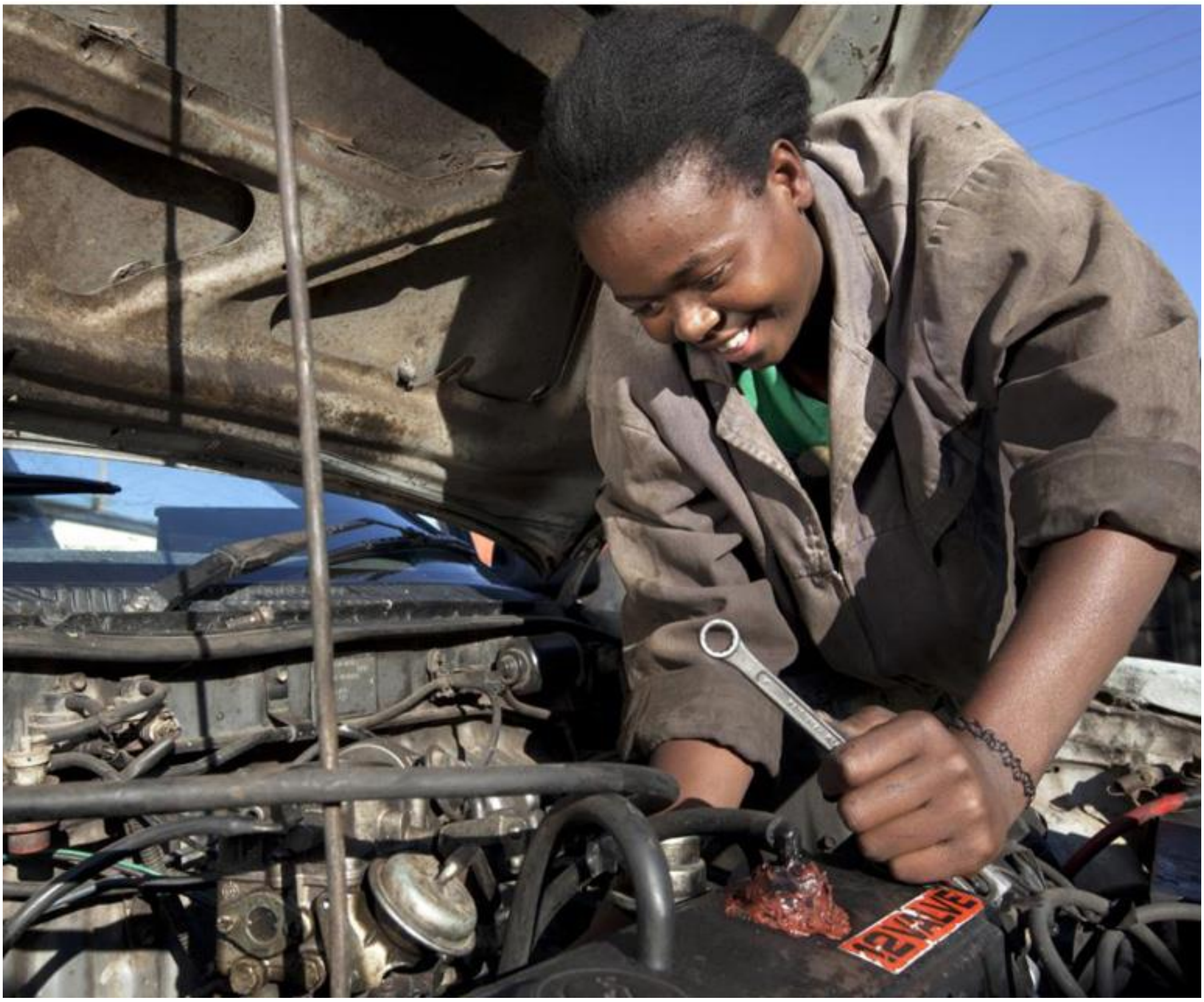
Department for International Development

UK aid from the British people

Bilateral Development Review: technical note



December 2016

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1. Process and methodology

The Bilateral Development Review set out to assess the shape of DFID's overall portfolio, geographical footprint and the mix of delivery channels in order to develop a set of allocations that will deliver the Government's commitments in the UK Aid Strategy ("UK aid: tackling global challenges in the national interest") and drive value for money. Rather than a top down allocation of money it prioritises a bottom up scrutiny of what results we can achieve through each country programme.

