Department for International Development

UK aid from the British people

Economic development for shared prosperity and poverty reduction: a strategic framework

Summary

Economic development is key to eradicating poverty. Accelerating progress is essential if the goal of zero extreme poverty by 2030 is to be achieved. The evidence is clear that this will require much higher growth rates in many countries, more inclusive growth – in particular for girls and women, and actions to tackle the structural barriers that deny poor people the chance to raise their incomes and find jobs.

The UK government can do more to help partner governments address the causes as well as the symptoms of poverty. This involves putting in place the building blocks that are crucial for countries to exit poverty: peace, the rule of law, property rights, stable business conditions, and honest and responsive governments, accountable to their citizens.

The Department for International Development's (DFID) economic development strategic framework highlights the importance of the institutions that encourage private investment and export growth: free and fair markets; sound macroeconomic management; clear and consistently applied policies, regulations and laws; secure property rights; and functioning commercial courts.

The private sector is the engine of growth. Successful businesses drive growth, create jobs and pay the taxes that finance services and investment. Foreign investment, and particularly exports, can accelerate domestic development. Governments have a role in encouraging responsible investment, and helping markets work better for poor people. This requires a focus on the long term, to ensure the measures we support now are aligned with the actions of the more forward-looking governments and responsible investors we want to partner with.

DFID has a growing economic development portfolio, with around a fifth of spend and substantial staff resources focused on this area. The portfolio is delivered through bilateral programmes, through our support to and engagement with multilateral development banks and other partners, and increasingly through working directly with businesses. DFID also makes wider investments in human development, improved governance, action on climate change, and humanitarian response, all of which are vital for sustained economic growth. But the potential for further action on economic development is significant.

Ten months on from the Secretary of State for International Development's decision to ramp up DFID's work on economic development, this document summarises DFID's strategic framework to deliver on this priority.

The framework has five pillars where we will increase our work:

1) Improving international rules for shared prosperity;
2) Supporting the enabling environment for private sector growth;
3) Catalysing capital flows and trade in frontier markets;
4) Engaging with businesses to help their investments contribute to development; and,
5) Ensuring growth is inclusive, and benefits girls and women.

Alongside current programming and use of existing financial instruments, DFID is working more closely with the private sector, making more use of loans and equity investments as well as grant aid, and exploring ways to harness UK expertise to enhance the impact of our aid. CDC, the UK's Development Finance Institution (DFI), and the Private Infrastructure Development Group (PIDG) will remain key instruments, with which we will explore new forms of support.

Whilst DFID leads on international development, the Foreign & Commonwealth Office (FCO), UK Trade & Investment (UKTI), Department for Business, Innovation & Skills (BIS), HM Treasury (HMT), Her Majesty's Revenue and Customs (HMRC), Department of Energy and Climate Change (DECC) and Department for Food & Rural Affairs (Defra) all play a role in promoting related UK interests overseas. We will work more closely together to ensure a coherent UK government approach to economic development which effectively brings to bear the potential UK business can contribute to economic development. UK aid will remain untied, but we will join up UK efforts where we can simultaneously promote poverty reduction and UK growth. Making developing countries better places in which to do business can benefit both local and international firms. The countries that we can help graduate from aid are the emerging markets of the future, which will help drive UK export growth and global prosperity.

To deliver on this priority, DFID is scaling up financial and staff resources. By 2015/16, we plan to target £1.8 billion of our budget on economic development, more than doubling the amount spent in 2012/13. This is on top of indirect funding through some of our core contributions to multilateral organisations. We have doubled the number of private sector development advisers over the past two years, bringing new skills and ways of working to all parts of the organisation. We are recruiting a new Director-General for Economic Development to help drive forward our scale-up and manage our growing investment. We have restructured parts of the Department to improve our coherence and learning.

Chapter 1 of this document sets out the vision and rationale for our work on economic development. Chapters 2 and 3 outline our objectives and how we propose to deliver them. Chapter 4 highlights new instruments and implications for our resourcing, management and results measurement. Chapter 5 sets out some next steps.

Chapter 1: Vision and rationale

Our vision for economic development

The UK government's vision is to eradicate poverty and transform economies by helping poorer countries achieve a secure, self-financed, timely exit from poverty through economic development.

To achieve our vision, growth and economic development must be core to the work we do. No country has been able to eradicate poverty without economic growth, and no country will graduate from aid without it.

Economic development takes place when a country achieves long term, high rates of economic growth *and* when this growth is accompanied by a wider economic transformation that benefits the poor and shares prosperity broadly.

Economic growth is vital for creating productive jobs and increasing the tax revenues that help developing countries fund their own services. Supporting the transformation of economies ensures that we are not only helping the poor where we find them, but generating a sustained transition out of poverty that creates new and long term opportunities for improved incomes.

Achieving our vision will require:

i) **High and sustained growth rates.** The number of people living in poverty has been falling since 1980, largely driven by sustained growth in developing country economies. However current rates of growth are not high enough to meet the zero poverty target that the UK government believes should be at the heart of the post-MDG (Millennium Development Goals) framework.

ii) Policies and investments that encourage inclusive, broad-based economic growth and are founded on sustainable use of natural resources. Growth is sustained in the long term by supporting inclusive political and economic institutions, and through responsible management of natural resources and managing dangerous climate change. Revenues from assets that will run out should be invested well, and renewable resources used sustainably.

iii) Removal of the structural barriers that stop individuals benefiting from economic development and keep people in persistent poverty. High rates of inequality and vulnerability reduce the impact of growth on poverty reduction, and lock some women and men out of opportunity. Poor people need economic development policies that directly target extreme poverty and discrimination, especially that faced by girls and women.

Our focus on economic development will include activities under five pillars, which together provide a coherent framework for supporting the main drivers to inclusive and sustained economic growth:

(1) Improving international rules for shared prosperity;
(2) Supporting the enabling environment for private sector growth;
(3) Catalysing capital flows and trade in frontier markets;
(4) Engaging with businesses to help their investments contribute to development; and,
(5) Ensuring growth is inclusive, and benefits girls and women.

Countries need private investment to grow. Economic development objectives can only be achieved through harnessing the technical, managerial and financial capabilities that lie in the private sector. At the same time, investment needs to be responsible, and meet social, environmental and corporate governance standards.

Private investment and job creation need governments to put in place the building blocks for economic development, and create the policy, legal, regulatory and institutional environment for markets to work and businesses to grow. Clear and consistently applied rules help to reduce the risks and costs of doing business, in turn encouraging higher rates of entrepreneurship and investment.

