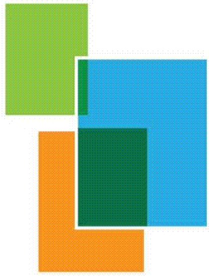

SOCIAL AND ECONOMIC POLICY

WORKING PAPER

IDENTIFYING FISCAL SPACE

Options for Social and Economic Development for Children and Poor Households in 182 Countries

Isabel Ortiz

Jingqing Chai

Matthew Cummins

October 2011

UNICEF POLICY AND PRACTICE

UNICEF SOCIAL AND
ECONOMIC POLICY
WORKING PAPER

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Identifying Fiscal Space: Options for Social and Economic Development for Children and Poor Households in 182 Countries

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3 UN Plaza, New York, NY 10017

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IDENTIFYING FISCAL SPACE

Options for Social and Economic Development for Children and Poor Households in 182 Countries

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JEL Classification: F35, H12, H2, H5, H6, H62, H63, I38, O2, O23
Keywords: fiscal space, fiscal consolidation, public expenditures, social spending, crisis recovery, development policy, equity, tax revenues, foreign reserves, official development assistance, government borrowing, debt, expansionary fiscal and monetary policy

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ACKNOWLEDGEMENTS

This study would not have been possible without substantive comments and contributions from colleagues and partners worldwide. The authors would like to thank the following persons in particular (by alphabetical order): Roberto Benes (Regional Adviser on Social Policy, UNICEF Regional Office for the Middle East and North Africa), Anis Chowdhury (Senior Economic Affairs Officer, United Nations Department of Economic and Social Affairs), Michael Clark (Interregional Adviser, United Nations Conference on Trade and Development), Degol Hailu (Economic Policy Advisor, United Nations Development Programme), Gail Hurley (Policy Specialist, United Nations Development Programme), Gabriele Koehler (Visiting Fellow, University of Sussex), Lisa Kurbiel (Senior Social Policy Specialist, UNICEF Mozambique), Fatou Lo (Programme Specialist, United Nations Women), Alberto Minujin (Professor, New School), Oscar Ugarteche (Senior Researcher, National Autonomous University of Mexico), Rolph van der Hoeven (Professor of Employment and Development Economics, Erasmus University), Matías Vernengo (Associate Professor, University of Utah) and Richard Wolff (Professor of Economics Emeritus, University of Massachusetts, Amherst). Special thanks also to Richard Morgan, Director of Policy and Practice, UNICEF, for his guidance and comments.

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Table of Contents

Page

Executive Summary....vi
Résumé Analytique....vii
Resumen Ejecutivo....viii
1. Introduction: Fiscal space exists even in the poorest countries....1
2. Re-prioritizing Public Sector Spending....5
3. Increasing Tax Revenues....7
3.1. Tariffs....8
3.2. Consumption/sales taxes....10
3.3. Income taxes....12
3.4. Corporate taxes....13
3.5. Natural resource extraction taxes....14
3.6. Other taxes....15
4. Increased Aid and Transfers....16
4.1. More North-South transfers: Official Development Assistance (ODA)....17
4.2. South-South transfers....20
4.3. Curtailing South-North transfers....22
4.4. New international sources of development finance....24
5. Using Fiscal and Foreign Exchange Reserves....25
5.1. Fiscal reserves....25
5.2. Central bank foreign exchange reserves....28
6. Borrowing and Debt Restructuring....30
6.1. Borrowing....31
6.2. Debt restructuring....33
7. A More Accommodating Macroeconomic Framework....38
7.1. More accommodative fiscal policy....38
7.2. More accommodative monetary policy....40
8. Concluding Remarks....43
Annex. Selected Fiscal Space Indicators for 182 Countries....45
References....50

Boxes

Box 1. Identifying Fiscal Space: How to use the Annex ... 3
Box 2. South-South Cooperation in Guinea-Bissau ... 21
Box 3. When Resources and Poverty Abound: The Paradox of Timor-Leste ... 27
Box 4. Debt Repudiation: Iraq and Iceland ... 37
Box 5. Debt Audits: The Case of Ecuador ... 37
Box 6. The Need for an International Debt Work-out Mechanism ... 37

Tables

Table 1. Developing Countries that Lowered Taxes for Top Income Brackets, 2009 ... 12
Table 2. Aid Concentration and Neglect, 2005-09 ... 18
Table 3. Net Transfer of Financial Resources to Developing Economies, 1998-2010 ... 23
Table 4. Sovereign Wealth Funds based on Fiscal Reserves in Selected Countries, 2011 ... 26
Table 5. Foreign Exchange Reserve Adequacy by Developing Region, 2011 ... 29
Table 6. Real Fiscal Deficits and Health Spending in 35 Sub-Saharan African Countries, 2011 ... 39
Table 7. Safe Inflation Thresholds for Developing Countries ... 41
Table 8. Developing Countries with Low Inflation Rates, 2011 ... 42

Figures

Figure 1. Total Government Expenditures in Selected Countries, 2011 ... 2
Figure 2. Military and Health Spending in Selected Developing Countries, 2006-09 ... 5
Figure 3. Tariff Rates by Country Income Groupings, 1996-2009 ... 9
Figure 4. Taxes on Goods/Services and Overall Tax Revenue by Income Groups, 2000-09 ... 11
Figure 5. ODA and Health Spending in Selected Countries, 2007-09 ... 19
Figure 6. Use of ODA in Sub-Saharan Africa, 1999-2005 ... 19
Figure 7. Illicit Financial Flows versus Official Development Assistance, 2000-09 ... 23
Figure 8. Assets under Management by Sovereign Wealth Funds, 2000-12 ... 25
Figure 9. Foreign Exchange Reserve Accumulation by Developing Region, 1993-2011 ... 28
Figure 10. Public Bonds by Developing Regions, 1980-2009 ... 32
Figure 11. Possible Borrowing Candidates, 2009 ... 33
Figure 12. Debt and Health Spending, 2007-09 ... 34
Figure 13. Poor Country Debt at a Glance ... 35
Figure 14. Fiscal Surplus and Health Spending, 2011 ... 40

Executive Summary

It is often argued that social and economic investments that benefit children and poor households are not affordable or that government expenditure cuts are inevitable during adjustment periods. But there are alternatives, even in the poorest countries.

This working paper offers an array of options that can be explored to expand fiscal space. These include: (i) re-allocating public expenditures, (ii) increasing tax revenues, (iii) lobbying for increased aid and transfers, (iv) tapping into fiscal and foreign exchange reserves, (v) borrowing and restructuring existing debt, and/or (vi) adopting a more accommodative macroeconomic framework. To serve as a general advocacy resource, the annex provides a summary of the latest fiscal space indicators for 182 countries.

The need to increase fiscal space for social and economic investments has never been greater. Just at a time when populations are most in need of public assistance, fiscal contraction is intensifying and spreading quickly across the developing world. Given the significance of public investment in enhancing the prospects for equitable, inclusive economic growth and social development, including the achievement of the Millennium Development Goals (MDGs), it is critical that governments explore options to ramp up social spending and employment-generating economic investments during—and in support of—the recovery.

All of the fiscal space options described in this paper are supported by policy statements of the United Nations and international financial institutions. Each country is unique, and fiscal space options should be carefully examined—including the potential risks and trade-offs associated with each opportunity—at the national level and considered in an inclusive dialogue of alternatives to ensure a Recovery for All, including children and poor households.

Résumé Analytique

On fait souvent valoir que les investissements sociaux et économiques qui profitent aux enfants et les ménages pauvres sont très couteux ou que des réductions de dépenses du gouvernement sont inévitables pendant les périodes d'adaptation. Mais il existe des alternatives de dépenses, même dans les pays les plus pauvres.

Ce document de travail expose un certain nombre de grands domaines qui peuvent être explorés pour étendre l'espace budgétaire. Il s'agit notamment: (i) de la réaffectation des dépenses publiques, (ii) de l'augmentation des recettes fiscales, (iii) puisant dans les réserves fiscales et réserves de change, (iv) du lobbying pour une aide accrue et les transferts, (v) de l'emprunt et restructuration de la dette existante, et / ou (vi) de l'adoption de politiques budgétaires expansionnistes et monétaires. En outre, pour servir de ressource pour la sensibilisation et le plaidoyer, l'annexe fournit un résumé des derniers indicateurs sur l'espace budgétaire dans 182 pays.

La nécessité d'accroître l'espace budgétaire pour les investissements sociaux et économiques n'a jamais été aussi grande. Juste au moment où les populations ont le plus besoin de l'assistance publique, la contraction fiscale s'intensifie et s'étend rapidement à travers le monde en développement. Étant donné l'importance des investissements publics dans l'amélioration des perspectives d'équité, de la croissance économique inclusive, du développement social, y compris la réalisation des Objectifs du Millénaire pour le développement (OMD), il est absolument essentiel que les gouvernements explorent les options possibles pour faire décoller les dépenses sociales et l'emploi, tous deux générateurs d'investissements économiques au cours de la reprise

Toutes les options d'espace fiscal décrit dans ce document sont soutenues par les déclarations officielles des Nations Unies et des institutions financières internationales. Chaque pays est unique, et les options d'espace fiscal devraient être soigneusement examinées (y compris les risques potentiels et les compromis associés à chaque option) au niveau national et pris en compte au cours du dialogue inclusif d'alternatives pour assurer une reprise pour tous les enfants et les ménages pauvres.

Resumen Ejecutivo

Frecuentemente se dice que las inversiones sociales no son asequibles, o que los recortes del gasto público son inevitables durante períodos de ajuste. Pero sí que existen alternativas, incluso en los países más pobres.

Este informe describe distintas opciones alternativas para aumentar el espacio fiscal: (i) la reasignación del gasto público, (ii) el aumento de distintos impuestos, (iii) la utilización de reservas fiscales y reservas internacionales acumuladas, (iv) el aumento de la ayuda al desarrollo y las transferencias, (v) el endeudamiento y reestructuración de la deuda existente, y (vi) la adopción de políticas de expansión fiscal y monetaria. Como útil para la defensa del espacio fiscal para los derechos de los niños, el anexo presenta un resumen de los últimos indicadores de espacio fiscal en 182 países.

La necesidad de aumentar el espacio fiscal para las inversiones sociales y económicas nunca ha sido mayor. Justo en el momento en que las poblaciones están más necesitadas de asistencia pública, muchos gobiernos están contrayendo el gasto público. Dada la importancia de la inversión pública en la mejora de las perspectivas de crecimiento económico inclusivo y el desarrollo social, y el logro de los Objetivos de Desarrollo del Milenio (ODMs), es absolutamente fundamental que gobiernos exploren opciones para incrementar el gasto social y las inversiones económicas que generen empleo, especialmente durante la recuperación.

Todas las opciones de espacio fiscal descritas en este artículo están apoyadas por las instituciones financieras internacionales y las Naciones Unidas. Cada país es un caso diferente, las opciones de espacio fiscal se deben examinar cuidadosamente mediante un diálogo nacional de las distintas alternativas para asegurar una recuperación para todos, incluidos niños y hogares pobres.

1. Introduction: Fiscal space exists even in the poorest countries

It is often argued that social and economic investments that benefit children and poor households are not affordable or that government expenditure cuts are inevitable during adjustment periods. But there are alternatives, even in the poorest countries. Finding fiscal space for critical economic and social investments is necessary for sustained equitable results for children and human development, particularly during downtimes. This rationale is not only based on the complementary effects of human capital to physical capital more generally, but also on the fact that children's deprivations can have irreversible adverse impacts on their future capabilities and, in turn, the prospects of their countries.

