposes and that it would weaken the poverty focus of development policy (Carbone 2007). However, against the backdrop of intensifying globalisation, frequent global crises and a steadily growing range of global challenges, the current trend among European donors[45] points towards a global outlook on development (Lammers 2010) and "a new 'grand purpose' for development policy: managing global interdependencies in a globalized world" (Severino / Ray 2009, 5).

This diversification of development policy and the increasingly complex set of objectives are also reflected in the changing nature of aid. During the last decade, the amount of aid allocated to GPGs has increased steadily. Whereas estimates on the exact share of aid financing for GPGs vary – largely due to different definitions used for GPGs – they all point towards a marked increase of aid that is directed to finance the provision of GPGs (te Velde et al. 2006; Cepparulo / Giuriato 2009). Shafik (2011) expects aid to become the "key catalyst for financing global problem solving" (ibid., 4) and to increasingly serve two distinct purposes: poverty reduction and the provision of GPGs. Blending aid resources for poverty reduction with the financing for GPGs, however, remains contested. Kaul (1999, 2010) has repeatedly called for financing ODA and GPGs separately, mainly to ensure that aid is not directed away from poverty reduction. Severino / Ray (2009), on the other hand, propose to combine both types of financing and to move from ODA to "Global Policy Finance" (ibid., 22) to better reflect the changing paradigm of development policy. Whatever view one takes in these debates, the current practice of categorising GPG-related expenditures as ODA implies that aid is currently being used to address both national and global development challenges.

The trend of orientating development policy towards global challenges has also been accompanied by a changing focus and interest that can be attributed to the provision of GPGs – from a one-sided focus on developing countries' interests to an emphasis on mutual interests in tackling global challenges. From a development policy perspective, the initial approach taken was that the provision of GPGs is essential for development and reductions in poverty. Linking poverty reduction with the provision of GPGs is an acknowledgement that global challenges and policies – for example mitigating climate change and reducing carbon dioxide emissions; regulating the financial sector; preventing

44 For example at the 2002 Financing for Development conference held in Monterrey in March 2002 or the 2002 World Summit on Sustainable Development in Johannesburg.

45 DFID is a somewhat special case in these discussions. On the one hand, the department continues to emphasise the primacy of poverty reduction in its development programmes. Yet, at the same time, DFID has set up a Global Partnerships Department to contribute towards shaping global development policies and working with emerging economies towards global outcomes; see: http://www.dfid.gov.uk/Documents/publications1/op/glob-parts-dept-2011.pdf. Moreover, in a recent speech on future cooperation with emerging economies, the UK's International Development Secretary, Andrew Mitchell, clearly stated that "[t]he really big strategic issues […] don't readily lend themselves to single country solutions"; see: http://www.dfid.gov.uk/News/Speeches-and-statements/2011/Emerging-powers/.

and controlling communicable diseases; and designing a favourable and development-conducive trade regime – pose challenges for poverty reduction that need to be addressed beyond the local and national levels. Following this line, the World Bank, for example, defined GPGs as:

> *"…commodities, resources, services and systems of rules or policy regimes with substantial cross-border externalities that are important for development and poverty-reduction, and that can be produced in sufficient supply only through cooperation and collective action by developed and developing countries"* (World Bank 2005, 2).

Development policy thus shifted towards a multi-layered approach, whereby its focus (theoretically) continued to represent the interests of developing countries as well as to work towards coherent external policies that do not undermine the objectives of development policy. This approach is also reflected in the German re-orientation of development policy from the end of the 1990s and the first definition given for global structural policy in the coalition treaty of 1998: "Today development policy is global structural policy, which aims to improve the social, ecologic and political conditions in developing countries."

This one-sided emphasis of a developing country's interests in a GPG approach to development has moved successively towards the notion of mutual interests or "collective self-interests" (Kaul 2010). The concomitance of global economic and political power shifts and a relative loss of importance of the EU and OECD countries vis-à-vis emerging countries on the one hand, and escalating global crises and the growing challenge to provide GPGs on the other, have now led to a situation in which development-related GPGs shape EU and OECD external relations. Addressing global systemic risks such as an increasingly fragile ecosystem, resource scarcity, unsustainable fossil-fuelled economic growth and the regulation of global financial and trade flows is not only in the interest of the EU and other industrialised countries. Finding solutions to these challenges ultimately depends on the development paths of emerging economies and other increasingly powerful developing countries and the interests they represent in global governance processes. The future challenge in cooperating with developing and emerging countries therefore lies in balancing European interests with those of partner countries and developing joint and mutual interests (Faust / Messner 2012). This shift can also be seen in BMZ's latest definition given for global structural policy: "Development policy is global structural policy. It promotes global public goods such as climate change, preserving environmental resources and security."[46]