Poverty is still predominantly a rural phenomenon. However, wealth creation and poverty reduction will rely in the long term on the majority of the rural poor finding livelihoods outside of agriculture. This will require sustained growth in job-creating manufacturing and services, over time.

Central to the success of economic development in poor countries is the growth and diversity of exports. Exports need to be broadened beyond a few core export products to tap into new markets, and to strengthen a country's resilience to changes in global prices.

Promoting economic development supports growth, which creates jobs and prosperity for poor people, generates taxes for investment by developing country governments, and is also good for the UK and the wider global economy. Growth in developing countries, including low income countries, is building the markets of the future for trade and investment.

UK exports to developing countries are already growing at more than twice the rate of exports to high income countries, and have generated an additional $48 billion of export business for UK firms since 1990. Since 2000, UK exports to sub-Saharan Africa have more than doubled. Frontier markets will become increasingly important for UK trade. UK companies also have a particular contribution to make to development, with high levels of technical expertise and innovation. They are often at the forefront of good global corporate governance, and are covered by the UK

Bribery Act (2010). The UK government used the G8 in 2013 to improve transparency in beneficial ownership.

The strategic framework

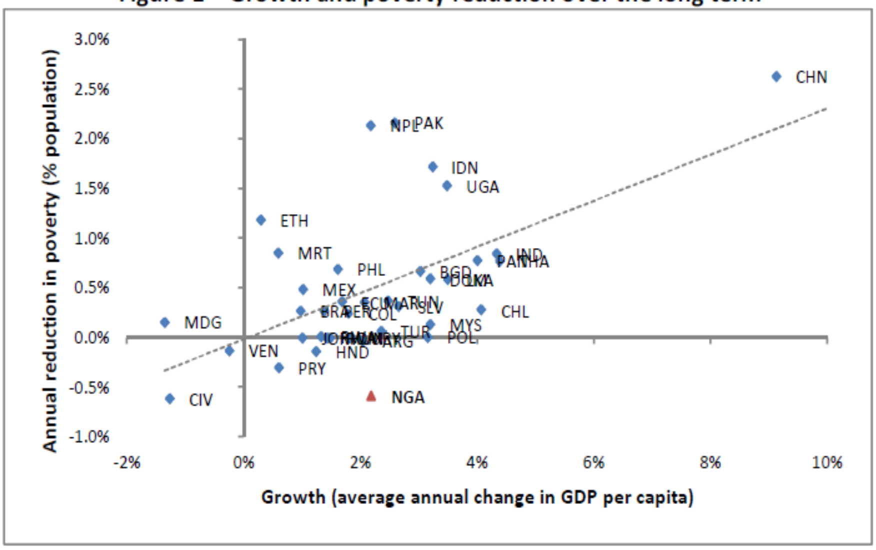
This economic development strategic framework is part of a broader shift to delivering longer-term, transformational and sustainable institutional change – as well as shorter-term, more immediate results which benefit poor people now.

Economic development requires progress on many fronts. At its core is: (1) *an inclusive growth environment* – ensuring institutions, resources and infrastructure create the environment for private investment bringing stable, robust growth, and; (2) *a growth transmission mechanism* – ensuring that growth is generated in sectors that can generate quality jobs and transform the economy.

DFID's approach to growth and economic development: The evidence base

Economic growth is the main driver of long term poverty reduction and shared prosperity. The evidence is clear. While the number of people living in absolute poverty has been falling since 1980, further reductions will be highly linked to maintaining or improving current rates of economic growth. Poverty reduction is determined by lots of factors, and is very context-specific. But high growth rates are associated with fast poverty reduction (see figure 1), and poverty has always fallen where long term per capita growth has exceeded 3%. Conversely, negative long term per capita growth is associated with stagnating or increasing poverty.

Figure 1 – Growth and poverty reduction over the long term



Source: DFID calculations based on data from World Bank WDI and IMF World Economic Outlook

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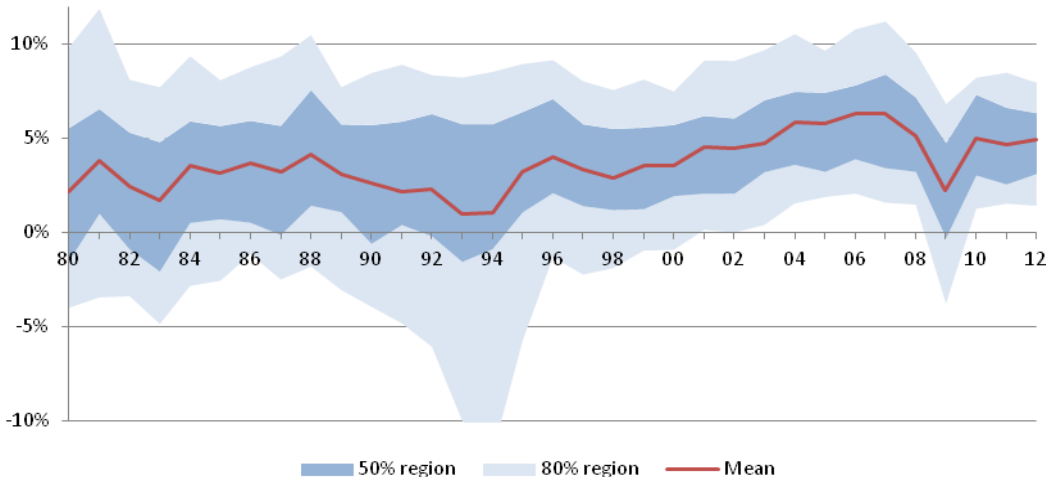
Both China and India have had impressive reductions in poverty – mostly driven by growth and economic development. In China, since 1981 poverty ($1.25 per day) fell from 84% to 12% in 2009. In India, since 1983 poverty ($1.25 per day) fell from 55% to 32.7% in 2010. At the same time we have seen high average per capita growth rates and dramatic economic development. China has averaged almost 10% per capita growth rates over the last 30 years and India has averaged more than 4%.

Over the last decade, growth in poor countries has accelerated and become less volatile. But it still remains far below the levels required for a transformation out of poverty. Average rates of low income country growth have risen from around 3% in the 1980s and 1990s to nearly 5% in the recent decade (see figure 2 below). Growth rates have been less prone to contractions, despite the impact of the global financial crisis from 2008 to 2009.

Figure 2 - The distribution of LIC/LMIC country growth rates 1980-2012



Source: IMF World Economic Outlook database, April 2012. Distribution of growth rates for all countries classified as Low Income Country/Low Middle Income Country by World Bank in 2000.