The Bilateral Development Review looked at where DFID previously operated and assessed what role we should play and how in the years ahead. This was based on evidence compiled from a range of analytical tools including Country Poverty Reduction Diagnostics, Inclusive Growth Diagnostics, a new approach to benchmarking aid allocation and a revised definition of fragile states.

This Bilateral Development Review technical note explains these analytical tools in more detail.

The Bilateral Development Review process consisted of three main phases. In **phase 1, bilateral spending teams (i.e. those in the main countries in which we operate and central teams with bilateral portfolios) prepared draft strategies.** These set out teams' visions of what they want to achieve, the proposed portfolio shifts during the Spending Review period and the space for DFID to act based on our comparative advantage. As part of this, DFID country offices refreshed Country Poverty Reduction Diagnostics to ensure that programming decisions were made using multi-disciplinary analysis, and Inclusive Growth Diagnostics to underpin programming discussions in the Bilateral Development Review around jobs and growth.

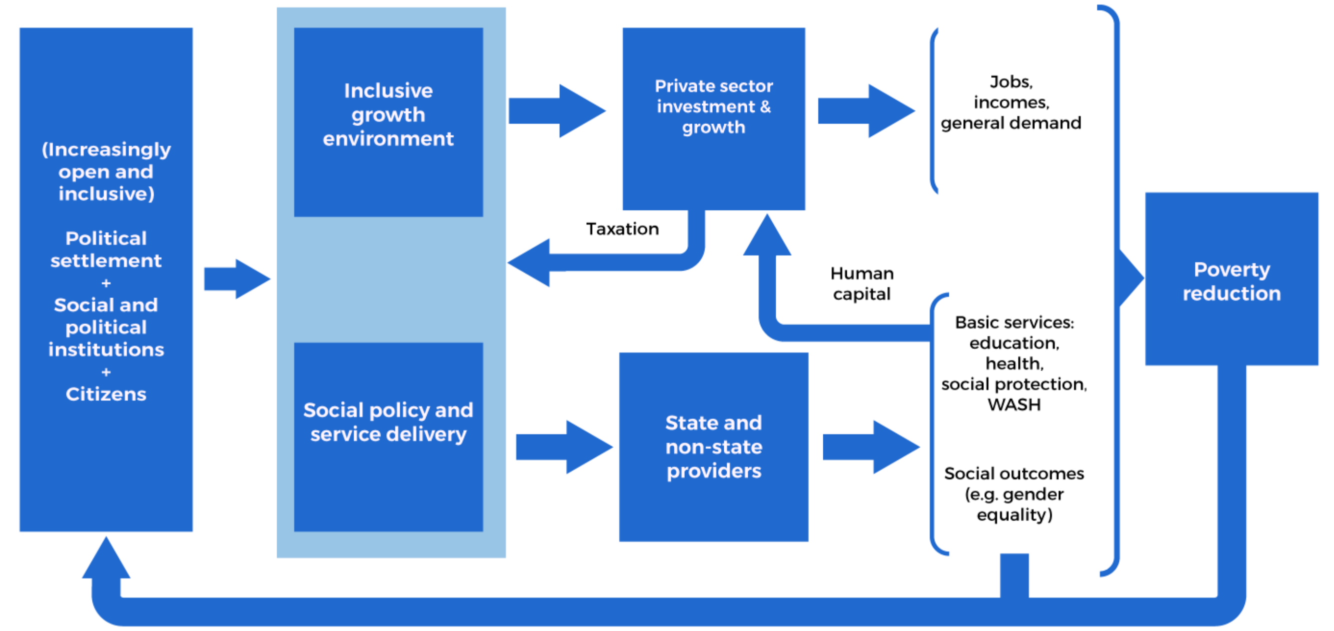
Building the evidence base - Country Poverty Reduction Diagnostics

The Country Poverty Reduction Diagnostic is a country programme planning and diagnostic tool designed and used by DFID to establish how we can make the most transformational investments in our partner countries to support a timely, self-financed and secure (low risk) exit from poverty.

DFID teams use the Country Poverty Reduction Diagnostic:

- to identify the most significant and causal barriers to poverty reduction in a country
- to identify how DFID can best address those barriers

This includes an analysis of what others are doing in the country (space for DFID to act) and what this means for a country strategy and programming choices given our particular expertise and comparative advantage. Teams use the Country Poverty Reduction Diagnostic to drill down to the core issues, think in a multi-disciplinary way (across economics, governance, social development, etc) and see the connections across sectors and different drivers of poverty.



