Gaps in financing poverty eradication and how to increase domestic resource mobilization

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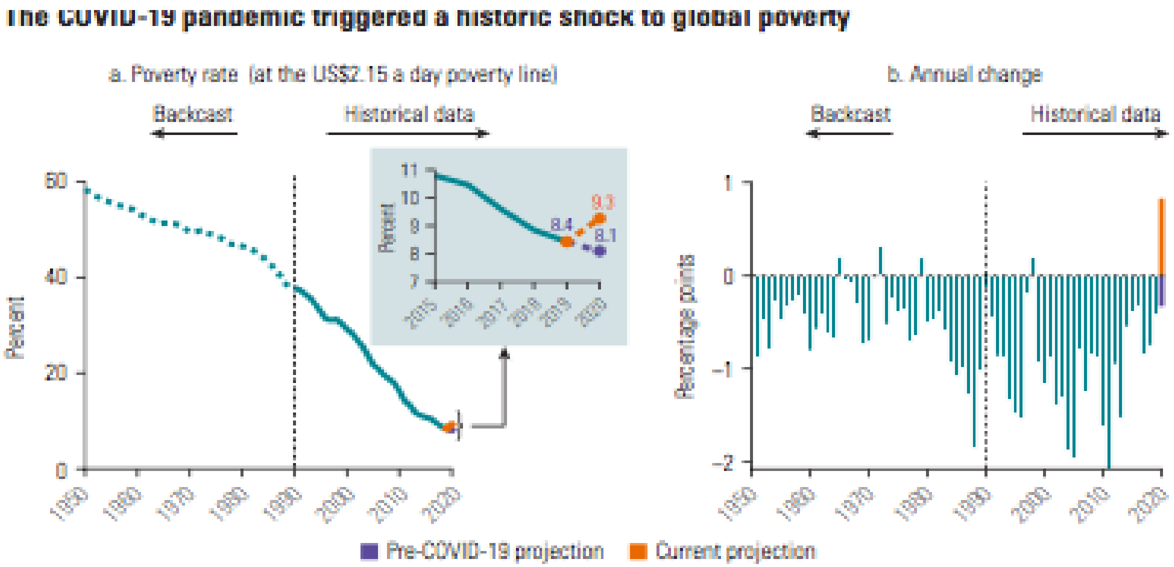
Introduction

- Poverty eradication is a multidimensional concept.
- SDG-1 aims to ***eradicate poverty*** (both extreme and according to national poverty lines), expand ***social protection coverage***, ensure equal ***access to economic resources and basic services***, and strengthen the resilience of the poor against ***climate-related extreme events***.
- ***Poverty eradication initiatives are difficult to pursue in low-income and lower-income countries.***
    - ***Resource constraints.***
    - ***Inadequate resource mobilization and lack of customized and targeted strategies (Target 1a, and 1b).***
    - ***More vulnerable to external shocks.***
    - ***Tendency to focus on short-term goals.***
- This discussion will highlight the challenges and constraints faced by lower-income countries and will offer some recommendations.

Current Status of Poverty Eradication

- Even before the COVID-19 pandemic the pace of poverty eradication was slowing down.
- Poverty eradication initiatives were ***seriously affected by the pandemic,*** and for the first time in decades, the number of ***extreme poor has increased***.



Source: Poverty and Shared Prosperity Report 2022, WB

- The World Bank forecasted that the extreme poverty rate (USD 2.15 a day) ***in the world will be 7% in 2030***, much higher than anticipated.

Current Status of Poverty Eradication

- Apart from the pandemic, the ***recent geopolitical issues, and the rise in inflation*** are likely to slow down the effectiveness of poverty eradication strategies.
- During the pandemic, the income loss of the poorest was much higher than that of relatively richer people. Not only has poverty increased, but income inequality has also widened.
  - Income losses of *the poorest 40 percent of the World's population were twice as high as those of the richest 20 percent*.
- Multidimensional poverty has also worsened, and the ***loss in health and education is much higher in lower-income countries*** than in higher- income countries.
  - Lower-income countries recovered slowly from the pandemic, while upper-middle and high-income countries recovered quickly.

Gaps in financing poverty eradication

- ***Challenges of raising funds for poverty eradication without hurting the poor.***
  - *Large informal sector* and *lower tax to GDP ratio*.
  - Limited resources restrict the government's ability to allocate sufficient funds to social welfare, health, education, and infrastructure development.
  - Reliance on indirect taxes, and the *combination of tax, subsidies, and transfers do not often benefit the poor*.

- ***Challenge of reducing inequality in resource allocation.***
  - Within countries, there is often a disparity in resource allocation, with marginalized communities and regions receiving disproportionately less funding.
  - Priorities are often determined by political pressure groups.
  - World Bank data reveals that after the COVID-19 pandemic, ***half of all spending on energy subsidies in low- and middle-income countries went to the richest 20 percent*** of the population.