However, recent poor country growth has been dominated by economies rich in natural resources, which make up half of high growth countries. Much of this growth has been driven by higher commodity prices – in large part by increasing demand from BRIC economies (Brazil, Russia, India and China).

Growth will be more sustainable and have a greater impact on poverty reduction if countries: (1) maximise the development benefits of their natural resources; (2) support economic growth that extends beyond a single sector of low-productivity; (3) ensure it is inclusive of all segments of society; (4) effectively manage their natural resources; and (5) put the building blocks in place to minimise the impact of shocks such as global financial instability, conflict and climate change. In addition, the long term prospects for growth in both developed and developing countries will be undermined if climate change is not addressed. We will help countries better understand and manage potential risks, to ensure these do not act as a barrier to diversification and development.

DFID's growth policy is heavily influenced by the Commission on Growth and Development (2008). The Commission analysed the determinants of long term periods of poverty reduction and shared prosperity. Its report defines 'high sustained growth' as growth in excess of 7% per year sustained over 25 years. Such growth nearly doubles the size of the economy every decade. The report found only 13 countries where this had been achieved in the post-war period.

The report concluded that growth is highly context-specific and will require different actions at different times. It highlighted that whilst growth is not an end in itself, it enables governments through taxation to achieve other important objectives, including improvements in education and health care services.

Five characteristics were identified which high sustained growth countries had in common. These countries: (1) were linked into the world economy, through an openness to the global economy and ability to export; (2) maintained macroeconomic stability (low inflation, low debt and exchange rate stability and sound fiscal and financial management); (3) achieved high rates of saving for public investment in key areas such as infrastructure and education; (4) allowed markets to allocate resources; and (5) had committed, credible, and capable governments.

Increasingly evidence suggests that in order for growth to have the largest effect on sustained poverty reduction, donors should be focusing on:

- Job-intensive activities and sectors
- Export sectors (goods and services) to create deep and durable markets
- Diversification of economies to create inclusive growth
- The institutional and political arrangements that facilitate growth
- Better management of natural assets in the long term interests of the population, and limiting the effects of economic and climate shocks

Evidence from consultations with business confirms the importance of economic development. In March 2013, 28 FTSE 100 company chief executives wrote to the Financial Times in support of the UK's aid spending, recognising that the developing countries of today can become the engines of future growth and prosperity. Business perceptions matter and help shape investment decisions. World Bank enterprise surveys conducted in over 100 countries show that the most important constraints voiced by businesses are fairly consistent across countries: (i) regulations, particularly related to taxation, business registration, competition and licensing; (ii) corruption – frequently fostered by unclear and inconsistently applied laws and regulations which can increase investor uncertainty; (iii) access to affordable and reliable infrastructure, especially power; (iv) access to finance; and, (v) skills shortages, particularly for larger enterprises.

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DFID's approach to growth and economic development: an evolving agenda

DFID's Structural Reform Plan, introduced in 2011 in line with the Coalition Agreement, set clear priorities to boost wealth creation – making British international development policy more focused on economic growth.

DFID has been skilling up to engage better with domestic and international businesses. DFID created a Private Sector Department in 2011 and has scaled up its private sector skills through recruiting more experts, and more systematic learning and professional development. We have expanded the use of instruments to leverage private finance, for example through PIDG and other partnerships. CDC has undergone significant reform to focus it more on DFID priorities. Aid for trade programmes have been established and expanded.

The Secretary of State for International Development has scaled up DFID efforts on wealth creation and wider economic development. In February 2013, in her speech '*Development in Transition'*, she called for *DFID to focus more on delivering one of the top priorities for poor people – jobs*. This set the basis for increasing DFID's focus on economic development.

"… we've got to look more strategically in DFID at how we can drive the economic growth that leads to job creation. How can we build on the work that has already been started, but still probably forms a comparatively small element of what we do as a department?"
Justine Greening, speech hosted by ONE, 7 February 2013

In March 2013, the Secretary of State highlighted in her speech *'Investing in growth: How DFID works in new and emerging markets'* several areas that play a critical role in driving economic development and where DFID should scale up efforts. She stressed the importance of international trade and reducing trade barriers, of unlocking the ability of the domestic private sector to grow and the need for greater investment. She highlighted the role that UK businesses can play in the development effort, and the opportunities for innovative financing to support our approach.

In January 2014, the Secretary of State outlined in her speech '*Smart aid: Why it's all about jobs*' some of the recent changes in DFID to scale up efforts on economic development. She highlighted new initiatives and partnerships as part of a longer-term ambition to deliver world-class economic development programmes, and set out her next steps for DFID and the wider development community.

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The UK's role in a changing context

The context of poverty, its geography, and the future prospects of the poor have been changing rapidly in recent years. Poverty will increasingly become concentrated in fragile states over the next 20 years, and much poverty will remain in countries that have reached middle income status.

Also changing is the way that development is financed. Poor countries have more choice in who they engage with on development. Countries are increasingly raising their own resources, domestically and internationally. Foreign investment, new sources of funding and remittance flows are becoming increasingly important in low income countries. But the financing required to achieve an exit from poverty still remains substantial for many poor countries, and aid remains vital for some. DFID is changing to ensure we can respond to countries' changing needs and circumstances.

The UK government already has a comparative advantage in supporting key areas of economic development. This comes from strong country presence, a diverse choice of instruments and willingness to innovate, influence over the multilaterals and, increasingly, new relationships with businesses. In other areas, for example the direct financing of public infrastructure, the multilateral development banks and others are well placed to respond.

International investor interest in the markets of tomorrow is increasing. This offers opportunities for the UK government to encourage businesses, including UK businesses, to increase their activities in frontier markets in ways that support growth and development. The UK government works to improve rules and institutions for investment and shared prosperity, including rules on trade, the international financial infrastructure, transparency in contracts and taxation. DFID engages with businesses to enhance the development impact of their investments through programmes, advice and policy dialogue, and facilitating networking.

The UK has world-leading expertise in many of the areas that facilitate economic development in our partner countries. This includes British expertise from other government institutions and professional associations. Sharing UK expertise, including from FCO, UKTI, BIS, HMT, HMRC, DECC and Defra, and strengthening working across government can maximise the wider UK contribution.

Chapter 2: Economic development objectives

The overall objective of DFID's work on economic development is to reduce poverty and increase prosperity by creating jobs and increasing incomes through the promotion of high, sustainable and inclusive growth.

All our economic development activities will be rooted in country need. Our activity will vary from country to country, depending on context. In the most fragile places, our support may be more focussed on state-building, creating the conditions for growth and addressing significant barriers to investment, such as political risk, low skills and weak markets.