The Country Poverty Reduction Diagnostic provides a common analytical framework based around seven core parts.

- Political settlement and institutions - the political settlement supports poverty reduction and inclusive growth. Social and political institutions must be increasingly open and inclusive and citizens increasingly empowered to ensure that benefits are shared and sustained.
- Conflict - the state is willing and able to establish sustainable peace across its national territory, and is free from, or can manage the impact of, regional and international drivers of instability.
- State capability - the state is willing and able to deliver core functions, including providing security and justice, drawing adequate taxation and managing public finances in order to fund the social policy and growth environments, and is able to implement their on-going upgrading.
- Growth - the growth environment is open and inclusive and facilitates private sector investment that results in robust, stable growth.
- Growth transmission - the growth process creates jobs, raises incomes and has a multiplier effect that raises formal and informal economic activity across the whole population.
- Social policy and service delivery - the social policy environment and service delivery is effective at reducing poverty, improving well-being and access to opportunities and choice for all, and provides sufficient outcomes to support growth.
- Resilience - the state and citizens have the will and capability to manage shocks and long-term trends that have the potential to derail growth and poverty reduction, including climate change, natural disasters and global or local economic crises.

Phase 2 of the Bilateral Development Review focused on coherence across DFID's portfolio bringing together initial findings from the Review with early findings from the Multilateral Development Review , Civil Society Partnership Review and the Research Review to help Ministers make choices to shape DFID's portfolio.

It ensured that DFID has the right mix of policy and sector priorities and channels to deliver priorities set out in the Government's manifesto, UK Aid Strategy, Spending Review and the Strategic Defence and Security Review. The coherence phase looked at what we are doing geographically, where we are working, and also how we are going to deliver our programmes. This includes whether we deliver through multilaterals, through bilateral programming or through central programming.

Building the evidence base - Inclusive Growth Diagnostics

Inclusive Growth Diagnostics look at the barriers to inclusive economic growth in a country. They examine a core part of the Country Poverty Reduction Diagnostic framework, focusing on the dynamics of economic growth and transformation from a less developed to a more developed economy, and how UK aid can best be targeted to support this process to accelerate poverty reduction. Inclusive Growth Diagnostics examine the country dynamics, including the theoretical opportunities in the economy, and the real economic and political constraints that are holding inclusive growth back. This helps to build the evidence base for how to prioritise economic development investment.

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The flexible and adaptive model asks analysts to work through the following stages:

Inclusive Growth Diagnostic stage 1 - diagnostics

- What accounts for the currently observed pattern of growth?
- What are the sectoral opportunities for inclusive growth?
- What factors constrain this growth and investment?
- What political or institutional factors enable the constraints to persist?
- What are possible future directions for the economic development portfolio?

Inclusive Growth Diagnostic stage 2 - DFID options

Stage 2 assesses country portfolios against the evidence base, and considers DFID's space to act.

- Is there a strong rationale for UK involvement?
- What mechanism is used to tackle this constraint at present?
- Would it be useful for another part of DFID to intervene, for example, a centrally managed programme?
- Does the multilateral system work in this area?

Phase 3 of the Bilateral Development Review focused on business planning. Teams finalised their various strategies, and aligned these with programme and operating cost budgets for the Spending Review period 2016/17-2020/21. This allocation process was used to drive value for money, ensuring that DFID continues to focus on investments that have the highest return and which we can deliver effectively. We aim to have a set of arrangements that sustain sufficient flexibility so that we will be able to respond to future challenges, as they arise, during the course of this Parliament.

DFID programme spend and indicative allocations by department are set out in DFID's Annual Report and Accounts 2015–16.

DFID country teams have consulted with a range of stakeholders on both the pre-Bilateral Development Review analytical work (Country Poverty Reduction Diagnostics and Inclusive Growth Diagnostics) and in the early phases of the Review, including Government, multilaterals, civil society, academics, the private sector and young people.

In July 2016, the Rt Hon Priti Patel MP was appointed Secretary of State for International Development. The Bilateral Development Review outcomes have been reviewed to reflect the Secretary of State's priorities, the UK's decision to leave the European Union, and recent machinery of government changes.

2. Aid allocation model

The Government will continue to give strong support to the world's poorest countries. **We are concerned with extreme poverty everywhere but we focus programming on countries where extreme poverty currently affects a significant proportion of the population and is projected to persist over the medium term, and where the country itself is unable to finance the reduction of poverty.** The majority of DFID's programming is focused on countries where DFID has a comparative advantage. DFID programming reaches other poor countries through our bilateral programmes managed centrally, including investment instruments, and our core funding to multilateral organisations, civil society and academia.