Gaps in financing poverty eradication

- ***Challenge imposed by the volatility of financing.***
  - Dependence on external sources of financing, including official development assistance (ODA), foreign direct investment (FDI), and remittance inflows.
  - These sources *can be volatile and subject to fluctuations in global economic conditions, geopolitical factors, and donor priorities*, making it challenging for countries to plan and sustain poverty eradication efforts.
  - In 2022, the per capita average net ODA receipt *was $79.59 in low-income countries and $141.97 in lower-middle income* countries with sizable country deviations.
  - ***Range of net ODA receipt per capita in 2022 :***
    - Low-income ($0.5 - $374.12)
    - Lower-middle-income ($0.5 - $1317.32)

Gaps in financing poverty eradication

- ***Challenge of making long-term investments in productive sectors.***
  - Lower-earning countries often make suboptimal investments in short-term objectives.
  - It is essential that low and lower-income countries continue to make and adhere to long-term, high-return investments in education, research and development, and infrastructure projects.
- ***Challenge of addressing the impact of climate change on poverty eradication.***
  - Climate change disproportionately affects countries.
  - Climate change affects poverty reduction initiatives through *direct impacts on the poor and through factors that influence poverty reduction*, such as achieving inclusive economic growth.
  - ***Challenge of insufficient fund and how to properly utilize the fund.***

Gaps in financing poverty eradication

- ***Managing corruption and governance challenges.***
  - Weak governance structures, corruption, and lack of transparency in financial management can undermine effective resource allocation and implementation of poverty reduction programs.
  - ***Tendency to focus on short term goals, policies often aims to favor certain pressure groups***, and failure to properly utilize the available fund.

Ways to increase domestic resource mobilization

- ***Progressive Taxation.***
  - Implementing progressive taxation systems can help generate revenue from those who can afford to pay more, thereby reducing income inequality and providing funding for poverty eradication programs.
  - Due to the presence of a large informal sector, low and lower-middle-income countries rely on indirect taxes for revenue collection.
  - These countries may *focus on relying more on property tax and other direct taxes and make the tax rate progressive so that the tax burden is shifted towards more wealthy individuals*.

Ways to increase domestic resource mobilization

- ***Broadening the Tax Base.***
  - Expand the tax base by bringing informal economic activities into the formal sector and reduce tax evasion and avoidance.
  - This may involve improving tax administration, implementing electronic tax filing systems, and combating illicit financial flows.

- ***Improving Tax Compliances.***
  - Enhancing tax compliance through public awareness campaigns, simplified tax filing procedures and measures to address tax evasion and corruption can help increase government revenue without imposing additional tax burdens on compliant taxpayers.

Ways to increase domestic resource mobilization

- ***Fund utilization from micro-finance schemes and financial inclusion initiatives.***
  - Poverty eradication can be accelerated by using microfinance and financial inclusion schemes in low and lower-middle-income countries.
  - The success of microfinance and other formal financial inclusion initiatives depends on the managerial skills of the borrowers.
  - *Success is not always guaranteed as the poor are not always expected to be good entrepreneurs.*
  - Supervision and engagement of lenders are crucial.
  - *Reluctance of formal financial institutions is a big challenge.*

Ways to increase domestic resource mobilization

- ***Capitalize opportunities offered by digital finance.***
  - Mobile banking, digital wallets, and other digital financial tools allow people to conduct transactions, access credit, and save money more conveniently and affordably, even in remote areas where traditional banking infrastructure is lacking.
  - Digital finance *can lower the cost of financial transactions and help low-income households manage their cash flow and cope with financial shocks more effectively.*
  - Digital savings accounts, insurance products, and microcredit platforms enable people to build financial resilience by saving for emergencies, accessing credit when needed, and protecting themselves against unexpected expenses or income loss.
  - *The World Bank report confirms that digital cash transfer programs in India and Brazil have been very successful during the COVID-19 pandemic.*

Ways to increase domestic resource mobilization

- ***Promoting inclusive economic growth.***
  - Fostering inclusive economic growth through investment in infrastructure, education, healthcare, and entrepreneurship can expand the tax base and generate additional revenue for poverty reduction efforts.
  - Supporting small and medium-sized enterprises (SMEs) and creating employment opportunities can also reduce dependency on social welfare programs.

- ***Private sector engagement.***
  - Encouraging private sector participation in poverty eradication efforts through corporate social responsibility initiatives, public-private partnerships, and investment in socially responsible projects can mobilize additional resources and expertise for sustainable development.

Recommendations

- ***Targeted cash transfer policies.***
  - The Poverty and Shared Prosperity Report 2022 reveals that more than *sixty percent of spending on cash transfers goes to the bottom forty percent*, and cash transfers also have a larger impact on income growth than subsidies.
- ***Ensure that public spending and donor funds are used for long-term investment purpose.***
- ***Utilize financial inclusion initiatives.***
  - Ensure engagement of formal financial institutions, enrich financial literacy, and ensure close monitoring.
- ***Utilize digital-finance to reach the unbanked, expand economic activities, and help the poor to mange cash flow and cope with shocks.***
- ***Ensure that the use of climate fund is aligned with the restoration of livelihood of the poor.***
- ***Make the tax system progressive, rely more on direct taxes, and adopt strategies to penetrate the informal sector.***

Conclusion

- The challenges facing low and lower-middle-income countries in financing poverty eradication efforts are formidable, encompassing issues such as inadequate resources, limited revenue streams, and inequalities exacerbated by ineffective tax systems and transfer payments. Moreover, the volatility of financing sources and the growing impact of climate change add further complexity to these endeavors.

- Addressing these challenges demands a comprehensive approach, including measures to boost domestic resource mobilization through progressive taxation, broadening the tax base, and enhancing tax compliance. Leveraging funds from microfinance schemes and embracing digital finance can also play a pivotal role in fostering financial inclusion and resilience among marginalized populations.

Thank You