Pillar 1 – Improving international rules for shared prosperity

The international system shapes the framework and rules for how developing countries participate in the global economy. DFID tries to make the international system works for poor countries. We push for reforms that support their integration into the global economy, and promote the inclusion of marginalised groups such as girls and women. We work internationally to:

a) **Support an open international trading system –** making it easier for least developed countries to compete in global markets. We will continue to press for progress on the World Trade Organisation (WTO) multilateral agenda, and use our influence to achieve positive outcomes for developing countries. On EU trade policy, we want the rapid conclusion of development-friendly Economic Partnership Agreements, in particular with Africa.

b) **Influence the post-MDG framework –** to reflect the High Level Panel aspirations for economic transformation through productive jobs and inclusive growth, by working through the United Nations (UN) Open Working Group process.

c) **Secure G8 commitments on tax, transparency and trade –** which underpin economic development. This includes international tax reforms, implementation of internationally agreed guidelines to promote good business practice and protect land tenure rights, and increasing transparency and accountability in the extractives sector. We will, for example, support the G20 Development Working Group to tackle issues such as tax avoidance and tax evasion, and work through the G8 and G20, as well as with individual countries, to encourage others to adopt common global standards on extractives transparency.

d) **Ensure global financial regulation supports development in low income countries –** we will use our influence to ensure that the global regulatory environment enables developing country policy-makers to promote access to formal financial services for poor people. The UK, for example, co-chairs the G20 Global Partnership for Financial Inclusion sub-group on regulation and standard-setting, which works with global standard-setting bodies to secure international rules on financial regulation that take account of developing country needs and circumstances.

e) **Help protect partner countries against financial and other shocks –** working with the International Monetary Fund (IMF) to ensure support is available to stabilise poor countries when financial shocks arise. We will also support global action to protect against food price volatility, and strengthen food security by working to improve the functioning of food markets and investment in agricultural sectors.

Pillar 2 – Supporting the enabling environment for private sector growth

Economic growth is driven by the incentives for firms to invest. The incentives are low where the costs and risks of doing business are high. DFID will help to accelerate economic development by working with partner countries to become better places in which to do business, for both domestic and international companies, large and small. Our work will focus on promoting:

a) **Stable macroeconomic environments conducive to growth –** working with finance ministries and institutions in priority countries, and with HMT and other institutions, to help build capacity and support policy reform, including in areas such as debt management. For example, policy dialogue in Sierra Leone and support to reform programmes have helped to improve public debt management that has contributed to lower inflation and is increasing space for the private sector to access affordable finance. It has also increased revenue collection, and strengthened policies to ensure a sustainable fiscal position.

b) **Open and inclusive economic institutions** – supporting reforms to simplify red tape, promote competition, strengthen security of land and other property rights, improve access to commercial justice and strengthen the functioning of institutions charged with regulating markets and maintaining professional standards. Central to this is improved governance of economic development. For example, through support to improving the investment climate in Bangladesh, DFID has helped to reduce the number of days it takes to register a business from 57 to three.

c) **Better conditions for infrastructure investment –** supporting improved power and transport sector policies in partner countries to address constraints that deter much needed investment in infrastructure.

d) **Tax policy and tax administration reforms –** tax laws need to be clear, and consistently and equitably applied. Strong tax authorities are needed to raise much needed domestic revenue. DFID will, with Her Majesty's Revenue and

Customs (HMRC) and others, continue to provide technical assistance to revenue authorities to help improve their tax administration. For example, a new unit established within HMRC is providing technical expertise to support capacity building of tax administration in partner countries. The unit will initially deliver tax programmes in Southern Africa, Tanzania, Ethiopia and Pakistan.

e) **Trade policy –** and related reforms that reduce the costs incurred by business and increase the added value of exports. DFID provides support to trade ministries and agencies to strengthen the technical knowledge and capacity of partner countries to implement reforms. The Africa Free Trade Initiative, for example, brings together regional trade initiatives from across DFID, BIS and the FCO to improve trading conditions in Africa, and is taking concrete steps to streamline cross-border bureaucracy and modernise customs and revenue procedures.

f) **Financial sector reforms –** that improve access to and the efficiency of financial service markets, including savings, loans, money transfer and insurance services. For example, we will provide technical assistance to developing country governments and regulators through the multi-donor Financial Sector Reform and Strengthening Initiative to improve financial sector stability, efficiency and inclusiveness.

g) **Integration of the effects of climate change and the value of natural capital into economic decision-making**, which will allow countries to plan for sustainable growth. We will encourage the development of national accounts which include the value of natural resources, including ecosystems. We will focus on the opportunities of less resource intensive growth – especially where there are market opportunities that companies and developing countries can exploit, including in renewable energy.

Pillar 3 – Catalysing capital flows and trade in frontier markets

Trade and investment contribute to economic development by raising productivity, creating jobs and boosting incomes. Inadequate infrastructure, shallow financial sectors and weak capital markets present major barriers to trade and investment. Our approach is to use a range of support and financial mechanisms to:

a) **Increase private investment into poor countries, regions and sectors, with a focus on high growth sectors to support economic transformation.** CDC, the UK's Development Finance Institution (DFI) is our principal mechanism for leveraging private sector investment. We will also foster growth of new investment markets that enable economic development, such as impact investing, and support the development of markets which strengthen the conditions for investment in frontier markets, for example through insurance.

b) **Develop financial sectors, including improving and developing capital markets that allocate capital efficiently to growing businesses, large and**

small. We will support financial institutions in partner countries to build essential market infrastructure, and extend commercial lending to small businesses through technical assistance and risk sharing. Through our support to the Global Small and Medium Enterprise (SME) Financial Initiative, for example, we have helped to raise additional funds and unblock commercial lending to small businesses from 25 banks in poor countries. We will support and help facilitate greater use of technology to address financial market infrastructure constraints, including access to finance. We will also support the development of local capital markets to catalyse investment, for example by enabling finance professionals and regulators in sub-Saharan Africa to access world class training. Following the Secretary of State's visit to Tanzania in November 2013, senior Tanzanian finance professionals received training from the London Stock Exchange Group Academy.

c) **Improve the provision of infrastructure that is critical for growth and trade.** DFID works to increase private sector investment in infrastructure from both international and domestic investors. Increasing the provision of power and transport infrastructure helps reduce a critical barrier for business. The Private Infrastructure Development Group (PIDG) is the most important vehicle for DFID in supporting this aim. We will also provide support for better project preparation, which is vital for bringing in private finance. We will do this through mechanisms such as the EU-Africa Infrastructure Trust Fund, the Public Private Infrastructure Advisory Facility, and country level technical assistance programmes.