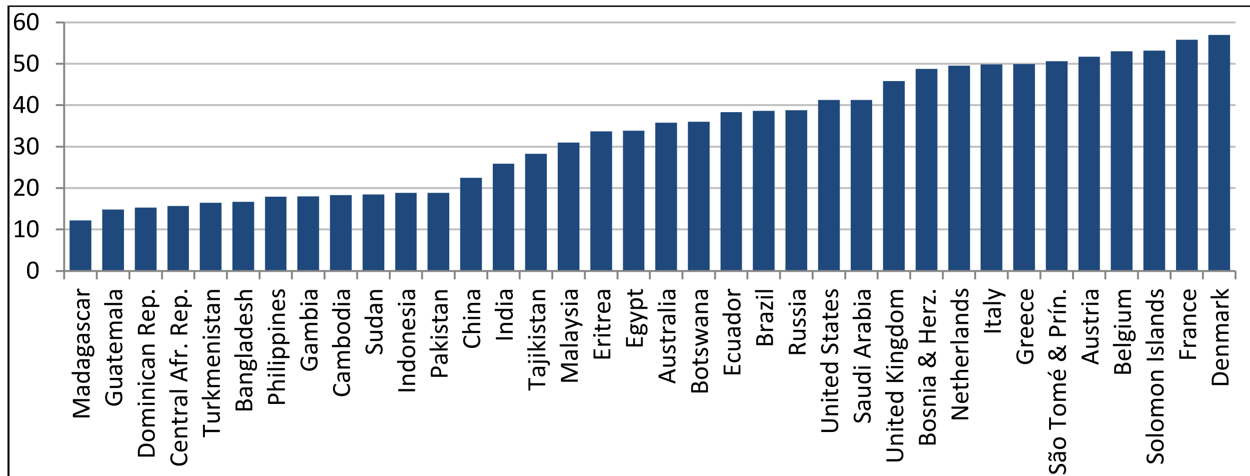
Today, the need to identify fiscal space for social and economic investments has never been greater. Poor children and their families have been hard hit by the unabated wave of food, fuel and employment shocks. Having exhausted available coping mechanisms, they are also likely to be disproportionately affected by reduced public support as well as the different cost-cutting measures that governments are undertaking. UNICEF's latest analysis (Ortiz et al. 2011a) finds that the scope of spending contraction is increasingly widespread and excessive, with total government expenditure expected to fall below pre-crisis levels during 2010-12 in many developing countries.

The increasing prevalence of expenditure contraction reflects the common perception that fiscal space has largely diminished in poor countries due to lower revenue and rising debt. However, this view is limiting and counterproductive because fiscal space is not just financing that is readily available today, but also the dynamic outcome of policy actions and reforms that governments may aggressively pursue for resource mobilization. In this sense, it is feasible to find fiscal space even in the poorest countries for increased social spending and economic investments.

To start, it is important to understand that government spending and revenue choices vary widely across the globe. For example, total public expenditure in Australia is expected to reach 35 percent of GDP in fiscal year 2011 compared to nearly 60 percent in Denmark, another high-income country (Figure 1). As in spending decisions, there is a similar disparity in how governments raise resources for social and economic development. While some governments utilize all possible options, others may not. Indeed, many countries—including some of the poorest—have succeeded in mobilizing significant resources for public investments during downturns. By utilizing all possible options to expand fiscal space and invest in their people, these countries have achieved a virtuous circle of sustained growth and further expansion of fiscal space; they set inspiring examples to others who have been trapped in limited fiscal space, low social investments and weak economic growth. Acknowledging the risks of premature and/or excessive fiscal consolidation, the new Managing Director of the International Monetary Fund (IMF), Christine Lagarde, called for "aggressive exploration of all possible measures that could be effective in supporting short-term growth."[1]

[1] See Financial Times, "Don't Let the Fiscal Brakes Stall Global Recovery," 15 August 2011.

Figure 1. Total Government Expenditures in Selected Countries, 2011
(as a percent of GDP)



Source: IMF's World Economic Outlook (April 2011)

This working paper is intended to serve as a guide for UNICEF staff, governments and development partners to identify possible funding avenues to boost investments in children and poor households today in support of an equitable Recovery for All (UNICEF 2010). It is not meant to be exhaustive, nor does it address the distinct risks and trade-offs that are associated with each of the different options. As such, this paper should be viewed as an overview of fiscal space-enhancing opportunities that are to be further explored at the country level. Given the priority of the United Nations to support human development, this paper ties many of the different options together by making comparisons in health spending in order to illustrate the possible benefits of increasing investments in key human development areas.[2]

The structure is straightforward: each section describes one of six options that are available to governments to expand fiscal space, even in the poorest countries. These different areas are summarized below, all of which are supported by policy statements of the United Nations and international financial institutions:[3]

i. *Re-allocating current public expenditures:* this is the most orthodox option, which includes assessing ongoing budget allocations through public expenditure reviews and thematic budgets, replacing high-cost, low-impact investments with those with larger socio-economic impacts, eliminating spending inefficiencies and/or tackling corruption.

ii. *Increasing tax revenue:* this is a main channel achieved by altering different types of tax rates—e.g. on consumption, corporate profits, financial activities, personal income,

[2] The option of privatizing public assets, services and enterprises is not considered in this paper given the remaining limited scope for privatization in many developing countries and the potential problems associated with earlier privatizations, namely, the loss of future revenues and the lack of extension of coverage of services, as well as the general absence of results to provide more affordable services.
[3] See, for example, Development Committee (2006), Roy et al. (2007), IMF (2009), United Nations (2009a), UNICEF (2009), ILO (2010), UNDP (2010), UNESCO (2010) and WHO (2010).

property, imports or exports, etc.—or by strengthening the efficiency of tax collection methods and overall compliance.

iii. *Increased aid and transfers:* this requires either engaging with different donor governments in order to ramp up North-South or South-South transfers, or reducing South-North transfers, such as illicit financial flows.

iv. *Using fiscal and central bank foreign exchange reserves:* this includes drawing down fiscal savings and other state revenues stored in special funds, such as sovereign wealth funds, and/or using excess foreign exchange reserves in the central bank for domestic and regional development.

v. *Borrowing or restructuring existing debt:* this involves active exploration of domestic and foreign borrowing options that are at low costs, if not concessional, following a careful assessment of debt sustainability. For those countries at high debt distress, restructuring existing debt may be possible and justifiable if the legitimacy of the debt is questionable and/or the opportunity cost in terms of worsening deprivations of children and other vulnerable groups is high.

vi. *Adopting a more accommodating macroeconomic framework:* this entails allowing for higher budget deficit paths and higher levels of inflation without jeopardizing macroeconomic stability.

The uniqueness of each country requires that fiscal space options be carefully examined at the national level and fully explored in an inclusive dialogue of recovery alternatives. A good starting point for country level analysis may be a summary of the latest fiscal space indicators, which is provided in the Annex for 182 countries and offers a general overview of which funding possibilities may or may not be potentially feasible for a given country. Box 1 illustrates how a rapid fiscal space analysis could be performed.

Box 1. Identifying Fiscal Space: How to use the Annex

The Annex provides a snapshot of different fiscal space indicators for 182 countries and can be used as a resource to carry out a rapid analysis of resource options that may be available to a particular government. It is important to note that the Annex only serves as a reference starting point. It is therefore critical to acquire the latest available figures, as well as projections, for relevant indicators and to perform in-depth analysis and outcome assessments for all possible scenarios. Moreover, such exercises should be carried out in consultation with development partners and key stakeholders.

The data below are extracted from the Annex and represent examples of two developing countries from different continents: Bangladesh and Guatemala. Examination of their different fiscal space indicators reveals numerous possibilities to boost social and economic investments today.

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010	(v) External debt (% of GNI)		(vi) Inflation, 2011
	Total	Health	Educ.	Military	Total	Tax			Service	Total	
Bangladesh	14.5	1.1	2.4	1.1	10.5	8.6	1.4	10.1	1.0	24.0	7.6
Guatemala	14.2	2.6	3.2	0.4	11.1	10.4	1.0	13.6	4.7	38.8	5.1

Source: Annex (all figures in percent of GDP for 2009, unless otherwise noted)

i. In terms of government spending, military expenditures in Bangladesh equal total public investments in health, suggesting that a reallocation of current spending is an area for further analysis. In the case of Guatemala, deeper examination of the budget is required to understand the distributional impacts of current allocations, to determine whether more effective investments can be introduced to try to reduce different spending inefficiencies (see Section 2).

ii. In terms of overall government revenue, Guatemala and Bangladesh have the second and third lowest levels of the 182 countries with data, respectively. The revenue fiscal indicator thus indicates that deeper investigation of tax codes and collection methods is warranted in both countries, as well as improving other revenue streams or identifying new ones (see Section 3).

iii. At just over one percent of GDP, levels of official development assistance (ODA) in Bangladesh and Guatemala point to ample scope to lobby for increased aid and transfers. As a first step, these governments could develop an enhanced aid strategy tailored to bilateral partners. Both countries could also explore possible tactics to enhance development cooperation with other strategic emerging donor countries (e.g. China and India in the case of Bangladesh; Mexico and Venezuela in the case of Guatemala), as well as estimate the size of illicit financial flows to evaluate whether policy changes could garner additional resources for development (see Section 4).

iv. The limited availability of data inhibits an assessment of fiscal reserves as a potential source for either country, and further investigation is required. In terms of foreign exchange reserves, both Bangladesh and Guatemala appear to be holding significant reserves in their central banks, thus warranting deeper analysis on the rationale of this policy, on the potential use of reserves as investment guarantees, on options of gaining higher investment returns in order to create new government revenue, and/or on direct loans for strategic domestic businesses (see Section 5 for more details including implied impact on the money supply or debt).

v. Regarding external debt, Guatemala's annual service payments approach five percent of GDP, which equals the total spent on education and health combined, suggesting that strategies to lower payments through restructuring or through some form of innovative debt swap arrangement may be worth exploring. Bangladesh's moderate levels of external debt, on the other hand, point to a ready option of additional borrowing, such as concessional or commercial lending or issuing government securities (see Section 6).

vi. Between 5-8 percent, both countries have relatively safe levels of inflation and may have room for expansionary monetary policy, if warranted. It would, however, be prudent to analyze other options first (see Section 7).

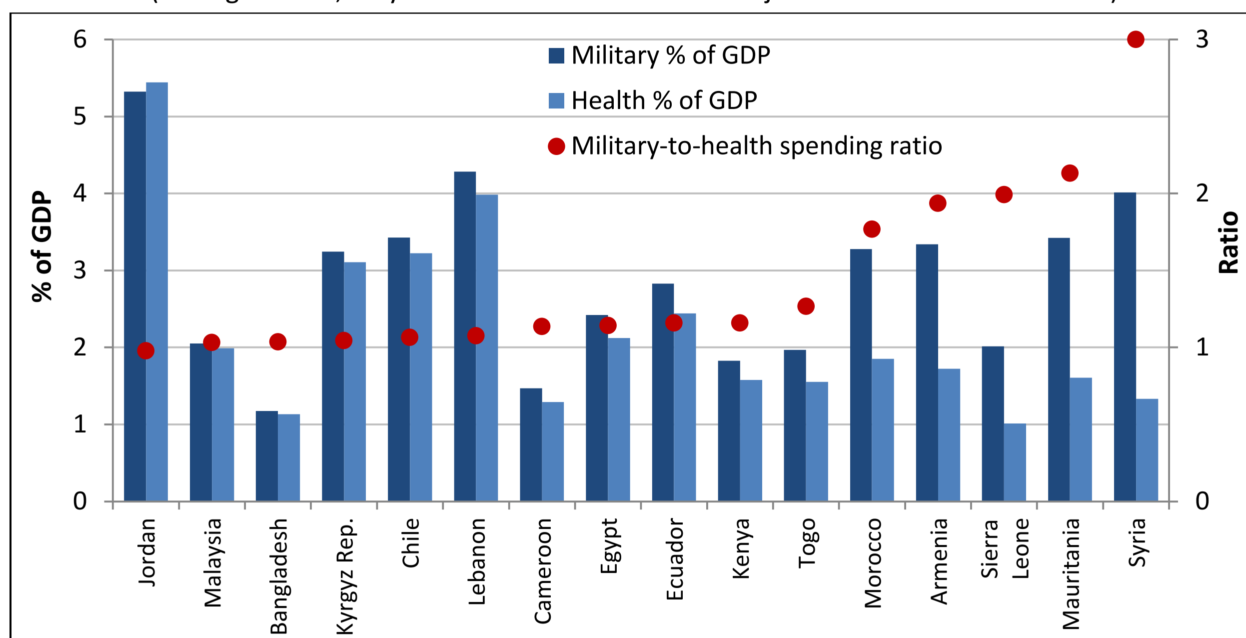
In sum, this rapid analysis identifies preliminary areas that can be further examined in order to boost investments in social and economic development today, even in the poorest countries.