How is this related to the question of continuing or discontinuing development cooperation with seemingly "better off" countries? As Altenburg (2010) argues, the principles that guide development policy are decisive for whether or not development cooperation with MICs and emerging economies is still appropriate. A broad definition of development policy and a GPG approach to development – with an emphasis on mutual and joint interests – requires continued EU engagement with emerging economies and other

46 See: http://www.bmz.de/en/what_we_do/principles/aims/index.html.

increasingly powerful developing countries. Consequently, the rise of anchor countries and emerging economies; their growing economic and political weight and increasingly important role in regional and global governance processes; as well as their systemic importance in the provision of GPGs has also led to a growing need among European development agencies to cooperate with these countries:

> *"In trying to deal with global problems and challenges, the governments of richer countries will be obliged to work in a highly networked mode with other (newly) powerful agents, often with the aim of changing the rules of political and economic games. The cooperation of a range of influential countries from among the ranks of the former "developing countries" will be essential, partly because they are increasingly the source of some problems (e.g. climate change), partly because it will be difficult to change international rules without their cooperation, and partly because they exercise influence of various kinds over smaller, poorer neighbouring countries"* (Harris et al. 2009, 25).

However, a continuation of such development cooperation should not be confused with a continuation of aid programmes in the way they have been implemented from a traditional development perspective. Achieving the MDGs and addressing widespread poverty in poor countries across the world requires different EU development approaches from those that address the development priorities of anchor countries or emerging economies such as China, Brazil, India, South Africa and Indonesia. Significant changes are required at the levels of objectives and with regards to inter-ministerial and inter-departmental coordination at the EU level.

4.3 The interrelatedness of poverty reduction and global challenges

Adopting a global outlook on development acknowledges that global challenges beyond poverty reduction have increased in importance and that development policy can make significant contributions to support the adequate provision of GPGs. On the level of objectives, one could therefore argue that development cooperation with emerging economies and anchor countries should focus mainly on regional and global development challenges and neglect national development challenges (Stamm 2004). Whereas the diversification of objectives is strategically important and necessary to address complex GPG challenges, national development challenges and poverty reduction still play an important role in a GPG approach to development. From a global governance perspective, EU development policy should continue to be concerned with a recipient country's internal development challenges as a strategically important element for cooperative global governance. The focus given to poverty reduction, however, changes from a GPG perspective. Whereas during the Cold War aid was mainly used to serve geopolitical interests, during the 1990s it started to be driven by a "compassionate ethic" (Severino / Ray 2009, 7). The poverty reduction focus that donors adopted at that time was (rhetorically) justified on moral grounds in order to help developing countries improve the living conditions of their citizens. A GPG approach to poverty reduction, on the other hand, emphasises industrialised countries' own interests in fighting global poverty, as it leads to defusing global problems created by poverty:

> *"The means which the governments of rich countries use to approach the "traditional" development problem of mass poverty in poor countries will become increasingly intertwined with the instruments they employ to deal with a range of other concerns over how, in an increasingly globalised world, problems left untreated in poor countries and regions can impact adversely on the richer world, through global warming, illicit migration, narcotics production, terrorism, piracy, epidemic disease etc".* (Harris et al. 2009, 25).

This is also acknowledged by the French Directorate-General for Development and Cooperation, which stresses that "from the public goods perspective, we help the poor because we need them to supply the environmental, agricultural, economic, etc. goods and services they alone are capable of supplying, and which benefit all of us, at the national, regional and global levels" (DGM 2011, 17). There is one additional point that illustrates the interrelatedness between poverty reduction and GPG challenges: if the global community fails to address issues such as climate change, food security, financial stability and a development-conducive international trade regime, it is likely to adversely affect the development progress of countries and threaten further economic and social progress.

Therefore, the challenge of poverty reduction and the provision of GPGs cannot be considered separately. If anchor or emerging countries continue to have vast pockets of poverty, donors should be concerned, not mainly due to reasons of solidarity but to prevent national systemic risks from spilling over into a country's respective regions or from developing into global systemic risks. In many country contexts, the boundaries between different policy objectives are not, and cannot be, as clearly separated as in the past.