Pillar 4 – Engaging with businesses to help their investments contribute to development

Engaging with businesses, both small and large, domestic and international, presents significant opportunities for supporting economic development. Investment from multinationals overtook development aid in 2000. What they buy today accounts for 25% of production worldwide. This creates major opportunities for developing country economies and communities. DFID will work with businesses to maximise their development footprint. Through our engagement we will:

a) **Encourage and support businesses to invest more, and responsibly, in poor countries as part of their core business strategy.** We will help companies looking to invest in frontier markets, by providing information and advice on market opportunities and conditions, through support for programmes such as the International Finance Corporation (IFC) Foreign Investment Advisory Services. We will also push for businesses to be more accountable to the people whose lives are affected by their decisions. We will, for example, provide support for the adoption of responsible business practices, such as results tracking and transparent reporting, setting up strategic partnerships with companies.

b) **Promote business investment in upgrading supply chains to benefit the poor as part of their core business strategy.** Our work will focus on encouraging the private sector to build more resilient supply chains, including sourcing from firms in poor countries, and to improve working conditions for poor workers. We are creating partnerships with business through programmes such as the new Trade in Global Value Chains Initiative. This is working with businesses to improve the skills, health and working conditions of workers and smallholder farmers.

c) **Support domestic businesses to grow and strengthen their productivity and capabilities so they can compete in regional and global markets.** We will work with local firms in developing countries to build their capacity to comply with standards and rules, and facilitate firms' integration into higher value chains in goods and services that will generate more growth and jobs.

d) **Support businesses to innovate to develop better solutions to development challenges.** We will support business innovation in products and services for the poor, and pilot new initiatives that make innovative use of technology and the expertise of non-traditional partners. For example, our new 'AMPLIFY' programme will use an open, on-line innovation platform to crowd-in solutions to development challenges from around the world, and enable innovators to work closely with end-users to design products and services that meet their needs.

e) **Encourage businesses to apply better standards in their work.** We will continue to promote responsible business practices by supporting partner governments to get the right legislation and institutions in place. We will support a range of other initiatives to drive better standards, including voluntary standards systems and alliances of businesses and other interest groups.

f) **Involve domestic and international businesses in policy debates on economic growth and development.** We are improving how we involve business in policy and programming, through more regular and systematic dialogue. We are entering into new strategic partnerships such as the alliance established at the 2013 G8 Nutrition for Growth summit, the recently signed partnership with the London Stock Exchange Group to support capital market development in East Africa, and work with Unilever on a range of sectors including water, sanitation and hygiene.

Pillar 5 – Ensuring growth is inclusive, and benefits girls and women.

Marginalised groups face specific structural barriers and are often over-represented among the extreme poor. They can include girls and women, ethnic and religious minorities, young and elderly people, conflict-affected populations, people with disabilities and geographically disadvantaged groups. Policies are needed that share the benefits of growth and directly target extreme poverty and discrimination, to ensure that these specific groups are not left behind. We will focus on the following specific actions, and also ensure that this approach is integrated across the other four pillars:

a) **Improving access of poor people to markets,** as producers, consumers, employees and entrepreneurs. This includes support for better infrastructure, such as rural electricity and feeder roads, improving access to market information, and supporting innovative business models that target the very poor. In the Middle East, for example, we will be scaling up support to link women entrepreneurs to new markets through the Arab Women's Enterprise Fund.

b) **Improving access to finance for both poor women and men**, helping them to generate and protect their own wealth. This includes working with both policy makers and financial institutions to support improved access to financial services, especially secure savings and affordable loans, and measures to increase financial literacy. Our Poorest State Inclusive Programme in India, for example, is reaching 12 million poor people with better financial services, three quarters of whom are women.

c) **Improving access to land and property markets for both poor women and men**, working with government agencies and community organisations to increase awareness of these rights, and addressing the laws and social norms that prevent certain groups from being able to exercise them. DFID is scaling up work that will help women to own land and make better use of productive assets.

d) **Increasing employment opportunities and access to jobs for poor women and men**, through support for enhancing labour participation and mobility, for example through tackling discriminatory social norms, investing in skills, and supporting active labour market policies. For example, we are supporting the International Trade Centre to work with governments and customs authorities in East Africa, to improve conditions for female informal traders who face harassment and extortion at borders.

Chapter 3: Delivering our strategic framework for economic development

Supporting economic development at the country level

We are analysing the constraints to economic development in each country we work in so we can help create the best opportunities for our target beneficiaries in the local context. We place a strong emphasis on understanding the political economy, especially in fragile states, recognising that some structures stop the benefits of growth reaching the poor. We will fund high quality support to local institutions and other partners to help create the right conditions for inclusive growth. Box 1 provides an example of one such bilateral programme.

Box 1: Technical assistance on infrastructure in Nigeria

Inadequate infrastructure is a major constraint to growth in Nigeria (a country of 162 million with as much grid power as the UK's West Midlands, with a population of 5.6 million). DFID established the award-winning Nigeria Infrastructure Advisory Facility (NIAF), a technical assistance programme designed to enhance the government of Nigeria's capacity to better plan, finance and operate infrastructure delivery at the federal and state level. NIAF results include helping increase power supply in Nigeria by 45%, and supporting the recent privatisation of the power sector which brought in $2.5 billion of private sector finance.

Our country work will focus on our existing 28 priority countries. These have been chosen through DFID's business model on account of having large numbers of poor people, where the future prospects for the poor remain weak, and where we have sufficient comparative advantage to have a full bilateral presence. In poor countries where we do not have a bilateral presence, we will continue to provide support through our centrally managed programmes and through our contributions to multilaterals.

We are increasing our work with other UK government departments that can also have an impact on economic development in poor countries where DFID has no bilateral presence. We will also consider how to integrate economic development into DFID's work with the emerging powers, where we try to help shape their impact on development in poorer countries.

Strengthening regional integration

Regional integration supports trade and economic growth. It is an important focus of our overall approach to economic development. DFID will continue to support activity that can best or only be done at the regional level to promote deeper regional economic integration, trade and the development of regional markets. Regional economic integration will help the many small or landlocked African markets take advantage of economies of scale, and benefit from cross-border infrastructure investments in transport, communications and power. South Asia, although growing, has the highest concentration of poverty in the world; improved regional economic integration will help to connect the benefits of growth to the poorest parts of the region.