2. Re-prioritizing Public Sector Spending

Rethinking sector-specific allocations within existing budgets is one strategy to increase social expenditures. We start with this option since it is normally the first to be considered. However, based on experiences from the 1990s and early 2000s, the re-prioritization of public spending has proven to be a contentious and difficult approach to fight for increased investments in poor households and children. This reflects the underlying assumption that no extra resources are available and, therefore, other sectors or subsectors must be reduced in order to allow for increased social investments—these sectors often represent important vested interests in a country. In other words, this approach presumes that the budget is fixed and a zero-sum game.

The extensive literature on public choice and public finance describes how different interest groups within and outside of government compete to influence public policies and budget allocations (e.g. Buchanan and Musgrave 1999). In cases where social sector ministries and groups representing or comprised of poor and marginalized sectors are incapable of garnering the support of policymakers or of society at large, the result is a collapse in allocations for pro-poor budget items. Moreover, even in situations where there is broad consensus that pro-poor expenditures should be boosted, policymakers often fail to agree on specific sectors to sacrifice (e.g. defense/security, commerce/finance). This debate is often imbalanced. For instance, when arguing that social expenditures may be part of the cause of large deficits, there is little or no debate on the role of military or other essentially non-productive expenditures (Figure 2).

Figure 2. Military and Health Spending in Selected Developing Countries, 2006-09
(average values, only includes countries with no major armed conflict since 2000)



Source: Authors' calculations using World Development Indicators (2011) and Uppsala Conflict Data Program's Armed Conflict Dataset (December 2010)

More importantly, various studies have highlighted the risks of pro-poor budget items being the most affected during budget consolidation (e.g. Cornia et al. 1987, Hicks 1991, Ravallion 2002, 2004 and 2006). Evidence from the recovery period following the debt crisis of the 1980s shows that social sector budgets, on average, received among the highest cuts when governments in Latin America scaled back on expenditures—just behind that of infrastructure budgets and expenditures for industrial and agricultural development, while defense budgets were highly protected (Hicks 1991:33).

Still, there are ways of prioritizing socially-responsive expenditures even when overall budgets are contracting. This re-prioritization requires, first and foremost, that governments have their budget priorities in place. For example, governments in Cambodia and Sri Lanka recently decided to reduce expenditures in the defense and security sectors in favor of increased spending in social sectors.[4] The political and technical challenges of identifying sectors/subsectors that can be reduced to promote fiscal space can be overcome through the following strategies (see Ortiz 2008a for further details):

- *Re-prioritizing through Public Expenditure Reviews (PERs) and thematic budgets*. These are well-developed approaches to public financial management that bring evidence and rationality to public policy-making by showing the distributional impacts of current budgetary allocations. A common exercise is to examine budgets from a child and/or gender perspective. Given that children and youth comprise nearly half of the population of many developing countries, as do females, public budgets should support these groups proportionally.

- *Replacing high-cost, low-impact investments*. Whether or not these investments are in social sectors, all new public investments can be re-examined. For instance, the social impact of a cardiology center in a national capital tends to be small and carries a high operational cost. Rural or slum area health interventions, conversely, tend to have much larger positive social impacts. To offer an example in the energy sector, the opportunity cost of building a nuclear power plant is usually very high when compared to investing in rural electrification systems that serve poorer populations. Similar trade-offs exist in the water and sanitation sectors. Public debates that include relevant stakeholders and civil society organizations are one strategic tool to replace high-cost, low-impact interventions, which can help to minimize the possible influence of powerful lobbying groups on public policy-making.

- *Eliminating inefficiencies*. Although linked to the previous point, deeper analysis of sector investments is required to eliminate inefficiencies. In particular, the overall cost-effectiveness of a specific programme or policy should be impartially evaluated according to various factors, including: (i) coverage (beneficiaries and benefits); (ii) total cost (as a percentage of GDP, public expenditure and sector expenditure); (iii) administrative costs (as a percentage of total costs and how the costs compare with other programmes—for

[4] See IMF country report No. 11/45, February 2011 and IMF country report No. 10/333, October 2010.

example, means-testing targeting is typically expensive); (iv) long-term social benefits and positive externalities; and (v) opportunity cost (how this policy/programme compares to alternatives). Making sector allocations more efficient also involves strengthening supervision and inspection as well as reducing other leakages, especially corruption (see below).

- *Fighting corruption*. Corruption can also be a significant source of waste and inefficiencies within sector budgets. This most commonly affects extra-budgetary accounts (where there is less transparency), the selection of investment projects, and the procurement of goods and services (overpriced or simply inexistent, such as "ghost" local investments or workers). Tackling corruption requires strategies that address both supply and demand factors, and, ultimately, strengthening transparency and good governance practices can increase the availability of resources for social and economic development.[5]

Nonetheless, while reducing inefficiencies is the most commonly used strategy since it avoids political tensions, **expenditure reforms take time** to advance and are unlikely to yield significant, immediate resources for social and economic recovery in the near term. In addition, expenditures aimed at social and economic recovery may be increased slightly, but their relative weight vis-à-vis other forms of investment may be too small to ensure a Recovery for All, including children and poor households. Thus, while the re-prioritization of public sector spending may be a good starting point to expand fiscal space, other options should also be examined.

3. Increasing Tax Revenues

Increasing tax compliance and/or raising tax rates are potential strategies to mobilize additional public resources without necessarily sacrificing other spending priorities. Moreover, new taxes, when well designed and executed, improve government revenues without increasing debt.[6] Aside from strengthening a country's overall fiscal position, new tax revenue can potentially support equity objectives, especially in situations of widespread disparities. For example, if income tax rates are increased among the richest groups of a country (known as progressive taxes), additional revenues can be generated and invested in the poorest households, which promotes poverty-reducing economic growth and sustains growth in the long run.

There are many types of taxes. Some of the most common include: consumption or sales taxes (e.g. on goods and services or on any operation that creates value; these are applied to

[5] Specific strategies to address corruption are widely documented by international agencies and development partners. See, for example, the United Nations, Transparency International and the World Bank.

[6] It is important, however, to carefully scrutinize the risks of reforms involving changes to tax rates. Some of the main arguments against raising taxes include the potential of: (i) *political risks* (higher income or business taxes are unpopular and can reduce the support of influential voters and campaign contributions); (ii) *inflation* (higher taxes on products are often passed on to consumers); and (iii) *increasing poverty* (higher sales taxes, such as through VATs, absorb a higher percentage of the income of the poor).

everybody), corporate taxes (applied to businesses), income taxes (e.g. on persons, corporations or other legal entities), inheritance taxes (applied when a person dies), property taxes (e.g. applied to owners of private property), social security taxes (applied to the wages/salaries of formal workers to provide income and health benefits to retirees), tariffs (e.g. taxes levied on imports or exports) and tolls (e.g. fees charged to persons traveling on roads, bridges, etc.).

In recent history, increasing progressive taxation from the richest income groups to finance social and pro-poor investments has been uncommon. This is largely the result of the wave of liberalization and de-regulation policies that swept across most economies beginning in the early 1990s. These led many developing countries to offer tax breaks and subsidies to attract foreign capital, as well as to scale back income taxes applied on wealthier groups and businesses to further encourage domestic investment. Moreover, to counter the revenue losses associated with these tax policies, many countries levied different consumption taxes.

The tax policy framework associated with liberalization and de-regulation continues to typify most governments today. Contrary to progressive, equity-based policies, many current tax regimes may be characterized as regressive in that they take a larger percentage of income from poor households than rich households. In particular, a large number of governments rely heavily on value-added taxes (VATs) for revenues, which tend to weigh most heavily on the poor since they spend a higher share of their income on basic goods and services when they are not exempted. In light of this reality, it is imperative that distributional impacts are at the forefront of tax policy discussions—across income groups, regions, gender and age.

In the present context, and given the urgency to increase fiscal space for equitable development, the United Nations and other international organizations are working with many developing country governments to boost tax revenues. For example, Ortiz et al. (2011a) review of the latest IMF country reports indicates that tax reforms are being undertaken in virtually all developing countries during 2011. Indeed, efforts to develop collection capacities and broaden the tax base are to be applauded, especially those aimed at cracking down on evasion, which has been estimated to result in annual revenue losses of US$285 billion for developing countries as a whole (Cobham 2005). Strengthening domestic tax and collection systems can also foster good governance by enhancing citizen-state dialogue on how taxes are spent, as well as increase incentives to pay taxes, thereby enforcing accountability and creating a demand for greater provision of public services (Brautigam et al. 2008).

The following considers six broad tax categories that governments can adjust to increase revenue streams, which include tariffs, consumption/sales taxes, income taxes, corporate taxes, natural resource extraction taxes and other taxes that use more innovative approaches.

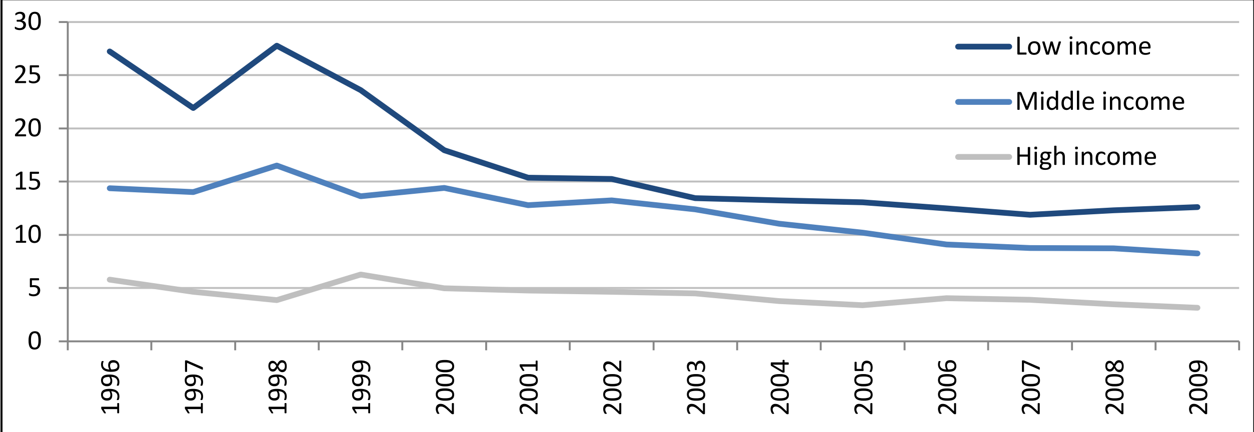
3.1. Tariffs

By some measures, developing countries appear to have steadily reduced tariff rates since the 1990s, implying lowered capacity to generate revenues from trade. The financial implications of

this trend are likely greater for low-income countries, which sliced tariffs by more than half from 27 to 13 percent between 1996 and 2009, on average, compared to a six percent average cut in middle-income countries (Figure 3). Some countries stood out, with India's average tariff rate falling from 71 to 13 percent between 1994 and 2009 and Brazil's from 51 to 14 percent between 1987 and 2009 (WTO 2010).