This blurring of objectives not only occurs at the individual country level. The adequate provision of GPGs requires controlling risks at the country level that have the potential to develop into global systemic risks, but it ultimately requires effective and cooperative global governance. Many important global governance fora or agreements – or stalemates – such as the WTO Doha Round or the Kyoto Protocol and subsequent climate agreements, suffer from diverging interests and fears over unequally distributed costs and benefits. Building on the liberal school of foreign policy analysis, Conzelmann / Faust (2009) argue that these lines of conflict cannot exclusively be attributed to an increasingly redundant "North-South" divide. Additionally, domestic conditions such as the varying socio-economic transformation pressures within a given country or the type of political regime heavily impact how countries engage in global governance processes: how cooperative they are, the strategies they adopt and the interests they represent. These domestic conditions often tend to create cooperation-adverse environments in non-OECD countries. In most developing countries, and even in the most powerful emerging economies, domestic political processes often tend to concentrate on ensuring basic material needs and on redistribution challenges that arise in the wake of rapid economic and political transformation (Chaudhuri / Ravallion 2006).

The significant role of domestic politics in shaping international cooperation has always been on the agenda of scholars engaged in international relations and foreign policy analysis (e.g. Putnam 1988; Moravcsik 1997). This interrelatedness is also reflected in a recent analysis of the EU's Strategic Partnerships.[47] Assessing the EU's strategic partnership with China, Grevi and Khandekar (2011) conclude that different domestic conditions and priorities have so far impeded the development of shared interests and more substantial cooperation at the global level: "As a developing nation, the priorities of China are different from those of a largely post-industrial society like Europe. […] The alleged EU-China strategic axis will remain elusive as long as both sides fail to address their internal problems" (Grevi / Khandekar 2011, 17). The same is found for the EU's strategic partnership with India, where a "mismatch of priorities" has so far prevented the identification of mutual interests: "The EU's priorities towards India are trade, security, energy and climate change […]. India on the other hand seeks in the EU a partner for sustainable agriculture, development, commerce and a source of technology transfer to maintain its growth" (ibid., 21).

While it is important to adopt a more complex set of strategic objectives with anchor countries and emerging economies and to support these countries in providing specific GPGs, it is equally important to acknowledge that national and global challenges are inextricably linked. Identifying and working towards mutual and joint interests could require the EU to continue offering support to tackle countries' poverty problems and internal development challenges, to ease the socio-economic transformation pressures and to accompany the countries on a sustainable development path. This is also in line with the approaches of other European donor agencies. The new concepts of BMZ, DFID and the French Directorate-General for Development and Cooperation, for example, all highlight the need to continue working *in* these countries to tackle national development challenges while working *with* these countries to achieve global development outcomes. Such multi-layered support, however, ultimately depends on the extent to which recipient countries are interested in the EU's engagement with domestic affairs.

Apart from poverty reduction objectives, the question of aid to MICs needs to be analysed within a GPG approach to development and a diversification of the EU's strategic objectives with anchor and emerging countries and other increasingly influential developing countries. In general, the financial dimension of development cooperation will lessen in importance as private capital flows increase, whereas knowledge-transfer and technical cooperation will gain in importance. Yet, financial transfers still seem justified if used in a targeted and effective manner. Compared to private capital flows, donors can allocate financial resources in a targeted way and ideally catalyse or accelerate individual measures and incentivise institutional and political reforms (Stamm 2004). The use of financial transfers can also be an important lever to support the provision of a specific GPG, as funding is often – though not always – necessary for their provision. Since the current practice allows for counting most GPG-related funding as ODA, it means that the

47 The EU maintains strategic partnerships with a rather heterogeneous group of 10 countries. Half of these (Brazil, China, India, South Africa and Mexico) have gained importance in global governance processes and are part of the G20, while at the same time qualifying for ODA eligibility according to OECD/DAC rules. Strategic Partnerships in general aim to provide a framework to engage with these countries on a wide range of policy areas (e.g. trade, environmental issues and development). However, the overall strategic orientation of the EU's Strategic Partnerships remains unclear (Gratius 2011).

nature and purpose of aid changes, while funding levels might decrease only slightly or even remain unchanged.