Working internationally and with multilaterals

DFID works with a range of multilateral organisations, including UN agencies, the EU, the Private Infrastructure Development Group (PIDG) and multilateral development banks (MDBs), such as the World Bank Group (including IFC and the Multilateral Investment Guarantee Agency (MIGA)) and regional development banks.

Multilaterals are a major source of finance and technical advice on economic development. The MDBs have particular expertise in areas such as financing large-scale capital infrastructure and access to finance, as well as growth analysis and economic policy advice. They also have a range of financing instruments at their disposal, and are able to raise significant funding from other sources, particularly the private sector.

As a major shareholder in and donor to many MDBs, the UK government is well placed to both shape and learn from MDBs' economic development work. DFID will work with the MDBs to ensure a more coordinated and strategic approach to economic development across each organisation. We will encourage MDBs to stimulate more private sector investment, particularly in the very poorest and fragile and conflict-affected countries. We will work with the MDBs and the private sector on larger, more strategic infrastructure projects, including regional programmes. Through targeted interventions with MDBs, such as deepening political risk insurance markets, we will strengthen the conditions for investment in fragile states. We will continue to push for better tracking and monitoring of the impact of economic development work.

DFID co-founded and is one of the principal funders of the Private Infrastructure Development Group (PIDG), a multilateral organisation with a portfolio of facilities that catalyse private investment in infrastructure in developing countries, by reducing risks for investors and targeting specific market failures such as early stage project development. In line with our objectives, we propose to scale up our funding for PIDG significantly. This responds to the huge needs in poor countries and the high priority poor country governments and businesses place on infrastructure. It also reflects DFID's comparative advantage and PIDG's strong performance to date. We will continue to ensure the governance arrangements are fit for purpose, and monitor the results delivered by the PIDG so that it keeps delivering value for money. We will also work more closely across headquarter departments and DFID country offices in priority PIDG countries, to ensure maximum poverty focus.

Within countries, DFID will increase its involvement with multilaterals on economic development. We will scrutinise investments more closely and identify further opportunities to align objectives and achieve greater impact from our combined resources. Internationally, we will continue to engage on key issues, including monitoring commitments made to promote private sector investment in the recently negotiated MDB funding agreements, helping shape proposals to stimulate infrastructure investment, and maximising the supply of finance for bankable projects, consistent with financial sustainability.

Working with business

We are increasing our work with small and large businesses, both national and multinational. Our engagement is through a combination of programming, dialogue, influencing and advice to business. Our support is provided in various ways, including through the New Alliance for Food Security and Nutrition, matching grants through competitive challenge funds (such as the Africa Enterprise Challenge Fund, which supports innovative business ideas in agriculture, agribusiness, renewable energy, adaptation to climate change and access to information and financial services), technical assistance (for example through the Business Innovation Facility, which provides support to companies to develop or scale-up inclusive business models), and increasingly loans/equity investments (particularly through CDC). We are ensuring rigorous policies are in place on when it is appropriate for us to work with for-profit businesses.

Over the last year, we have listened to business leaders to hear their views on how commercial and development objectives can support each other. We have learnt more from them about the constraints they face in frontier markets, and how we can better support companies to improve their development impact. In response we are overhauling how we engage with businesses, including:

a) Simplifying our website to bring together all DFID and external opportunities for business support in one place;
b) Adding dedicated advisory support to the cross-government business support helpline (run by BIS), providing information on working in DFID priority countries and new DFID programmes;
c) Conducting a series of roundtables with business representatives from the extractives, retail, infrastructure/construction and accountancy industries/professions to understand the opportunities and challenges in these sectors;
d) Pioneering ministerial visits to developing countries with business representatives to explore areas for collaboration on economic development and promote investment, such as the Secretary of State's visits to Tanzania in 2013 (see box 2).
e) Redesigning our systems for managing relationships with priority companies with significant potential to help reduce poverty through their core business, including dedicated company contact points, senior sector leads, regular strategic

relationship review meetings, and memoranda of cooperation around joint objectives.

Box 2: Secretary of State's economic development visits to Tanzania

In June 2013, the Secretary of State for International Development visited Tanzania to discuss how to make progress on the challenges international and local investors face. In November 2013, the Secretary of State returned with 18 organisations including firms such as Unilever, Diageo and SAB Miller, focussing on agriculture, the London Stock Exchange Group focussing on capital markets development, and smaller and local companies looking to invest in renewable energy.

The visits provided the opportunity for DFID to raise important economic development issues at a high level with the government of Tanzania, including on the investment climate, agriculture, and regional trade. The visits also accelerated some specific proposals for the delivery of DFID's economic development objectives, through co-investments in agriculture alongside established international and local investors.

It is not just about large multinational firms. Developing country entrepreneurship has a major role to play in development. Local entrepreneurs also offer investment opportunities, particularly in frontier markets. DFID is increasingly engaging with UK SMEs through face-to-face events organised with UKTI, and by ensuring those in other UK government departments that talk to SMEs, and organisations representing SMEs, are aware of opportunities to work with DFID.

UK businesses and networks have experience and reach that can make a big contribution to development. British companies are leaders in driving up ethical performance, through responsible investments and supply chains that can build vibrant local private sectors that don't harm poor people's interests. The UK Bribery Act (2010) ensures that UK companies adhere to the strictest guidelines on corruption. We are working to benefit poverty reduction and UK interests, within the terms of the International Development Act and our OECD commitments on aid untying.

Working with CDC

CDC is DFID's principal mechanism for leveraging private sector investment in poor countries. It plays an important role in our overall approach to economic development. With a reputation for high quality due diligence, which attracts capital from other Development Finance Institutions and commercial investors, CDC invests in businesses across Africa and South Asia, especially in the more difficult parts, with the potential to create jobs. In 2012, CDC capital was supporting 1,250 businesses in 77 countries. Those businesses are in turn supporting over 1 million jobs. Priority sectors for CDC investment include infrastructure, financial institutions, agribusiness, manufacturing, construction and health and education. CDC is increasingly using a wider range of financial instruments, including direct equity, direct debt and impact investing. All new investments are assessed for their development impact as well as their financial return. DFID and CDC are also considering how they can work together differently in the most difficult fragile and conflict-affected countries.

Harnessing other UK expertise and cross-government working

The UK has world-leading expertise in many of the areas that facilitate economic development in our priority countries. DFID is increasingly working with other UK partners and across government, to make use of this expertise to support economic development and poverty reduction. Our Investment Facility to Utilise UK Specific Expertise (IFUSE), for example, mobilises technical support from across businesses and government agencies to support our partner countries.

