

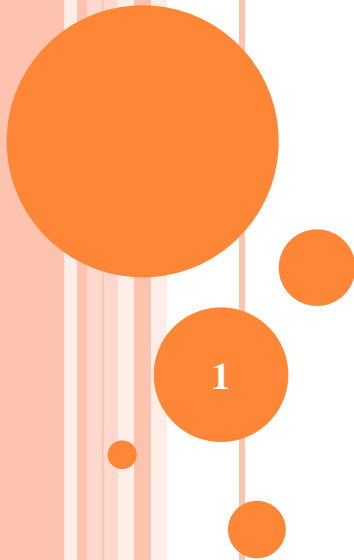
**BACKGROUND DISCUSSION PAPERS FOR ECFIN
CONFERENCES**

ASEM – CONFERENCE

**THE ASIAN EXPERIENCE IN
FINANCING RURAL
DEVELOPMENT**

PRESENTED BY: PAUL SCHOEN

11 December 2009, Shanghai



PRESENTATION OUTLINE

1. Summary Profile of Asia and Asian ASEM Countries
2. Patterns of Rural Development (RD) and Financing RD:
 - a) RD typologies
 - b) Financing rural development
3. Role of International Finance Institutions (IFIs)
4. Assessment of the effectiveness of financing RD
5. Key lessons learned
6. Recommendations for the future

1. SUMMARY PROFILE OF ASIA AND ASIAN ASEM COUNTRIES

- Asia and the Pacific, as a whole, is the world's largest and most diverse region, ca. 30% of the globe.
- Its population at 4 billion in 2006 (66% are rural based) accounts for 61% of the world's total.
- The region is diverse, ranging from large countries, such as the PRC, India and Indonesia, to very small Pacific island nations and landlocked states.
- Diversity of endowment, context and pattern of human settlement suggests that any strategic approach to RD must be situation and setting-specific.
- Drawing out commonalities is problematic and flawed except for a few broad generalisations.

1. SUMMARY PROFILE OF ASIA AND ASIAN ASEM COUNTRIES (CONT.)

- The geographic scope of this presentation covers the 16 Asian states that make up Asian members of ASEM.
- These 16 contain a wealth of diversity, experience and challenges and share a common interest in RD.
- They have a combined population of 3.3 billion of which ca. 60% are rural based.
- Whilst dynamism of the Asian economies with high aggregate growth rates is widely acknowledged, the distribution of population and income underlines a wide disparity within the region.
- Low per capita income reflects low standards in social parameters such as maternal and child mortality rates, access to potable water, malnourishment and wasting in school enrolment.

2. PATTERNS OF RD AND FINANCING RD

- Fully understanding RD is important although the concept is itself nebulous with a range of definitions.
- While it is often totally identified with agriculture, it is also has a multi-sectoral dimension – such as land and water development, fisheries, livestock or income generating activities.
- Other aspects of RD are education, health, WATSAN, market development and financial services.
- RD has come to be associated with poverty and particularly rural poverty.
- Financing mechanisms for RD have become increasingly concentrated on those segments of population with poor access to regular credit.

2. PATTERNS OF RD AND FINANCING RD

(CONT.)

- RD does not appear as a category on its own in any budget databases of the countries under examination nor of IFIs and development partners.
- Comparison of the allocation of government and donor budgets is therefore problematic.
- It is only when agriculture based production activities is packaged together with a range of other activities that are focused on the rural areas, has it been labelled under the category of RD.
- One of the reasons why the WB has preferred to perceive it (i.e. RD) as activities within the arena of “rural space”.

2. A) RURAL DEVELOPMENT TYPOLOGIES

- Patterns of RD suggested focus on 3 typologies:
 - a) **Financing public infrastructure (hardware).**
 - b) **Provision of public goods, institutional development and capacity building (software).**
 - c) **Investment in agricultural and non-farm based rural business.**
- Implementation modalities and drivers include instruments such as Community Driven Development (CDD), Self-Help Groups (SHGs) and potentially the typology of Public Private Partnerships (PPPs).

2. A) RD TYPOLOGIES

- The typologies are very different in themselves requiring different sources, levels and types of financing.
- However, the provision of sufficient financing for rural activities and particularly for the rural poor has not been successfully achieved by all the countries in the region, although it has been addressed by nearly all of them.
- The typologies attempt to categorise the broad spectrum of activities that encompass RD in Asia regardless of the method of its financing.
- While they appear as independent categories there are obvious areas of overlap and in an effort to nurture development in the rural areas, a variety of approaches define the manner within which RD has been pursued.

2. B) FINANCING RD

- 5 key financing mechanisms in Asia are discussed:
 - a) National Mechanisms.
 - b) Official Development Assistance and Official Development Finance - Financing for Rural Development.
 - c) Foreign Direct Investment (FDI).
 - d) Public Private Partnerships.
 - e) Remittances.