Moreover, addressing complex GPG challenges and managing the interface between global and internal development challenges requires new forms of cooperation with anchor countries and emerging economies, but also ultimately necessitates cross-ministerial and cross-departmental cooperation. This imperative for more coordination and joint action is an overlooked factor in discussions at the EU level about how to best engage with emerging global players. Unlike traditional North-South development cooperation, which is implemented by development ministries in a niche approach that is often decoupled from other foreign and internal policies, regulating a globalised world and implementing effective policies for the provision of GPGs cannot be accomplished by development agencies alone. A broad definition of development policy also implies that the interfaces between different political responsibilities become larger and that the demand for inter-ministerial or inter-departmental coordination increases significantly. The areas in which the EU needs to cooperate with non-OECD countries have increased significantly with the growing range of global challenges. Securing GPGs and identifying mutual and joint global interests blur the lines between traditional development policy (representing the interests of developing countries) and foreign policy (representing national interests) (Faust / Messner 2012). In addition, many emerging countries increasingly attract the interest of other sectoral Directorates-General (e.g. trade, climate, environment, energy), as many departments have discovered their interest in these countries and internationalised their work areas in the course of globalisation. Managing these interfaces will become more important as the difficulties in distinguishing between the competences and responsibilities of different Directorates-General increase. The newly created European External Action Service has a special role to play in this respect, given its mandate to ensure more coherent EU external policies and to coordinate the EU's foreign policy interests with development objectives. In addition to primary foreign and security interests, the European External Action Service needs to take on the challenge to ensure a coherent EU-wide approach towards the provision of GPGs and to align different EU external policies behind this common objective (see also Duke / Blockmans 2010; Furness 2010). Moreover, avoiding a fragmented and incoherent EU approach to GPGs also implies that a development-related GPG strategy with emerging and anchor countries has the support of other Directorates-General in order to ensure a coherent and institution-wide EU strategy towards these countries.

5 Implications for EU development policy

The changing development landscape and the need for greater differentiation require substantial changes in EU development policy. The adaptation of objectives and a more differentiated approach towards partner countries are key challenges in ongoing efforts to modernise EU development policy. Putting the question of development cooperation with MICs in the context of a changing geography of poverty and the need to think of development as a global endeavour reveals the conceptual challenges inherent to this question. This last section will outline some of these challenges and focuses not only on the EU's role as an additional bilateral European donor but in particular on its specific role for ensuring complementarity, coordination and coherence across European donor practices and policies. In this light, it emphasises the substantial coordination challenges the EU is facing in ensuring a coherent GPG approach and a strategically consistent engagement with anchor and emerging countries.

Poverty reduction will undoubtedly remain the primary concern and policy objective for EU development policy, reaffirmed by legal provisions in the Lisbon Treaty. However, against the backdrop of a more differentiated development landscape and significant economic development in many partner countries, the question about when countries graduate from EU aid aimed at poverty reduction has become increasingly relevant. In working towards global poverty reduction, the EU will have to differentiate between countries where EU aid can still have an impact and those that are – even without continued development assistance – sufficiently able to overcome their internal development challenges. One way of concentrating the EU's development assistance would be to focus on a decreasing number of poor countries. Such an approach, however, fails to acknowledge that the challenge of global poverty reduction has changed and that national income has become an insufficient criterion to capture the poverty problem and development challenges of a country. Therefore, one challenge for the EU relates to finding better "technical" solutions to classify countries and to avoid a reliance on classifications that only reflect a country's economic development. According to the analysis in this paper,[48] such a classification system would have to combine a number of categories to better reflect a country's social and political development and to better capture the increasing complexity of the developing world. In essence, this would require creating groupings of countries with similar characteristics and development challenges rather than solely relying on a country's increase in average income. Such country classifications would provide the EU with a basis to apply a more differentiated approach that is based on specific problem constellations of partner countries.