We will strengthen our work across government. Whilst DFID leads on international development, the FCO, UKTI, BIS, HMT, HMRC, DECC and Defra all play a role in promoting related UK interests overseas. We will work more closely together to ensure a coherent UK government approach to economic development. UK aid will remain untied, but there are lots of opportunities for joining up UK efforts to promote poverty reduction and UK growth simultaneously.

In addition to more regular policy engagement, DFID is forging closer links through specific collaboration across government, such as the well-established joint DFID/BIS Trade Policy Unit, the production in September 2013 of a Business and Human Rights Action Plan in collaboration with FCO, BIS and the Ministry of Defence (MOD), and the FCO-UKTI-DFID High Level Prosperity Partnerships in Africa. These partnerships aim to deliver a step-change in economic and trade relations in five pilot countries: Tanzania, Angola, Côte d'Ivoire, Ghana and Mozambique. The pilot projects are testing an increased and joint UK government focus on strengthening economic and trade links between the UK and Africa.

Working with civil society

Civil society organisations make an important contribution to economic development and ensuring equitable and inclusive growth and poverty reduction. They can also play a more direct role in promoting private sector growth and investment through, for example, support to microenterprises and microfinance in poor countries, closer work with small and medium businesses in for instance, agriculture, and through their knowledge of the local context. They do this through direct programming, policy and partnership work, but also by holding to account businesses for responsible and ethical behaviour, and governments for their policies and other actions.

DFID supports organisations such as the Ethical Trading Initiative to promote and monitor adherence to responsible and ethical business practices. Some civil society organisations are increasingly working with the private sector to achieve development outcomes. For example, Oxfam is on the Marks and Spencer Ethical Advisory Board, Practical Action is working with companies to develop or strengthen products and services that benefit the poor (such as market data updates sent to smallholder farmers via mobile phones), Save the Children is partnering with companies to improve access to medicines and vaccines for poor children, and CARE is providing support to strengthen dairy value chains targeting low income farm households. DFID will continue to provide support to organisations that are well placed to help address strategic priorities for economic development, both at the country and international levels.

Ensuring coherence

Delivering a coherent set of investments in economic development across the world and in individual countries is central to the success of this strategic framework. It will require close working across country and central offices. Headquarter departments will identify opportunities to drive efficiency through the use of programmes managed from the centre. Country offices will increase their engagement with multilaterals, such as the PIDG and the MDBs, and have a better overview of all relevant activity in that country. We will identify shared priorities and opportunities for more joined-up working across Government. In addition, we will consider implications of all our work on cross-cutting priorities, including climate change and women and girls. This framework provides a good basis for achieving greater coherence across the portfolio. Box 3 illustrates the extent to which multiple activities can work together to support a development priority.

Box 3: Supporting economic development in the extractives sector

Working with companies in the extractives sectors, with governments, nationally and regionally, across the UK government, civil society and internationally, DFID is promoting the transformative potential of natural resources for the economies and governance of developing countries. Having formed a Ministerial steering group with seven FTSE-100 companies last year, we are expanding our work to develop skills and build capacity for governments, and for local companies to allow them to sell into extractives supply chains. We have advanced plans to work with the Africa Legal Support Facility to ensure that African countries negotiating large-scale oil, gas and mining contracts have access to world-class legal expertise.

Building on UK leadership at the G8 in 2013, DFID is working with the FCO, BIS, leading international extractives companies and civil society, to deliver common global standards of extractives transparency in more countries. As we work with more countries in 2014 and 2015 to adopt the Extractives Industry Transparency Initiative (EITI) or match EU rules for listed extractives companies to report payments, this will help level the playing field for business internationally, and will give governments and citizens information to help improve tax revenues from extractives, and build accountability for use of extractive resources.

Chapter 4: Resources and effective delivery

Instruments

DFID has several well-tested instruments to deliver on its economic development objectives. We are also developing new instruments, and building the evidence base for which work best. These include investment vehicles, including new ways of working with CDC, innovative grant and technical assistance programmes, and partnerships with businesses. Our choice of instruments will consider the ability of our partners to finance their own investments, targeting our grant funding to those most in need and where it will have most impact, and making increasing use of loans and investments to maximise value for money.

DFID will continue to scale up its provision of financial services, access to energy, business services and advice on the investment environment. In conjunction with direct financial support, DFID provides a significant amount of technical assistance and policy advice in keys areas such as macroeconomic policy, natural resource management, tax administration, managing large scale infrastructure, and other constraints to economic development.

We are gradually increasing our use of investment instruments to stimulate private investment that benefits poor people. Through returnable capital, including loans and equity, we will share some of the risk that would otherwise slow down investment and business growth. Where we are sharing the risk of launching or expanding a business venture, we will also seek to share the rewards. This enables us to redeploy our aid money many times over, multiplying the development impact and reducing the distortion to the private market. Box 4 provides an example from the PIDG, which has substantial experience in leveraging private finance. In the last year, DFID has launched several returnable capital investments including the Impact Fund run by CDC, and the Samridhi Fund, targeting inclusive growth in India's poorest states. Investment instruments require additional skills and management processes to traditional grant programmes. We have been developing our capability, and will continue to do so as our use of investment instruments increases. We will be monitoring the financial returns and development impact of these investments closely.

Box 4: Leveraging private sector finance for infrastructure

The PIDG Group comprises nine donors who fund specialised companies to provide early stage equity and debt, guarantees and technical assistance to private sector infrastructure projects. DFID funds five investment companies and two grant facilities under PIDG.

One of these companies, Emerging Africa Infrastructure Fund (EAIF), *provides long term loans to projects in Sub-Saharan Africa to support infrastructure projects that would otherwise be difficult to finance, often because they are perceived to be very high risk. Commercial financiers and DFIs have provided loans to EAIF to on-lend. Financiers also benefit from the long duration of loans offered by EAIF, and invested around $2 billion alongside $100 million of EAIF financing to five projects in 2012. Around 90% of these investments by value was in low income countries and 60% in fragile or post-conflict states. For example, EAIF provided $6 million of funding to SAEMS Nyamwamba Hydropower Station in Western Uganda, with co-investments of $30 million. This is a 14MW run-of-the-river hydro plant which is expected to improve energy supply for about 580,000 people and create short-term and long term jobs.*

The funds invested by EAIF will be repaid at a later date, and will be available for EAIF to reinvest in other projects. If EAIF were wound up, DFID would be able to deploy the repaid funds towards other development activity.