In order to inform our approach to overall, multilateral and bilateral aid allocation, DFID has developed an aid allocation model. This model provides an allocation of aid for the reduction of poverty and does not address humanitarian aid or aid to transition countries (when countries can finance their own development the nature of the relationship with the UK will change). We will use the model as a benchmark to evaluate global aid allocation, including how multilaterals allocate their resources and the graduation policy that these allocations imply. We also use the model as a benchmark for the allocation of bilateral country programme resources focused on extreme poverty and poor human development outcomes. We take into account a range of factors in our bilateral approach to allocations including specific risks, national security priorities, our comparative advantage, the degree to which countries receive aid in comparison to their needs and our ability to deliver the Government's commitments.

Building the evidence base - benchmarking aid allocation

DFID's aid allocation model is based on the principle that aid should be allocated in relation to:

- present need as expressed by extreme poverty corrected for large deviations in child mortality and the multi-dimensional poverty index
- aid effectiveness - the degree to which aid can translate into poverty reduction in a particular context
- future need - since aid can largely be expected to have a permanent effect, we should take into account this effect on future poverty
- ability to self-finance - aid should not be given to the same extent in countries that could self-finance their poverty needs

We have introduced a new concept, Person Poverty Years - the number of people in poverty in a country multiplied by the number of years they are expected to remain poor. These principles combine into an overall objective that aid should be used to maximise the reduction in person poverty years until a country is able to self-finance poverty reduction.

A country is deemed able to self-finance when the aggregate poverty gap - that is the amount required to bring all incomes up to the extreme poverty line - falls below one percent of Gross Domestic Product. While this is a simplification of unknown financing potential, it represents an appropriate challenge to a government, and provides an implicit graduation criterion for the model. Rather than countries graduating from aid at a particular income or poverty level, this approach brings a trade-off between the two, with better-off countries graduating at higher poverty thresholds than less well-off countries.

3. Fragile states methodology

The Bilateral Development Review assessed the shape of our geographical footprint, looking at where DFID currently operates, what role we should play and how. As set out in the Strategic Defence and Security Review and the UK Aid Strategy, **DFID is committed to spending at least 50% of our budget in fragile states and regions in every year of this Parliament**.

Building the evidence base - approach to defining fragile states and regions

We have identified fragile states and regions that: suffer external and social stresses that are particularly likely to result in violence; lack the capacity to manage conflict without violence; and neighbouring states that are especially susceptible to instability.

Our assessment of fragile states is based on open-source data from a range of sources, including the World Bank, United Nations and the World Peace Index. Our full list of fragile states and regions (below), which we will update regularly to reflect changes in the data, includes:

- countries on DFID's fragile states list
- Overseas Development Assistance eligible countries neighbouring high fragility states (excluding China and India)
- 3 specifically designated fragile regions, which contain many of the fragile states on DFID's list

Table A: List of fragile states and regions

High fragility	Moderate fragility	Low fragility	Neighbouring high fragility states	Regions
Afghanistan	Bangladesh	Liberia	Jordan	Middle East
Burma	Ethiopia	Nepal	Rwanda	South of Sahara
Congo, Dem. Rep.	Kenya	Sierra Leone	Tanzania	North of Sahara
Iraq	Kyrgyz Republic	Uganda	Zambia	
Pakistan	Lebanon	Cameroon	Thailand	
Somalia	Nigeria	Belarus	Algeria	
South Sudan	Occupied Palestinian Territories (OPTs)[1]	Cambodia	Armenia	
Sudan	Tajikistan	Colombia	Laos	
Syrian Arab Republic	Zimbabwe	Congo, Rep.	Tunisia	
Yemen, Rep.	Angola	Côte D'Ivoire	Turkey	
Central African Republic	Azerbaijan	Djibouti		
Libya	Egypt, Arab Rep.	Honduras		
Burundi	Guinea	Madagascar		
Chad	Guinea-Bissau	Mauritania		
Eritrea	Haiti	Niger		
Iran, Islamic Rep.	Mali	Paraguay		
Korea, Dem. Rep.	Turkmenistan	Timor-Leste		
	Uzbekistan	Ukraine		
	Venezuela			

[1] The OPTs are a non-member observer state at the UN.

The Department for International Development:
leading the UK Government's fight against world poverty.

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