2. B) FINANCING RD (CONT.)

a) National Mechanisms

- Investments are generally funded through the financial and banking system including public development banks, private banks, cooperatives and credit unions, and increasingly, MFIs.
- The Agricultural Development Bank (AgDB) instrument provides a good example of the experiences of delivering finance as a national mechanism, to the rural sector but in this case targeted at agriculture in particular. Examples of AgDB include: Bank for Agriculture and Agricultural Cooperatives (BAAC), Khan Bank (Mongolia), Bank Rakyat Indonesia (BRI)

2. B) FINANCING RD (CONT.)

b) **ODA/Official Development Finance – FfD**

- ODA stems from post-war international economic system design, recognizing the need for official financing to counteract insufficient private capital flows and the need to support developing countries.
- Private financing to developing countries surged in the 1970s until the late 1990s when, there emerged a realization that ODF had perhaps peaked.
- Private capital vagaries during the 1980s and, again, since the 1997 Asian crisis, plus increasing marginalization of the poorest countries, saw a renewed focus on ODF.
- The 2002 International Conference on FfD was a landmark, resulting in the Monterrey Consensus, restoring the central role of ODA, support for the poorest countries and reaffirming the 0.7% GDP IDA target.

2. B) FINANCING RD (CONT.)

- During the 1980s and 1990s, the WB and IMF promoted changes in the way that developing country governments financed both recurrent and capital investment.
- Under Structural Adjustment Programmes (SAPs), agriculture in particular and RD in general, received less government and donor funding, preferring market forces and the private sector to be encouraged or “enabled” through policy support.
- Institutional strengthening became the official way forward.
- ODA to the focus ASEM region was about US\$ 10 billion or 10% of total global ODA in 2008/9.

2. B) FINANCING RD (CONT.)

c) **Foreign Direct Investment (FDI).**

- The largest source of investment in Asia remains FDI dwarfing all other sources of overseas capital inflow.
- Some is invested in the rural sector but exactly how much is difficult to say – disaggregating by location and purpose is hugely difficult.
- Most FDI in the region goes to middle and high-income economies as one would expect.
- FDI analysis suggests capital inflow goes to countries with skilled workforce and developed physical infrastructure suggesting that funds are designed to support industry rather than “rural space” development.
- In 2007 alone, FDI to Asia and the Pacific as a whole climbed 28% to reach US\$ 372 billion or 2.4 times the yearly average for 2001-2005.
- China continued to receive the largest amount at US\$ 83.5 billion in 2007.

2. B) FINANCING RD (CONT.)

- d) **Public Private Partnerships (PPP).**
- A new approach however to development has been the shift to utilise private finances to fulfil government directives.
- Often due to a lack of public funds state or public institutional activities are hampered and therefore instead of financing projects alone (often large scale infrastructure type ventures), government has turned to cooperate with private sector investors.
- Although there are few examples there is an interesting case of UNDP and Nestlé forming a development partnership in Pakistan which has shown some promising results.

2. B) FINANCING RD (CONT.)

e) **Remittances**

- Remittances are clearly an important source of financing. With over 50 million migrants from Asia they have generated >US\$ 100 billion a year.
- India and China are the top recipient countries receiving >US\$ 21 billion respectively and constitute ca. 3% of the regions GDP
- A significant amount flows to rural areas and is used for asset creation and generation of economic activities (e.g. land purchase, farm investment and human capital).
- Remittances have had a positive impact in transforming the banking infrastructure with banks responding to the demands of migrants to facilitate flow of resources, provide services to speed up transfers and manage funds more effectively.
- There is also evidence of land price increases in certain areas where groups have migrated *en-bloc* such as India and the Philippines.

3. THE ROLE OF IFIS

- IFIs have played an instrumental role in the development of the rural sector and complement the direct financing of projects and programmes by the grant based agencies.
- Leading and dominate Asian IFIs: WB and ADB.
- Other supporting institutions include IFAD
- These institutions provide loans to Government on payback conditions usually long term and at interest rates attempting to match affordability.
- IFIs also provide, of course, some grants and/or TA to identify, scope, design, and appraise projects for which the loan are used.

3. THE ROLE OF IFIS (CONT.)

- Paragraph 45 of the Monterrey Consensus highlighted the role that IFIs should play “in serving the development needs of developing countries and countries with economies in transition”.
- It stated that IFIs should:
 - “...contribute to providing an adequate supply of finance to countries that are challenged by poverty, follow sound economic policies [who] may lack adequate access to capital markets. They should also mitigate the impact of excessive volatility of financial markets. Strengthened regional development banks and sub-regional financial institutions add flexible financial support to national and regional development efforts, enhancing ownership and overall efficiency. They also serve a vital source of knowledge and expertise on economic growth and development for their developing member countries”* (Sagasti, Bezanson and Prada, 2005)

4. ASSESSMENT OF THE EFFECTIVENESS OF FINANCING RD

- The effectiveness of RD financing is very difficult to assess without specific country-by-country field based research and analysis.
- There are no general studies/literature readily available.
- Although numerous studies have been undertaken in a number of countries dealing with the approach taken to address the critical outstanding issue of access to credit by the rural poor and the role of the banking system, this does help in coming to conclusions on the financial policy environment and the effectiveness of MFIs.