Figure 3. Tariff Rates by Country Income Groupings, 1996-2009*

(in percentage points)



Source: World Development Indicators (2011)

* Values reflect unweighted average of applied rates for all traded products subject to tariffs

Such declines in tariff revenue have at times been associated with trade liberalization. In theory, the overall gains to free trade were supposed to outweigh the loss of tariff revenues, but, in practice, less developed countries tend to have limited ability to recover foregone revenues, which results in net revenue losses. For example, Baunsgaard and Keen (2005) find that while rich countries have been able to offset reductions in tariff revenues by increasing their domestic tax revenues, this has not occurred in most developing countries. Middle-income countries were found to recover only up to 60 cents of each dollar of tariff revenue lost, and low-income countries recovered no more than 30 cents.

Consequently, in many developing countries there may be a good rationale to examine current tariff levels, at least until domestic tax collection mechanisms are strengthened, to sustain or increase levels of revenue. In countries such as Brazil and India, there may be ample scope to raise tariffs since prevailing levels are far below the WTO-bound tariff rate ceilings agreed to in the 1995 Uruguay Round of trade negotiations (Gregory et al. 2010).

Moreover, for countries undergoing export-driven commodity booms, fiscal space could be enhanced for social investments by introducing or raising export tariffs. In many Latin American countries, for instance, special funds and laws have been created to govern the use of revenue derived from price increases in commodities exports (Gallagher and Porzecanski 2009). One of the most well-known examples is Venezuela, where an increasingly progressive windfall tax is

levied on oil exports to fund social development projects.[7] To highlight the overall potential of commodity export taxes, we estimate that a 2-5 percent tax on oil exports from petroleum-exporting developing countries could generate anywhere from US$40 billion to US$102 billion in additional resources to support economic and social investments in children and poor households during 2012.[8]

3.2. Consumption/sales taxes

By some accounts, many developing countries have introduced more consumption or sales taxes, such as VATs, over the past decade. According to the World Development Indicators, between 2000 and 2009, the overall share of consumer-related taxes increased by over one percent in low-income countries and by 3.2 percent in middle-income countries, on average, in terms of total revenue, while this share slightly declined in higher income economies (Figure 4). Within the cohort of developing countries, it also appears that these new taxes have been a source of a steady increase in overall tax revenues.[9] While there is limited data for developing countries prior to 2000, which likely hides much of the marked increase, available data show that the contribution of new consumption taxes to overall revenue increased from around ten percent of GDP in 2000 to 14 percent in 2009 for middle-income countries, on average, with a slightly lower increase for low-income countries.

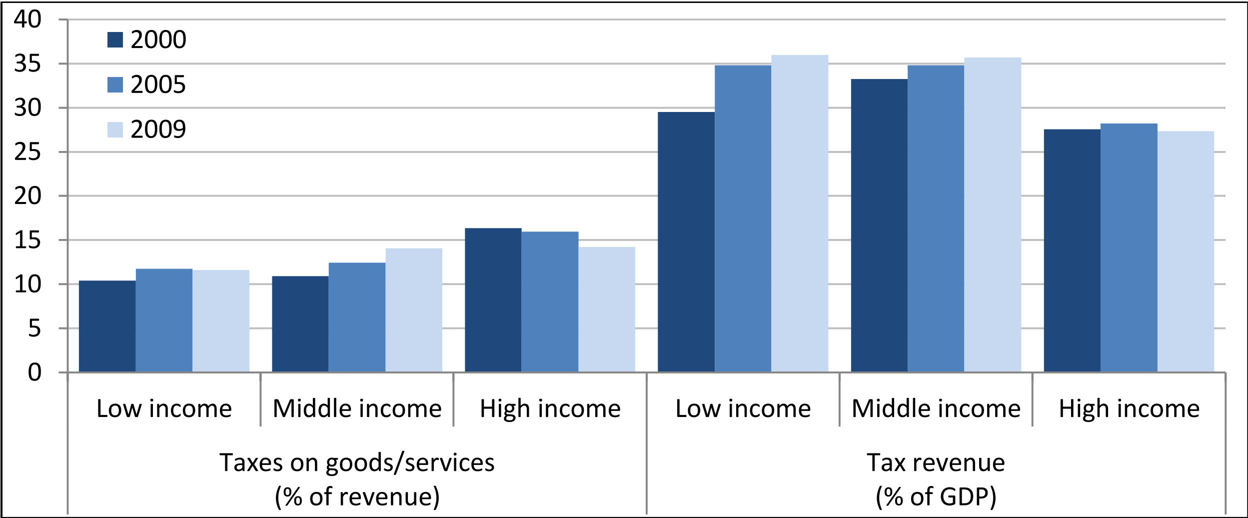
If the distributional impact of such a change in tax policy is not properly addressed, there is the additional concern of worsening inequity by disproportionately shifting the tax burden to families in the bottom income quintiles of society. Contrary to progressive taxes, universal taxes on goods, especially on basic food and household items, can be regressive since they do not discriminate between high-income and low-income consumers. For example, given that poor families spend a higher proportion of their disposable income on food items, applying or increasing consumption taxes on basic food items means that relatively more of their income is subjected to product taxes.

However, as in the other tax measures, levying or increasing consumption taxes or VATs can be a prudent policy objective and strengthen fiscal space if targeted to the products that the better-off consume disproportionately more. For example, it is possible to exempt necessary basic goods that many low-income families depend on while setting higher rates for luxury goods that are principally consumed by wealthier families. In this manner, progressively designed consumption taxes can increase public resources and protect the most vulnerable (see Schenk and Oldman 2001 for discussion). For instance, according to IMF country reports, Antigua and Barbuda is introducing sales tax exemptions for basic commodities, Kenya is

[7] See Taxation News and Information, "Venezuelan Oil Taxes to Reach up to 95%," 26 April 2011.
[8] Estimates reflect the 2009 average barrels per day of oil exports from Algeria, Angola, Iran, Iraq, Kazakhstan, Libya, Nigeria, Russia and Venezuela as reported by the United States Energy Information Administration (combined total of 21.6 million barrels) and the forecasted price of crude oil for 2012 (US$94.5/barrel of Brent crude) according to the Economist Intelligent Unit's Global Forecasting Service (as of August 2011).
[9] This may reflect in part strengthened collection of existing taxes, the extent of which cannot be ascertained due to a lack of consistent data.

lowering taxes on fuel and food staples consumed by vulnerable populations, and the Solomon Islands is reducing taxes on food and fuel items. At the same time, many developing countries also seem to be considering tax increases on luxury items, such as cars, including Costa Rica, Ghana, Kosovo and the Republic of Congo.

Figure 4. Taxes on Goods/Services and Overall Tax Revenue by Country Income Groupings, 2000-09*



Source: World Development Indicators (2011)

* Tax revenue refers to compulsory transfers to the central government for public purposes and does not include social security contributions; Taxes on goods/services include general sales and value added taxes, selective excises on goods, selective taxes on services, and taxes on the use of goods or property, among others

More recently, a review of IMF country reports by Ortiz et al. (2011a) finds that during 2010-2011 no less than 53 developing country governments have adopted or are planning to adopt an increase in general consumption taxes, either through increasing or expanding VAT rates or sales taxes or, alternatively, by removing exemptions. However, the potential ripple effects of this policy change must be carefully examined. First, tax policies that increase the cost of basic goods, such as on food and fuel or energy items, may enhance the vulnerability of poor households by further reducing their already limited disposable incomes. Second, there is a risk of weakening aggregate demand, which is important for solidifying still fragile growth; and third, slowdown in economic growth will likely lower tax receipts and create new budgetary pressures—which is ironically the original impetus for the tax increase.

Another type of consumption tax that can be used to increase fiscal space is an excise tax, which is collected on goods such as beer, cigarettes and petroleum whose consumption creates negative externalities (e.g. the cost of the good does not factor in the negative side effects to third parties or society that result from its consumption). The advantage of increasing so-called "sin" taxes is that they may be more politically acceptable, especially if the revenue is directed towards social expenditure. Based on current tax proceeds, WHO (2009a) estimates that a 5-10 percent increase in the tobacco tax rate could net up to US$1.4 billion per annum in additional revenue in low-income countries and US$5.0 billion in middle-income countries; raising tobacco

taxes by 50 percent could cover nearly half of public health expenditures in a number of developing countries. Given the public health spillovers and revenue potential associated with new or higher "sin" taxes, many governments appear to be considering this option in the current policy environment, including Antigua and Barbuda, Jamaica, Kyrgyz Republic, Liberia, Republic of Congo and Turkey, according to IMF country reports.

3.3. Income taxes

In contrast to taxes on goods and services, income taxation is often progressive—that is, people in higher income brackets pay higher tax rates than those in the bottom. According to the World Development Indicators data, with the exception of Eastern Europe and Central Asia along with Sub-Saharan Africa, developing countries have, on average, increased personal and corporate income taxes, as well as those levied on capital gains, since 2001. The rise in various income taxes is likely to have led to enhanced revenue streams for most developing country governments.

However, this progressive trend hides important disparities within income tax policies. In particular, a number of developing countries have reduced income tax rates on the wealthiest groups (Table 1). In terms of individual income taxes, 12 of the 39 countries with data (or 31 percent of the sample) had lowered the tax rates applied to the highest income earners in 2009 when compared to the 2005-08 period. Of the 71 developing countries that offer corporate income tax data, 33 (or nearly half) had reduced the tax rate applied to the top income bracket in 2009 when compared to previous years. For these countries, expanding the income tax base through more efficient collection, especially through eliminating evasion, or by decreasing the income required to qualify for higher tax brackets, could increase available fiscal space over the short term.

Table 1. Developing Countries that Lowered Individual and Corporate Income Tax Rates for the Top Income Brackets, 2009*

Individual Income Tax	Corporate Income Tax		
Bulgaria	Albania	Ghana	Romania
Colombia	Bangladesh	India	Russian Federation
Egypt	Bosnia & Herzegovina	Indonesia	Serbia
Indonesia	Bulgaria	Kazakhstan	South Africa
Kazakhstan	China	Kenya	Swaziland
Lithuania	Colombia	Macedonia	Thailand
Malaysia	Costa Rica	Malaysia	Tunisia
Mauritius	Côte D'Ivoire	Mauritius	Uganda
Mexico	Dem. Rep. of Congo	Mexico	Venezuela
Pakistan	Dominican Republic	Papua New Guinea	
Papua New Guinea	Ethiopia	Peru	
Viet Nam	Fiji	Philippines	

Source: Authors' calculations using World Development Indicators (data extracted on 15 January 2010)

* A country is included if its highest marginal tax rate in 2009 was lower than the 2005-08 average rate

Furthermore, there is an urgent need to introduce increasingly progressive income taxes to counter current trends in inequity. The large income inequalities that characterize most developing countries—especially middle-income countries—are being exacerbated during 2011 due to persistently high unemployment, rising food and fuel prices, and lower government spending patterns, all of which have a disproportionate, negative impact on the bottom quintiles (Ortiz and Cummins 2011:33-36). As a result, income taxes—which are the principal redistribution tool available to policymakers—should be examined on both fiscal space and equity grounds in order to enlist the political support of citizens, safeguard children's lives, nutrition and basic education, and engender social stability.