Resourcing and management

To deliver on this ambitious agenda, we will scale up our financial and staff resources. This will involve a scale-up of our bilateral spend in countries, regions and from the centre. We will devote more staff time across the organisation to economic development. Working with the private sector in new ways requires new skills. DFID has enhanced its private sector skills through recruitment of new advisers with relevant expertise, and through more systematic professional development. We have stepped up our training on the use of new financial instruments, fighting corruption and fraud and working with particular sectors such as the extractive industries.

As part of an internal spending review, all business units within DFID have been tasked with developing more ambitious economic development programming. This process will be complete by July 2014. To signal our level of ambition, by 2015/16 we plan to target £1.8 billion of our budget on economic development, more than doubling the amount spent in 2012/13. This is on top of indirect funding through some of our core contributions to multilateral organisations. The level and focus of our spend will vary across countries and regions.

As part of the scale-up of effort on economic development, DFID has been re-structured, and is recruiting a Director-General for Economic Development. The new Director-General will help drive the scale-up of our work on economic development and ensure coherence across the department. We are also bringing together relevant policy and programming teams within our headquarters to improve our coherence.

We will ensure a robust approach to managing risks across our portfolio. Our economic development activities cover a broad range of countries, sectors and partners, including in areas that are relatively new for DFID. Ensuring successful delivery of our portfolio will require a comprehensive approach to risk management and mitigation, both at the programme and portfolio levels. We will undertake regular risk assessments for all our programmes, revising our approach to implementation as required. We will continue to follow best practice on anti-corruption and strengthen our approach as necessary to minimise the fiduciary and corruption risks.

Economic development work in fragile and conflict-affected states carries specific but manageable risks. We will seek out partners with a track record and expertise of working in these places, and ensure that they have appropriate systems in place to understand and respond to the context. We will work to ensure our own understanding and experience of these difficult environments is combined with that of our partners to strengthen our interventions. We will also help to deepen knowledge through research and evaluation on what works and how to operate in fragile states, to help manage these risks.

Increasing our work with businesses requires some specific risk mitigation measures. All partnerships that we enter into will adhere to rigorous principles of engagement that ensure value for money from our spend, and that uphold the UK's commitment to untied aid, and the other provisions of the International Development Act. We will only work with legitimate, financially sound businesses, with strong commitment to development impact, and to environmental, social and governance standards. Robust due diligence will help to safeguard our investments.

Monitoring, evaluation and value for money (VFM)

DFID will scale up efforts to monitor and evaluate the impact of our work on economic development. Across many organisations, including DFID, monitoring and evaluation of economic development results is at an early stage. Some multilaterals have more experience, and there are opportunities to both challenge and learn from their approaches to measuring results and impact on poor people.

In the first half of 2014, DFID ministers are making decisions on resource allocation from 2015 onwards, based on country analysis of the scope to implement policy priorities. These decisions determine the balance of our economic development work across the five pillars, and the aggregate outcomes we can deliver. Once complete, these decisions will form the basis for developing an appropriate framework of indicators to monitor progress against our objectives.

We envisage developing two sets of indicators. The first will track progress on economic development across our partner countries, and the impact of our work. The second will seek to capture other management information useful for tracking our activity, and for assessing the relative effectiveness of our interventions. Through our monitoring, we will ensure that learning of what works and what doesn't feeds into our decision-making and helps to build on best practice, particularly in fragile states where evidence is weak and hard to obtain.

We will strengthen our knowledge base by commissioning new research on the tools we use to bring about economic development, such as challenge funds and smallholder supply chains. This research will inform the design of future programmes and underpin training and learning events. We also plan to evaluate over 30 economic development programmes during the next four years.

We will continue to invest in lesson learning, skills building and sharing of expertise across the organisation, including through professional development conferences bringing networks of advisers together to learn from each other, and from leading academics and private sector practitioners.

Some areas of this agenda, such as job creation, investment and trade, are complex to measure, where the transmission of development activity through to growth and poverty reduction can involve several steps and take time. Where direct attribution is not possible we will seek to identify the contribution that DFID's interventions have made, and to assess value for money and the necessary conditions for success. However long the causal chain, we will do more to understand how beneficiaries see our interventions.

Changes to the investment climate and the international rules for shared prosperity will require tailored and different approaches to assess the impact of particular actions. We will be clear about our objectives and success criteria for areas of DFID support where direct impact is harder to measure, such as for policy dialogue, influence and funding to the multilateral system.

We will retain a strong focus on value for money. Our work on the enabling environment can impact whole sectors and industries and, if successful, the benefits can far exceed the investment of staff time and resources. Working at the international level is likely to complement our activities in countries, maximise impact and extend our global reach. The creation and expansion of advisory services and risk-sharing financing platforms for the private sector will also help to mobilise more private finance for investments, with greater developmental outcomes and opportunities to redeploy funds in the future.

We will assess and measure VFM across all instruments and spend, using VFM metrics where appropriate for specific interventions. Ultimately, the gradual reduction in aid dependency that economic development can accelerate represents the best value for money for the UK taxpayer.

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Chapter 5: Next steps

This paper sets out a strategic framework for DFID's economic development work. Our thinking on how to deliver against these objectives will continue to evolve, at various levels. Specifically:

a) At the highest international level, the debate among UN member states about what succeeds the MDGs in 2015, and the discussion of the role of business in development through the Global Partnership on Effective Development Cooperation, will shape the global international development landscape. DFID's work needs to fit into, and continue to influence, this landscape. The UK government continues to show strong political leadership in these debates, led by the Prime Minister. But we are also listening to others, including developing countries, businesses and civil society. We will engage internationally and with the multilateral system to ensure we maximise the effectiveness of our engagement and that of other donor partners.

b) Across the countries we work in, we are generating more detailed analysis of the national, regional and global constraints to economic development and poverty reduction. This will inform the activities we will support in each country and regionally/globally, how we will allocate resources, and the results we can deliver. We will take stock of what we plan to achieve in mid-2014, and continue work to monitor progress against our objectives.

c) As we develop and make more use of new instruments to support economic development, particularly those using returnable capital, we will continue to improve our policy and guidance about how best to use them, based on an increasing evidence base.

d) As we intensify our direct engagement with businesses, we are building up our knowledge of best practice of how we can work with companies to deliver development outcomes for poor people, and what they and other partners expect from us.

e) We will continue to invest in monitoring and evaluating our own programme impact and effectiveness to deepen the evidence base. We will share and apply knowledge, innovative ideas and best practice within DFID, in our partner countries, in international institutions and across the wider development community.

Our learning from all of these areas will feed into how we implement this strategic framework, and ultimately help finalise DFID's economic development strategy, based on a clear understanding of what works and achieves greatest value for money and impact.