A second challenge relates to the political dimension and the question of cross-country division of labour among European donors. The process of selecting partner countries is still considered a national prerogative by European bilateral donors and is insufficiently coordinated at the EU level, despite the Code of Conduct on Complementarity and Division of Labour adopted in 2007. So far, the concerns over such an uncoordinated approach have related to an uneven cross-country distribution of aid, resulting in "aid darlings" (countries that attract a number of EU donors and where the level of ODA per capita is relatively high) and "aid orphans" (low-income and often fragile countries where only a limited number of EU donors are present and where ODA levels per capita are low). The European Consensus (Art. 48) and the Code of Conduct have assigned the EU with the role of compensating for such an uneven distribution of funds. At present, however, this is mainly related to looking after aid orphans and fragile countries where the conditions are considered too difficult and too risky by many member states to implement

48 The need for classifying countries beyond average income is also increasingly being called for in the development research community; see:http://www.policyinnovations.org/ideas/innovations/data/000208.

aid programmes. The EU's global presence has been considered a comparative strategic advantage. In particular, it has ensured a European presence in all developing countries, since the EU is not just focussed on economically or strategically attractive countries, or on those where the institutional environments allow for (potentially) achieving development results.

Any discussion on the EU's reduction or cutting of aid to certain countries is therefore also a discussion about the role and comparative advantage of the EU vis-à-vis member states' development policies and partner country selection. As a supranational actor, the EU is confronted with diverging interests of individual member states (or like-minded groupings of member states) and the different expectations they articulate towards the EU. Such articulation of interests often reflects an understanding of complementarity, which is in many cases characterised by member states' attempts to align the EU closer to their own national development policy guidelines and to seek the EU's support in specific countries or regions. Much of the criticism about the EU's above-average funding in MICs, for example, comes from the United Kingdom, whereas Spain has repeatedly expressed its concern that the EU minimises its development engagement with MICs in Latin America, where Spain continues to have close ties due to its colonial history. Any discussion on a potential cutting of aid or a move away from focussing on a country's internal development challenges also needs to include a discussion on the comparative advantage and global presence of the EU: Is the EU the so-called donor of last resort, meaning that it maintains a global presence to ensure EU support to countries where member states decide to withdraw their assistance? Or is the EU an actor that should have more focus, move more closely to the profile of a 28th bilateral European donor and closely align its policies and partner country portfolio to those of member states?

A complementary approach at the EU level also needs to include a perspective to better coordinate cross-country division of labour among European donors. If the EU applied similar income cut-offs as member states (in most cases upper-middle-income status), without including a more holistic view towards country-specific development challenges (poverty and human development, social inequality, institutional and financial capacities), it could result in marginalising seemingly better-off countries that continue to experience serious internal development challenges. In many Latin American countries that have grown richer in per capita terms but continue to experience significant development challenges, the EU is already one of the few European donors left (Morazán et al. 2012).

Therefore, any approach to global poverty reduction and partner country selection should not be decided by member states or by the EU individually. Rather, it should be accompanied by a joint strategy and division of labour towards countries where it is not the absolute lack of resources that constitutes the main challenge, but rather where the EU and member states can make an important contribution in the areas of governance, public sector reform, setting up effective taxation systems and promoting domestic accountability. Such coordinated and concerted actions would also avoid an over-concentration of EU donors and funds on a decreasing number of poor countries, while MICs are increasingly being left alone in their fight against poverty and social exclusion. In view of the increasing number of MICs and the varying degrees to which economic growth has so far been accompanied by reduced levels of poverty – and the fact that attempts to reduce global poverty will increasingly have to deal with inequality and distributional challenges within countries that have become wealthier in per capita terms – the need for such a joint approach has become ever more relevant.

Developing a coordinated EU approach to address the new geography of poverty requires making necessary changes within the existing narrow definition of EU development policy. A second far-reaching policy challenge for the EU is to address the mismatch between its partner country portfolio and its development objectives. Against the backdrop of multiple global challenges and the strategically important role of the developing world in securing global commons, a narrow definition of development policy and an exclusive focus on poverty reduction will be increasingly difficult to sustain. On the contrary, due to its global presence, the EU is ideally placed to adopt a broad definition and a global rationale of development policy. This means that – in cooperating with anchor and emerging countries and other strategically important countries for the provision of GPGs – the EU will have to target a portfolio of strategic objectives instead of a single objective (Gavas et al. 2011).

More than ever, this requires the EU to break up the traditional structures of an asymmetric donor-recipient relationship. Moving towards mutual interests requires the EU to reconcile European interests with those of influential partner countries, to identify GPGs of joint strategic interest and to identify European contributions to a country's development path. Given the interrelatedness of internal development challenges on the one hand and cooperative governance on the other, the key challenge for the EU will be to find the correct balance in addressing poverty reduction objectives and internal development challenges while promoting strategic objectives that are in the mutual interest of the EU and partner countries.