3.4. Corporate taxes

Increasing business taxes is another possible strategy to generate additional fiscal revenues. Developing countries across all regions decreased commercial tax rates, on average, between 2005 and 2010. Eastern Europe and Central Asia along with the Middle East and North Africa underwent the largest reductions according to data from the World Bank (World Development Indicators 2011). East Asia and the Pacific, Latin America and Sub-Saharan Africa also lowered commercial tax rates by 3-5 percent, on average, over the same time period.[10]

The logic behind lowering corporate taxes and related license costs and fees was to encourage entrepreneurial risk-taking and generating new economic activity. However, the potential tradeoff needs to be carefully balanced, to ensure that the gains from increased economic activity do not come at the expense of foregone essential investments for human and social development. This may be particularly important in those countries that have undergone major reductions—e.g. Belarus, Georgia, Mauritania, Sierra Leone, Timor-Leste and Uruguay, all of which reduced commercial tax rates by more than 25 percent between 2005 and 2010—as well as those that have among the world's lowest commercial tax rates—e.g. Georgia, Kosovo, Macedonia, Maldives, Namibia, Vanuatu, Timor-Leste and Zambia, all of which had commercial tax rates under 17 percent as of 2010.[11]

The former logic is being questioned in many countries following the global financial crisis, particularly related to the financial sector. Different financial sector tax schemes may offer another possible revenue stream for stepped up social investments, provided that their impact on financial sector development is carefully evaluated. Many countries are considering special taxes on the profits and remuneration of financial institutions. For instance, Turkey taxes all receipts of banks and insurance companies, and, in the United Kingdom and France, all bonus payments in excess of €25,000 were taxed by 50 percent (IMF 2010a). Another example is a bank debit tax in Brazil, which charged 0.38 percent on online bill payments and major cash withdrawals; before its discontinuation in 2008, it raised an estimated US$20 billion per year and financed healthcare, poverty alleviation and social assistance programmes. And Argentina operates a 0.6 percent tax on purchases and sales of equity shares and bonds, which, in 2009

[10] Authors' calculations using World Development Indicators (2011).
[11] Ibid.

accounted for more than ten percent of overall tax revenue for the central government (Beitler 2010).

In addition to altering corporate tax rates, governments can also increase fiscal space by taking concerted actions to minimize tax evasion and/or aggressive avoidance of taxes on the part of large companies. Transnational corporations, in particular, commonly shift profits and losses around so that they are recorded in different jurisdictions in order to minimize overall tax liabilities. Such practices are difficult to track, but estimates suggest that total lost revenues could amount to US$50 billion per year among developing countries (Cobham 2005). Proposals have been put forward to increase the transparency of transnational corporations and hold them accountable for their tax obligations, such as reporting profits, losses and taxes paid in each location where the company does business (see Kar 2011 for details).

3.5. Natural resource extraction taxes

Developing countries that rely on non-renewable natural resources as a main source of wealth should consider applying extraction taxes or introducing specific windfall taxes to support social and economic development initiatives. In terms of finite assets, including energy, minerals and forests, governments face a limited window of opportunity to use these for national development aims. There are also significant environmental and social externalities associated with natural resources, such as the impacts on local communities, which, if not adequately addressed, serve as a subsidy to extracting companies and further distort the true cost of development.

A government may raise revenues either by extracting the natural resources through a state-owned enterprise or by selling off the exploitation rights and taxing the profits, both of which can provide significant revenues for social and economic development. Regarding the former, a number of countries have effectively managed their natural resources through public companies, including Botswana (diamonds), Brazil (oil), Indonesia (oil and gas) and Malaysia (forestry, tin, oil and gas) (Chang 2007). In terms of the latter, ample care must be taken to find the right types of contracts, including licenses, joint venture, production-sharing arrangements, etc. (Radon 2007). While Norway's approach of taxing oil profits and storing the revenues in the Petroleum Fund (now called the Government Pension Fund Global) is perhaps the best-known case, developing countries offer several innovative examples of channeling natural resource revenue streams for social development. In Peru, for example, the government recently expanded taxes levied on the mining sector whose proceeds are being invested into health and education programmes.[12]

Given the volatile nature of primary commodity prices, many governments have created "stabilization funds" based on windfall taxes. Such funds allow governments to smooth their income and expenditure, keeping savings in years of bonanza for "rainy days" when prices of

[12] See Peruvian Times, "Peru Organization Says New Mine Tax to Make Important Dent in Social Breaches," 30 August 2011.

commodity exports may be low, and hence ensuring that investments in social and economic development remain constant. Chile's Copper Stabilization Fund, Iran's Oil Stabilization Fund, Papua New Guinea's Mineral Resources Stabilization Fund and the Stabilization Fund of the Russian Federation stand as examples. During the recent economic downturn, a number of countries have accessed these "rainy day" funds to finance stimulus measures and increase social protection.

3.6. Other taxes

Alternative tax options could also help raise public revenues for investments in poor households and children, several examples of which are described below.

- *Property taxes:* Higher real estate and inheritance taxes are a form of progressive levies that require large landowners and wealthier generations to contribute more to government revenues. There are many advantages to such taxes, including fairness, evasion difficulties and an impact on those with assets whose value is increased by public services and infrastructure. In many developing countries, higher property taxes could transform into a robust source of funding for local governments. For example, a 2.5 percent property tax in Thailand is estimated to be able to finance all local government spending (Hall 2010:41). According to the latest IMF country reports, many countries appear to be considering introducing or increasing property or real estate taxes in the current policy environment, including Costa Rica, Kosovo, Russia and St. Lucia. Land taxes are another example, which are a broader form of property tax applied to all land, not just buildings. Campaigns for land taxes have surfaced in many developing countries recently. In Latvia, for instance, a group of economists and other activists argued for the introduction of a land tax as an alternative to deep public spending cuts (Strazds 2010), and there are similar discussions in parts of Southern Africa.

- *Airline and/or hotel taxes:* Many developing countries have recently increased taxes charged at airports or on the sale of airline tickets. As demonstrated in recent IMF country reports, this has been most commonly observed in small island states, like Antigua and Barbuda and the Maldives, as well as in emerging tourist destinations, such as Ghana and Liberia—the latter which increased taxes on airlines and hotels by 3.0 percent in fiscal year 2012.[13]

- *Linking taxes to social programmes*: Another strategy to enhance fiscal space for economic and social development is to tie the revenues raised from new or existing tax measures to the financing of specific social programmes, which can help to secure resources and make them less volatile, as well as ensure wider public support. For example, Mexican lawmakers agreed to raise VATs by one percent (from 15 to 16 percent) and the top income tax rate by two percent (from 28 to 30 percent), as well as to increase taxes on beer producers and on certain bank deposits, with all of the proceeds specifically earmarked to support anti-

[13] See IMF country report No. 11/174, July 2011.

poverty programmes.[14] Ghana has also introduced links between taxes and public services: 2.5 percent of the VAT is reserved for education, another 2.5 percent of the VAT is allocated for social health insurance, and 20 percent of a communication service tax is directed to a national youth employment scheme (Hall 2010:40-41). And in India, an education cess of 2.0 percent is levied on corporate income taxes, service taxes, and excise and customs duties.[15]

- *Remittance taxes*: Some countries have introduced taxes on remittance inflows to support economic and social development. Such tax schemes vary widely. For instance, remittances were subjected to a 0.004 and 0.1 percent tax rate in Colombia and Peru, respectively; a 12 percent VAT was applied to remittances in Ecuador; Georgia and Poland imposed income tax rates on remittance inflows; and, in the Philippines, banks deducted withholding taxes for interest earned on deposited remittances (de Luna 2006). However, a wide body of literature suggests that lowering transaction costs and even subsidizing remittances may do more social good than taxing inflows and directing the revenue to specific development uses (see, for instance, Inter-American Dialogue 2007, Ratha 2007, Rosser 2008, Barry and Øverland 2010). This conclusion is generally attributed to the following factors: (i) migrants have already paid income and sales tax in the host country on money remitted, (ii) taxes reduce incentives to remit, (iii) taxes lower the value of funds received by poor households, (iv) remittance taxes encourage informal transfers and financial exclusion, (v) countries with overvalued official exchange rates already implicitly tax remittances by requiring recipients to convert at uncompetitive official exchange rates, (vi) remittance tax policies are difficult to administer, and (vii) remittance taxes are regressive. As a result, developing countries should look to other options to create fiscal space before considering remittances taxes.

In summary, it is critical to take into account the distributional impacts of tax systems and support tax reforms and tax collection that benefit children and poor households. Sound tax approaches are progressive, broad-based and reliant on multiple sources, especially in middle-income countries.

4. Increased Aid and Transfers

Governments have three main options for increasing net international transfers in order to support socio-economic investments today: (i) lobby for further North-South aid flows, (ii) lobby for additional South-South transfers and development assistance, and (iii) curtail South-North financial flows.

[14] See Reuters, "Mexico Lawmakers Adopt Tax Plan – Raise VAT, Income Tax," 1 November 2009.
[15] See Embassy of India, "Taxation System in India," September 2011.

4.1. More North-South transfers: Official Development Assistance (ODA)

In principle, ODA is a first option for expanding fiscal space for low-income countries in particular. However, there is significant uncertainty surrounding future aid flows in a climate of fiscal consolidation that is increasingly taken hold of many traditional donor countries during 2011.[16] There is also concern over aid commitments more generally. In particular, current aid levels remain far below the 0.7 percent of gross national income (GNI) threshold that was first agreed to by wealthy countries in 1970 and which has been repeatedly re-endorsed at the highest levels, most recently at the G8 Gleneagles Summit and the United Nations World Summit in 2005.

The justification for meeting the 0.7 percent GNI aid target has never been greater. Global inequality is staggering: the top 20 percent of the global population enjoys more than 70 percent of total world income, contrasted by two percent for those in the bottom population quintile (Ortiz and Cummins 2011).[17] Given the stark disparities at the global level, ODA serves as the main redistributive channel to ensure equity. However, current international redistributive flows are simply insufficient. As of 2009, net ODA amounted to only 4.7 percent of total GDP in Sub-Saharan Africa followed by 1.3 percent of GDP in the Middle East and North Africa and far below one percent of GDP in all other developing regions.[18] Moreover, as an outflow, OECD countries contributed a meager 0.23 percent of their GDP to developing countries.[19] In short, meeting aid targets is a matter of global justice, and the failure of donors to provide additional development support indicates that globalization continues to benefit a privileged few.

In its current form, foreign aid is characterized by problems of size, transaction costs, limited predictability, macroeconomic impacts ("Dutch disease"), tied aid, lack of policy coherence, fungibility and conditionality (see Ortiz 2008b for further details). Concentration of ODA is another major problem, which has direct implications for fiscal space. Given limited development resources and increasing bilateralism, donors oftentimes pick their favorite allied developing countries and those in which they perceive to be strategic interests (often referred as the problem of the aid "orphans" and aid "darlings"). When measuring average global aid flows between 2005 and 2009, among the list of "darlings" includes Afghanistan, Democratic Republic of Congo, Ethiopia, Iraq, Nigeria, Pakistan, Sudan, Tanzania, Vietnam, and West Bank and Gaza (Table 2). Overall, 15 countries receive more than 50 percent of all international assistance. On the other end of the spectrum, many of the neediest countries are virtually left out of aid flows (the "orphans"). As Table 2 demonstrates, 20 of the world's poorest countries

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[16] World Bank analysis of historical ODA flows from donor countries during past crises suggests that aid could drop 20-25 percent (relative to the counterfactual) and recover only after about a decade (Dang et al. 2009). Preliminary data, however, show that net aid flows appear to have increased by 6.5 percent in 2010, at least (OECD 2011).

[17] Estimates are based on PPP constant 2005 international dollars. See Ortiz and Cummins (2011) for further discussion.

[18] Authors' calculations using World Development Indicators (2011).