4. ASSESSMENT OF THE EFFECTIVENESS OF FINANCING RD (CONTINUED)

- To answer the effectiveness question involves establishing what the finance was designed to do in the first place.
- In its broadest definition, the intention of making finances available or actually paying for a development activity such as infrastructure, is of course economic growth and sustainability.
- This is the overall objective but the specific objectives are often something much less grand but equally difficult to achieve and attribute.
- The analysis of finances from bilateral and multilateral donors including IFIs for example, whether global or regional, demonstrates an erratic nature of fund availability and therefore impact.

4. ASSESSMENT OF THE EFFECTIVENESS OF FINANCING RD – IMPACT IN ASIA

- There is little doubt that poverty in Asia-Pacific as a whole reduced since in the 1990s.
- Poverty incidence, using a dollar-a-day standard, declined by about 30% over the decade.
- In 1990, about 32% of people in the region were living below the poverty line. By 2000 this proportion had come down to 22% and rural poverty declined from 39% to 28%.
- The absolute number of the poor also declined, by ca. 180 M, from 900 M in 1990 to ca. 720 M by 2000. This was achieved in spite of the 1997 financial crisis which depressed regional growth.

4. ASSESSMENT OF THE EFFECTIVENESS OF FINANCING RD (CONTINUED)

- ESCAP sums up the issue of effectiveness :

“A growing understanding of the factors that constrain the effectiveness of aid has helped identify problems in respect of both the supply of donor funds and the limitations in recipient countries. The challenge for the official donor community as well as policymakers in developing countries has thus been to recognise the weaknesses of the earlier approaches in aid delivery and to work towards new frameworks to enhance aid effectiveness.”

(World Economic and Social Survey for 2005).

4. ASSESSMENT OF THE EFFECTIVENESS OF FINANCING RD (CONT.)

- ADB and WB have increased their attention to agriculture and rural development and the scene is set for implementation of this (even if there is a decline in financial spend to these sectors).
- The WB has also developed two new sub-regional strategies for S Asia and East Asia-Pacific since 2004, but it is too early to tell how effective these will be.
- According to the 2004 Annual Review of Development Effectiveness of WB, close to 85% of the WB's operations globally showed satisfactory outcomes in the agriculture and rural sectors from 2000 to 2004, up from around 75% between 1995 and 1999, with operations in all sectors in Asia and the Pacific performing better than other area operations.

5. KEY LESSONS LEARNED

- The region displays great variation in its approach to developing rural areas and finding solutions to poverty. There appear to be no “silver bullets” which can be replicated with success across the region and real commonalities are difficult to find.
- Various typological approaches to RD can be identified as experiences of rural financing such as those for public goods, public infrastructure and those for private sector support, including those through the financial system.
- Financing RD means more than just agriculture, although agriculture is a useful “gateway” for financial consideration.
- The knock-on and integrated relationship that agriculture has with all other activities in rural areas is important and should be promoted.

5. KEY LESSONS LEARNED (CONT.)

- Creating the institutional framework for a financial and banking sector where formal institutions reach downward to the rural poor and the informal ones help the poor reach upwards into more formal financial mechanisms presents a challenge.
- The challenge of financing RD has to be solved primarily by the private sector (domestically or internationally) because of the huge resources available to them either through FDI, through the financial and banking systems or through remittances.
- PPP opportunities exist with even modest sized schemes yielding promising social and economic returns.

6. RECOMMENDATIONS FOR THE FUTURE

- A common definition for RD would be helpful.
- National and institutional data on finances, loans and grants should be disaggregated sufficiently to understand where investment is going (disaggregated by rural/urban regions).
- RD is a product of various financing sources with careful needed to ensure that the linkages across rural space are established and consequences are fully understood. This has a bearing on sustainability and impact of the investment.
- A careful review of alternative financing instruments needs to be considered and complementarities established - providing incentives for private funds (such as remittances, credit and FDI) to flow more effectively complementing public services.

6. RECOMMENDATIONS (CONT.)

- Rural financial markets have an important role to play and should be promoted through establishing an appropriate policy environment, building financial infrastructure and developing institutions to deliver tailored finances that meet the demands of those needing credit or financial services.
- Reviews of the scope and effectiveness of rural activities of government and multilaterals should be considered a continuous exercise.
- Collaborative reviews, monitoring and evaluation of delivery mechanisms should be regularly and routinely undertaken with ASEM being a good platform for this.

Let me conclude here with some food for thought regarding the “The Golden Rule”.

“The person with the gold, makes the rules”

Ladies and Gentlemen, you have the opportunity to make the rules and ensure that RD works well for the majority.

Thank You Very Much for Your Time.

For further information on the topic please e-mail:

paul.schoen@smartscore.eu