When a traditional development agency that is mostly concerned about poverty reduction and a country's internal development challenges moves towards a global rationale of development, this substantially increases the coordination challenges, both at the EU institution level and between the EU and its member states. At the member state level, the trend towards a global approach to development has so far not been accompanied by subscribing to a common EU development strategy for addressing GPG challenges and jointly engaging with strategically important partner countries for this purpose (Furness / Makhan 2011). Given the declining influence and manoeuvring space of EU donor agencies in these countries, a move towards joint and coordinated approaches could increase the weight and potential leverage of the EU's development programme significantly. This, however, would have to entail that member states and the EU align and coordinate their strategic engagements with emerging economies and that they make distinct choices about where their joint global priorities lie. Such a process might prove to be challenging, since it requires reconciling mutual and joint European interests with the national interests that member states pursue through their bilateral aid programmes.

At the EU institution level, it requires the EU to redefine the role of development policy vis-à-vis other policy fields. Foreign policy, economic and trade policy, finance and investment policy, environmental and climate change policy, migration, technology transfer and research policies have gained importance in the EU's relations with rapidly emerging countries and require EU development policy to effectively manage the linkages with these policy areas (Makhan et al. 2012). Ideally, a GPG approach to development would be integrated in an overarching and joint EU strategy for the provision of GPGs and the EU's engagement with emerging economies. So far, however, the EU has not adopted a joint global strategy on how to best engage with anchor countries and emerging economies to this end. While in general, Strategic Partnerships aim to provide a framework to engage with these countries on a wide range of policy areas (e.g. trade, environmental issues and development), the EU has not yet identified its main interests and objectives for these partnerships or chosen the strategic partners needed to achieve them accordingly (Gratius 2011). Unlike the anchor country concept, which is based on a systematic selection of countries with a particular importance for the provision of GPGs and global governance processes, the overall strategic orientation of the EU's Strategic Partnerships remains unclear. Herman van Rompuy, President of the European Council, publicly admitted: "[W]e have strategic partners, now we need a strategy."[49] This relates as much to the selection of strategic partners as to the content and overall joint objective of these.

An EU-wide approach to the provision of GPGs thus has to go beyond the realm of development policy and integrate other policy fields and ambitions behind a common objective. For this purpose, the establishment of a new EU strategy for how to work – from a development perspective – with emerging global players needs to be aligned to other policy fields and closely coordinated at the EU level and with member states' global strategies. Given the complex institutional and policy set-ups of the EU, this will be no easy task. Competences over policies with specific importance to the provision of GPGs vary significantly: some are exclusive to the Commission (e.g. economic and monetary policy, trade and agriculture), some are shared competences (development, climate change and environmental policies), while foreign and security policy remains in the domain of member states. Establishing an EU-wide approach to GPGs is therefore likely to include conflict over competences and thematic responsibilities – a conflict that cannot be solved by individual departments or policy fields. Addressing these will require strategic decisions in the highest political forums of the EU.

Managing global interdependencies and securing the adequate provision of GPGs pose far-reaching challenges for the EU. Adopting a global rationale for development policy and reorganising the EU's development cooperation with anchor countries and emerging economies are necessary and important steps. They need to be accompanied, however, by a strategic debate among the EU and its member states about how best to jointly tackle global challenges, leading to clear decisions about how to align relevant policies – in addition to development policy – with this common global strategy. Moreover, implementing their own strategic direction to secure GPGs will require the EU and member states to negotiate and reconcile European interests, norms and values with those of strategically important partner countries. A development approach to mutual interests –

as much as any other external policy of the EU – needs to make sure that the EU's interests are compatible with those of partner countries. A shift towards mutual global interests, therefore, needs to be accompanied by a thorough understanding of the partner country's interests, its internal and external policy priorities, and its expectations towards the EU.

Moving towards a more differentiated approach between partner countries is a challenge that will remain relevant beyond the actual political negotiations around the EU's next multi-annual financial framework. On the member state level, it is relevant when individual member states decide on their partner country portfolio and when they make strategic choices on how to engage with emerging economies and other powerful developing countries. On the EU level, it will remain relevant once the next phase of country programming begins in 2014 and, most importantly, when negotiations on the future of the Cotonou Agreement and the group of African, Caribbean and Pacific countries kick off. Then, at the latest, the EU should have a coherent concept of how to address the challenges of global poverty reduction, how to organise a European division of labour for this purpose and how to jointly address global challenges.

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