[19] These estimates differ from those of the OECD due to differences in the base value year of the US dollar as well as those between GDP and GNI—OECD (2011) estimates total net aid outflows to be 0.31 percent of GNI in 2009.

received a combined total of only ten percent of all ODA; indeed, there is a strong case for the so-called "orphans" to lobby for increased North-South assistance.

Table 2. Aid Concentration and Neglect, 2005-09

(average values)

	Country	% of Global Aid	Aid Volume*	Aid per Capita**	GDP per Capita**	Infant Mortality Rate†	Aid as % of GDP	Public Health Spending as % of GDP
Significant Aid Flows	Iraq	12.3	10.6	352	1,891	35	18.5	2.6
	Nigeria	5.3	4.55	31	1,085	86	2.8	1.9
	Afghanistan	4.8	4.13	146	354	134	40.9	1.8
	Ethiopia	3.2	2.73	35	254	67	13.5	2.4
	Vietnam	2.9	2.51	30	871	20	3.4	2.4
	Tanzania	2.7	2.28	55	433	68	13.1	3.3
	Sudan	2.5	2.13	53	1,095	69	4.8	1.9
	Pakistan	2.4	2.06	13	865	71	1.5	0.8
	West Bank and Gaza	2.3	2.00	525	1,123	25	49.9	…
	Dem. Rep. of Congo	2.2	1.91	31	152	126	20.0	3.2
	India	2.1	1.83	2	997	50	0.2	1.2
	Mozambique	2.0	1.74	79	377	96	21.0	3.7
	Uganda	1.8	1.58	52	397	79	12.9	1.7
	Bangladesh	1.7	1.47	9	455	41	2.0	1.1
	China	1.7	1.42	1	2,722	17	0.0	2.0
	Total/Average	***50.0***	***42.9***	94	871	66	13.6	2.1
Limited Aid Flows	Gambia	0.10	0.09	53	391	78	13.5	3.0
	Guinea-Bissau	0.13	0.11	72	461	115	15.5	1.6
	Central African Republic	0.21	0.18	42	399	112	10.5	1.6
	Eritrea	0.21	0.18	39	306	39	12.5	1.3
	Togo	0.26	0.22	35	398	64	8.8	1.5
	Guinea	0.27	0.23	24	370	88	6.4	0.7
	Timor-Leste	0.27	0.23	219	394	48	55.2	11.3
	Tajikistan	0.33	0.28	42	559	52	7.5	1.3
	Chad	0.47	0.40	38	631	124	6.0	2.9
	Sierra Leone	0.47	0.41	75	302	123	24.8	1.2
	Burundi	0.54	0.47	59	132	101	44.9	5.0
	Zimbabwe	0.58	0.50	40	412	56	9.7	…
	Niger	0.62	0.53	38	309	76	12.1	3.2
	Nepal	0.72	0.62	22	371	39	5.9	1.9
	Cambodia	0.75	0.64	45	598	68	7.5	1.6
	Malawi	0.87	0.74	51	249	69	20.5	4.8
	Haiti	0.87	0.75	77	572	64	13.4	1.3
	Rwanda	0.88	0.75	79	405	70	19.4	4.2
	Madagascar	0.90	0.77	41	383	41	10.7	2.7
	Total/Average	***10.1***	***8.7***	63	392	75	19.3	2.9

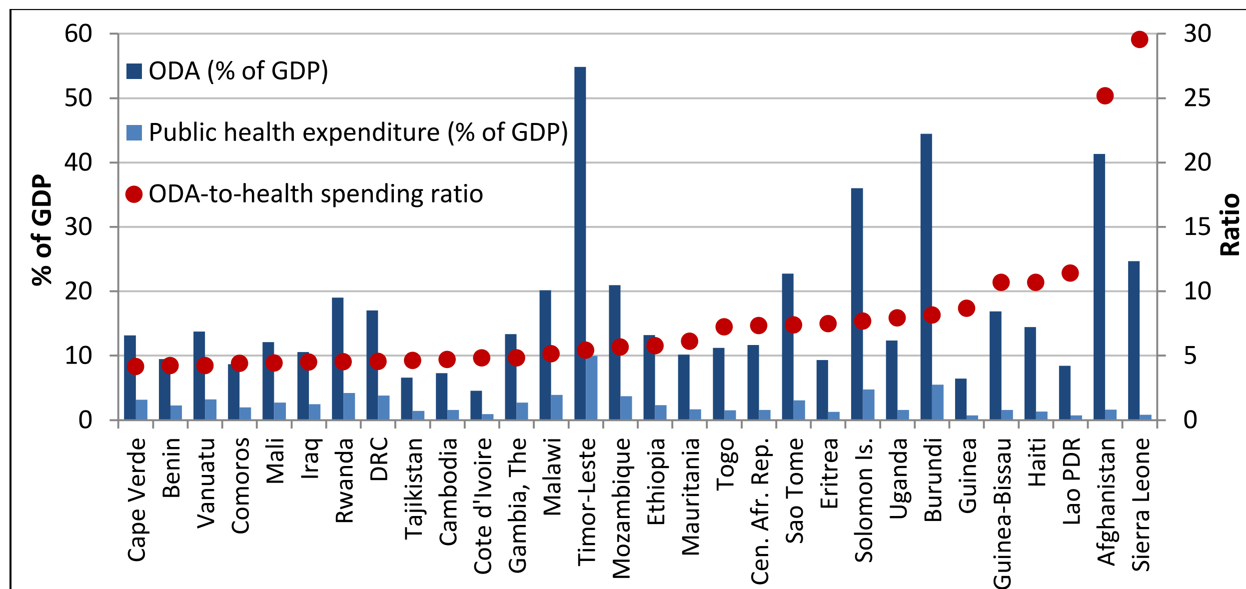
Source: Authors' calculations using World Development Indicators (2011)

* billions of current US dollars, ** in current US dollars, † per 1,000 live births

There is also the issue of where bilateral assistance is actually invested. Figure 5 reflects the three-year average values of ODA flows alongside health spending during 2007-09 in a selected group of developing countries, many of which rank among the aid "darlings." The striking feature is that health spending tends to pale in comparison to overall aid volumes, thus suggesting that the social sectors are not a major priority area for foreign assistance in many countries. This is perhaps best illustrated by Afghanistan and Sierra Leone. Although these countries rank among the worst in the world in terms of infant mortality rates and public health

expenditures, the average aid that they received during 2007-09 was more than 25 times the size of overall public investments in the health sector.

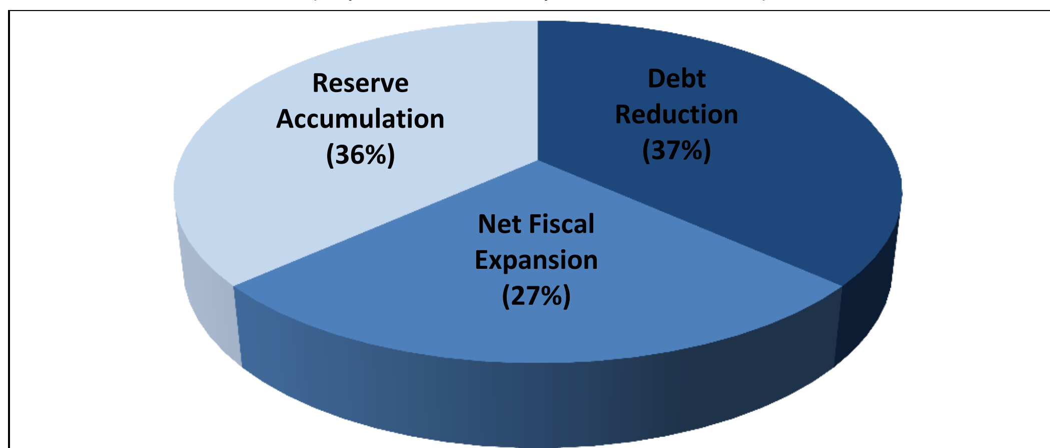
Figure 5. ODA and Health Spending in Selected Developing Countries, 2007-09
(average values)



Source: Authors' calculations using World Development Indicators (2011)

But where is the ODA directed when it actually reaches recipient countries? Following a comprehensive study of aid in Sub-Saharan Africa, the IMF's Independent Evaluation Office found that nearly three-quarters of aid given to poor countries between 1999 and 2005 was used to accumulate reserves and pay off debt rather than invest in much needed economic and social programmes (Figure 6). Such a strategy implies high human development opportunity costs, as vulnerable groups in Sub-Saharan Africa suffer from food insecurity, poor basic services and nutritional deprivations.

Figure 6. Use of ODA in Sub-Saharan Africa, 1999-2005
(in percent of anticipated aid increase)



Source: IMF (2007:42)

For developing countries not among the "darlings" or "orphans," donor resources tend to move in and out together, causing herd-like behaviour (see, for instance, Khamfula et al. 2006, Desai and Kharas 2010, and Frot and Santiso 2011). Poverty Reduction Strategy Papers (PRSP) and Country Policy and Institutional Assessments (CPIA),[20] which are performed by international financial institutions (IFI), function like rating signals for donors—similar to international credit rating agencies for private investors. Sometimes there are good reasons for donor withdrawal, such as when the policy-making process is captured by an interest group that benefits disproportionately from public policies rather than ensuring development for the majority of the population. On other occasions, however, the IFIs base their ratings on compliance with orthodox conditionality (e.g. fiscal and monetary austerity measures), which do not always allow for policy flexibility (Ortiz 2008b).

A final important point on North-South transfers is that only about half of traditional donor aid ever reaches developing countries. Data on the OECD's country programmable aid (CPA) shows that just 54 percent of ODA ends up in recipient countries, on average (Benn et al. 2010). The rest is spent on humanitarian aid (11 percent), in-donor costs (10 percent), debt relief (10 percent), and NGOs and local government (3 percent), with another 12 percent simply unallocated. Given that some donors deliver more CPA than others, it may be strategic for governments to target those donors with better records in providing higher amounts of CPA.

4.2. South-South transfers

For governments, South-South transfers are a clear avenue to tap into regional and cross-regional resources for social and economic development. South-South transfers are becoming increasingly important and take place through three main channels of cooperation: (i) bilateral aid, (ii) regional integration and (iii) regional development banks.

As a first major channel of South-South transfers, bilateral aid (non-OECD donors) is led by Brazil, China, India, Kuwait, Saudi Arabia, South Africa, United Arab Emirates and Venezuela (in alphabetical order). Data on South-South transfers are disparate and unreliable, and further difficult to compare in the absence of a universally-agreed definition of ODA. Nevertheless, estimates suggest that total worldwide ODA provided by non-OECD and non-European Union member countries leaped from US$8.6 billion in 2006 to US$15.3 billion in 2008 (or from about

[20] The CPIAs are the base of the World Bank's International Development Association (IDA) Resource Allocation Index for IDA eligible countries (concessional loans). Countries are ranked against a set of 16 criteria grouped in four clusters: economic management, structural policies, policies for social inclusion and equity, and public sector management and institutions. Designing a universal rating system for allocating resources is very correct, but criticisms naturally accompany criteria. For instance, macroeconomic criteria measure whether aggregate demand policies are consistent with macroeconomic stability, whether monetary and exchange rate policies ensure price stability, and whether private sector investment is crowded out. In terms of trade, criteria include measuring tariff levels, which need to be less than 12 percent, on average, and never exceed 20 percent, as well as evaluating internal tax policies to ensure that they do not discriminate heavily against imports (World Bank 2010a). Many argue that these criteria are based on contractionary policies that, combined with trade liberalization, are obstacles to inclusive growth and job generation in developing countries. Even the Independent Evaluation Group questions whether these criteria lead to growth and has recommended a series of revisions (2010:59-64).

seven to ten percent of total global development cooperation) (United Nations 2010a). If such estimates are at all indicative of actual flows, South-South aid offers a fast-growing opportunity for developing countries to finance social investments in children and poor households.

Two examples underscore the potential of South-South transfers. Given the magnitude of its investments in developing countries, especially in Sub-Saharan Africa and neighboring East Asian countries, the case of China must be highlighted. The Export-Import Bank of China, in particular, plays a strategic role, lending mostly to large infrastructure projects. Another case is oil-rich Venezuela, which has funded numerous economic and social investments in neighboring countries, such as under the Petrocaribe Initiative. One of the largest projects, Project Grand National, was launched in 2007 and supports everything from literacy programmes, regional universities and radio/TV media with indigenous content to energy generation and distribution. It is important to note that about 90 percent of South-South cooperation is in the form of country programmable aid or CPA, which means that assistance from these "emerging" donors plays a much larger role in increasing fiscal space than that from traditional donors whose CPA is only about half the size (United Nations 2010a:15).

Box 2. South-South Cooperation in Guinea-Bissau

Traditionally, the main development partners of Guinea-Bissau have been the European Union (EU), European bilateral donors, and multilateral organizations such as the World Bank, the African Development Bank, the United Nations and the Economic Community of West African States (ECOWAS). During 2000-09, among donors that report to the OECD Development Assistance Committee (DAC), the EU (US$294 million), Portugal (US$132 million), the World Bank (US$125 million), Italy (US$78 million) and Spain (US$55 million) provided the most development assistance to Guinea-Bissau. Not captured in these figures, however, is development assistance from key providers of South-South cooperation. Providers of South-South cooperation in Guinea-Bissau have typically provided project financing, often for infrastructure, as well as technical assistance. Southern providers include Angola, Brazil, and China.

Angola provided a US$12 million (about 1.3 percent of GDP) grant in February 2011, which the authorities intend to use to finance roads and agriculture projects and to pay previous years' arrears to the private sector. In October 2010, Angola announced that it would open a US$25-million line of credit to support entrepreneurs from both countries who want to invest in Guinea-Bissau. In 2008, Angola provided US$10 million in budget support. In addition to financial assistance, Angola has been actively involved in security reform.

Brazil has cooperated with Guinea-Bissau across several sectors. It has provided technical assistance to increase agricultural production; established training centers for the military, the police, teachers, and ex-combatants; and helped build capacity to combat HIV/AIDS. The UNDP estimates that Brazil's bilateral assistance to Guinea-Bissau totaled US$6.2 million during 2006-09.

China has realized several large projects in Bissau, including a 20,000-seat stadium, the National Assembly building (US$6 million), a new government office (US$12 million) that will house 12 ministries and a hospital (US$8 million). China has also provided technical assistance to improve rice production.

Source: IMF country report No. 11/119, May 2011, p. 7.

A second channel is regional integration, which is a major form of South-South cooperation. Regional trading strategies can be an effective means of protecting, promoting and reshaping a region's division of labour, trade, production and consumption. Regional integration can also help to redress social asymmetries and raise living standards through social spending, public investment, and macroeconomic policies geared towards employment and the expansion of national markets. The European Union is the best existing example of how regional solidarity may be articulated, but there are increasing experiences in developing countries. In fact, virtually every country in the world belongs to a regional block: the Association of South East Asian Nations (ASEAN), the African Union (AU), the Andean Community (CAN), the Caribbean Community (CARICOM), the League of Arab States (LAS), the South Asian Association for Regional Cooperation (SAARC) and the Southern Africa Development Community (SADC), to name a few. In terms of fiscal space, regional formations can offer a means of "locking in" finance for the development of member countries, which can be achieved through regional transfers or through regional development banks (see below).

A third major avenue of South-South transfers is regional development banks. The earliest South-South multilateral banks were founded in the Arab and Islamic world, where institutions were established in the 1970s as vehicles to transfer resources from the oil-rich countries to poorer countries. One such example is the Islamic Development Bank, whose objective is to foster the economic development and social progress of Muslim communities in accordance with the principles of Islamic law (*shari'ah*). In 2006, it announced a major funding operation in support of MDG-related expenditures among its member states. The second-largest regional development bank is the Arab Fund for Economic and Social Development (AFESD), which provides soft lending for Arab League countries, but mostly for infrastructure projects. There are many successful cases outside of the Islamic world, such as the Andean Development Corporation (CAF), whose portfolio of $3.0 billion, mostly in infrastructure, has largely surpassed investments by the World Bank and the Inter-American Development Bank in the South American sub-region. Also from Latin America, countries are collaborating to create alternative regional development banks, such as the Bank of the Bolivarian Alternative for Latin America (ALBA) and the Bank of the South.

4.3. Curtailing South-North transfers

Net financial flows between the South and North show a different picture: debt interest payments, profit remittances and public/private investments in capital markets in developed economies largely offset net financial inflows to developing countries. According to United Nations (2011), net financial flows out of developing economies totaled $557 billion in 2010, which is below the peak of US$881 billion reached in 2007 but significantly above trends from the 1990s (Table 3). Most of this goes to the United States, which accounts for two-thirds of global savings, followed by other developed countries like the United Kingdom, Spain and Australia. In sum, poor countries are transferring resources to rich countries, not *vice versa*.[21]

[21] Indeed, some of these flows are private or public savings in developing countries that are chasing safe investment returns in capital markets in developed countries. Nevertheless, global savings are flowing in the wrong

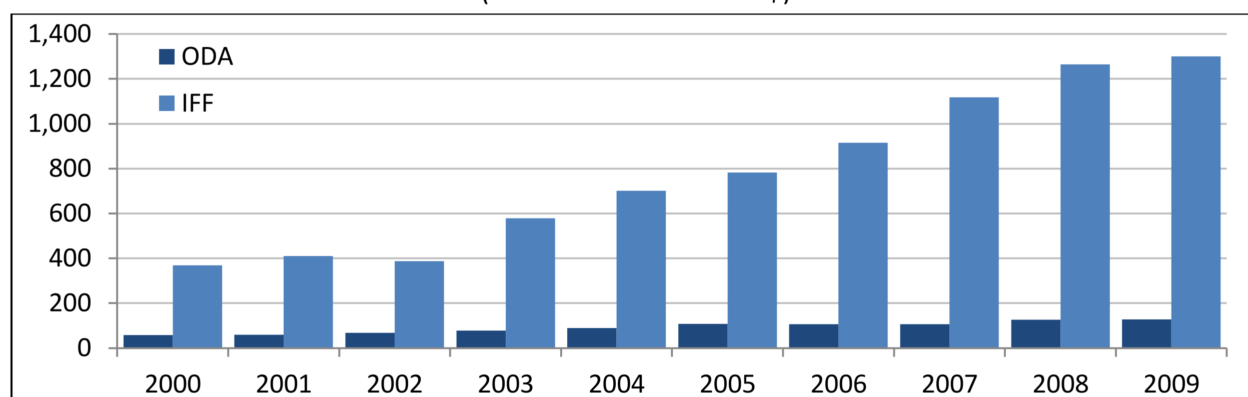
Table 3. Net Transfer of Financial Resources to Developing Economies, 1998-2010
(in billions of US dollars)

Developing Region	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Africa	2.9	1.6	-13.7	-16.4	-4.2	-16.1	-34.5	-76.4	-108.3	-100.9	-99.1	2.9	-35.3
Sub-Saharan Africa*	11.5	7.9	2.3	6.4	4.4	5.3	3.5	-0.6	-10.5	-9.1	-4.8	27.3	14.6
East and South Asia	-129.8	-139.8	-122.8	-120.8	-149.2	-175.6	-183.4	-265.7	-385.7	-529.8	-481.3	-427.5	-352.9
Western Asia	34.5	2.7	-35.3	-29.7	-23.2	-46.7	-76.3	-143.7	-175.6	-144.0	-222.5	-48.4	-112.7
Latin America	41.5	7.4	-4.2	2.5	-33.6	-64.3	-85.4	-111.4	-138.0	-106.4	-73.5	-72.1	-56.1
All Developing Economies	-41.0	-128.0	-194.0	-164.4	-210.2	-302.7	-379.5	-597.2	-807.8	-881.1	-876.4	-545.1	-557.0

Source: United Nations (2011:71)
*excludes Nigeria and South Africa

In addition to legal financial flows, curtailing illicit financial flows (IFF) could also free up additional resources for critical economic and social investments in many developing countries. IFFs involve capital that is illegally earned, transferred or utilized and include, *inter alia*, traded goods that are mispriced to avoid higher tariffs, wealth funneled to offshore accounts to evade income taxes and unreported movements of cash. More than US$1.3 trillion in IFFs are estimated to have moved out of developing countries in 2009 (Figure 7), mostly through trade mispricing with nearly two-thirds ending up in developed countries (Kar et al. 2010). As of 2009, IFFs amounted to more than ten times the total aid received by developing countries.[22] To put this in perspective, the net effect would be that for every one dollar that developing countries receive in ODA, they are giving back about seven dollars to wealthy countries via illicit outflows. Thus, it may be very worthwhile for developing country governments to examine possible strategies to crack down on IFFs through increased transparency rules, for example (see Kar 2011 for a description of different options).

Figure 7. Illicit Financial Flows (IFF) versus Official Development Assistance (ODA), 2000-09*
(in billions of current US$)



Source: Kar and Curcio (2011) and World Development Indicators (2011)
*Only includes ODA given by OECD countries

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direction, and countries need to ensure that more of their savings are directed toward domestic and regional development objectives rather than being exported to rich countries. Reversing the outflow of financial resources may require an overhaul of the financial system to provide greater banking stability and foster confidence in financial institutions.

[22] Authors' calculations using Kar and Curcio (2011) and World Development Indicators (2011).

4.4. New international sources of development finance

Given the failure of most donors to meet their aid commitments of 0.7 percent of GNI, an array of alternative sources of development finance has been proposed. Most of these involve taxing luxury activities or those that have negative social or environmental externalities (Atkinson 2004), and developing countries and partners could advocate for novel or "innovative" sources of development finance. Several of the more popular ideas to increase financing for development are summarized below.

- *Currency transactions taxes:* Applying a 0.005 percent single-currency transaction tax on all four major currencies could yield up to US$33.0 billion per year for developing country assistance. And if applied more broadly to cover all financial transactions globally, a 0.01 percent tax could raise over US$1.0 trillion annually (Leading Group on Innovating Financing for Development 2010).

- *International transportation taxes*: Taxing fuel emissions for cargo transports could raise between US$2.0-19.0 billion a year in maritime receipts and US$1.0-6.0 billion a year in aviation receipts (Institute for Policy Studies 2011).

- *Carbon taxes:* Charging a flat fee for every ton of CO2 emitted could lead to up to US$10.0 billion a year in development financing (Institute for Policy Studies 2011).

- *Arms trade taxes*: A ten percent tax on the international arms trade could accrue up to US$5.0 billion annually in new development revenue (WHO 2009b).
- *Airline taxes:* A number of countries have implemented an air ticket solidarity levy that is charged to all passengers taking off from their national airports. In France, for example, this raised €160 million for additional development assistance in 2009 (Leading Group on Innovating Financing for Development 2010).

- *Global lottery:* The idea of a global lottery for development financing was widely touted following the introduction of the MDGs, but its popularity has since waned. Nonetheless, introducing national versions of a global lottery game, or a single global lottery sold worldwide and run by one organization, still has immense potential once valued at US$6.2 billion annually (Carnegie Council 2005 and Inwent 2005).

In summary, there are ample opportunities for developing countries to increase fiscal space through strategies to increase North-South and South-South transfers, as well as to capture and re-direct illicit funds into development aims. Similarly, there is an array of innovative sources of development financing available to donor countries, which means that there are no longer any excuses for falling short on aid commitments. And for all countries—rich and poor—fiscal and foreign exchange reserves present additional creative options to boost fiscal space.

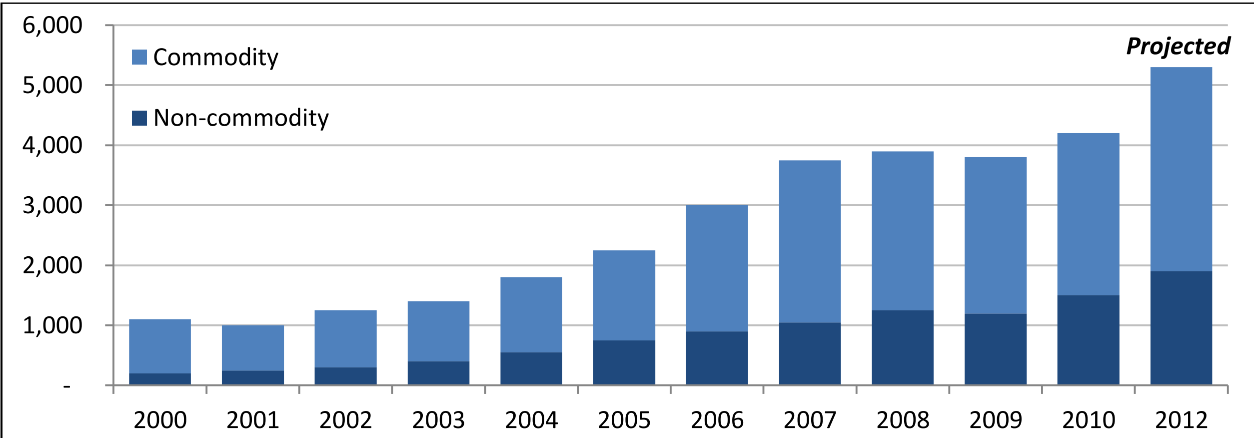
5. Using Fiscal and Foreign Exchange Reserves

Fiscal reserves and central bank foreign exchange reserves (also known as international reserves) offer other potential sources of financing for investments in children and poor households today. Fiscal reserves are accrued through government budget surpluses, profits of state-owned companies or other government net income (the classic example is export revenues from natural resources, such as oil). Foreign exchange reserves, on the other hand, are accumulated through foreign exchange market interventions by central banks within the context of current account surpluses and/or capital inflows. It is important to note the conceptual difference between fiscal reserves and central bank reserves. While fiscal reserves provide additional fiscal resources for the government and can be spent without incurring debt, central bank reserves are financed by issuing bonds or currency and do not constitute "free fiscal assets" since they have counterpart liabilities (i.e. currency or bonds). Regarding the latter, it follows that if a government wishes to "spend" central bank reserves, it must borrow to cover its new liabilities or otherwise creates new monetary liabilities (Park 2007).

5.1. Fiscal reserves

For most developing countries, it is difficult to identify the overall levels of fiscal reserves, largely due to transparency issues as well as differing central bank and government accounting methods. However, given that many governments channel at least a part of their fiscal reserves into special funds, the most popular being sovereign wealth funds (SWFs), we are able to broadly identify certain countries that could potentially access such resources for social and economic development. SWFs are state-owned investment funds composed of different financial assets that seek to maximize returns according to set levels of risk. SWFs have existed since the 1950s, but have grown rapidly over the past decade, reaching a record US$4.2 trillion in assets in 2010 (Figure 8).[23]

Figure 8. Assets under Management by Sovereign Wealth Funds (SWFs), 2000-12
(in billions of current US$)



Source: TheCityUK (2011)

[23] An additional $6.8 trillion was held in other sovereign investment vehicles (e.g. pension reserve funds).

There are two main types of SWFs: commodity and non-commodity. About two-thirds of all assets in SWFs are funded by commodities exports (oil, gas, copper, phosphates, etc.), which is why they are oftentimes referred to as oil or natural resource funds. The two largest commodity-based SWFs are the Abu Dhabi Investment Authority (US$627 billion) and Norway's Government Pension Fund Global (US$572 billion).[24] Non-commodity SWFs, in contrast, can be funded through government budget surpluses, profits of state-owned companies and foreign aid. Singapore is home to two of the most well-known non-commodity SWFs—Temasek Holdings and Government of Singapore Investment Corporation—which managed more than US$400 billion in combined assets as of June 2011.[25]

As evidenced by recent and projected trends in SWFs, many developing countries appear well endowed with fiscal reserves. Some of the more notable candidates are identified in Table 4 below, with Russia topping the list at more than US$140 billion in fiscal reserves followed by Libya, Algeria, Kazakhstan, Malaysia and Azerbaijan, all of which had more than US$30 billion as of June 2011. Importantly, no least developed countries (LDCs) appear on this list.

Table 4. Sovereign Wealth Funds (SWFs) based on Fiscal Reserves in Selected Developing Countries, June 2011

Country	Fund Name	Assets*	Inception	Origin
Russia	National Welfare Fund	142.5	2008	Oil
Libya	Libyan Investment Authority	70.0	2006	Oil
Algeria	Revenue Regulation Fund	56.7	2000	Oil
Kazakhstan	Kazakhstan National Fund	38.6	2000	Oil
Malaysia	Khazanah Nasional	36.8	1993	Non-Commodity
Azerbaijan	State Oil Fund	30.2	1999	Oil
Iran	Oil Stabilisation Fund	23.0	1999	Oil
Chile	Social and Economic Stabilization Fund	21.8	1985	Copper
Brazil	Sovereign Fund of Brazil	11.3	2008	Non-Commodity
Botswana	Pula Fund	6.9	1994	Diamonds and Minerals
Timor-Leste	Timor-Leste Petroleum Fund	6.3	2005	Oil and Gas
Mexico	Oil Revenues Stabilization Fund of Mexico	6.0	2000	Oil
Venezuela	FEM	0.8	1998	Oil
Vietnam	State Capital Investment Corporation	0.5	2006	Non-Commodity
Kiribati	Revenue Equalization Reserve Fund	0.4	1956	Phosphates
Indonesia	Government Investment Unit	0.3	2006	Non-Commodity
Mauritania	National Fund for Hydrocarbon Reserves	0.3	2006	Oil and Gas
	Total	452.4		

Source: SWF Institute (2011)
* in billions of current US dollars

The logic behind SWFs is to maximize financial returns, normally in international capital markets. A great deal of attention has been devoted to the fact that SWFs from the South are buying assets, real state, sovereign and corporate debt, private equity, hedge funds and

[24] According to SWF Institute (2011).
[25] Ibid.

commodity stocks in the North. Many have questioned the logic of investing earned public income for capital market growth to spend at some future point when those resources could be invested in needed social and economic goods and services at home today. Venezuela, for example, has used its fiscal reserves to finance a number of development objectives both domestically and internationally. Domestically, the government has fostered local development since 2001 through the Bank for Economic and Social Development of Venezuela (BANDES), which offers concessional rates to public and social enterprises (such as state-owned and community/family enterprises as well as cooperatives), supporting everything from milk producers to health services. And in neighboring Latin American countries, Venezuela has channeled its fiscal reserves in support of economic and social development through the Petro-Caribe and Petro-Andes Initiatives. However, it is also important to understand the capacity issues that underlie a government's ability to spend fiscal reserves today, as evidenced by the case of Timor-Leste (Box 3).

Box 3. When Resources and Poverty Abound: The Paradox of Timor-Leste

A number of countries are sitting atop abundant natural resource funds, yet social indicators and progress towards development objectives remain dismal. One such case is Timor-Leste. For example, the share of people living in poverty increased from 36 to 50 percent between 2001 and 2007, levels of underweight children and maternal mortality remain unacceptably high, and it ranks in the bottom 30 percentile of all countries in terms of the human development index (HDI). Yet, at the same time, Timor-Leste has an estimated US$6.3 billion stored in a SWF. If these funds were simply divvied up amongst the populace, they could, in effect, increase the average Timorese per capita income by more than 11-fold, to US$5,500 per person. So why isn't the government using the available resources to ramp up investments in its people?

Timor-Leste's government faces many development challenges. In addition to rampant poverty and unemployment, infrastructure remains dilapidated following years of conflict, and, despite vast petroleum reserves, it is the most oil dependent country in the world. Perhaps the biggest challenge, however, is the lack of institutional capacity, which makes it difficult for the government to effectively deliver public goods and services, especially to the poorest groups. As a result, present spending levels have stretched administrative capacities and created bottlenecks in the economy. The government has recognized the existing constraints and developed a plan to address budget under-execution and to build administrative capacities; possibilities for procuring external capacities are also being explored for areas that are locally unavailable. With capacity development—especially "investing in investing"—now at the fore of the government's agenda, further tapping into available fiscal reserves could lead to a big return on socio-economic investments in the near future.

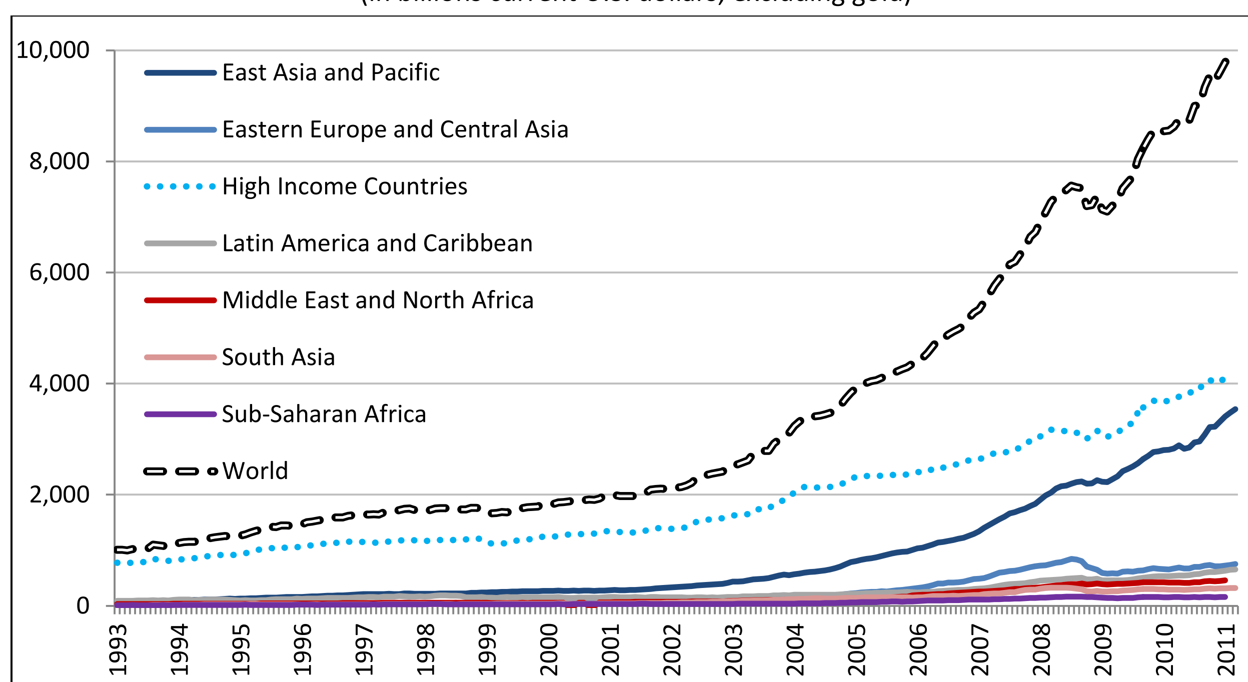
Sources: World Bank (2010b) and Gomes and Hailu (2009)[26]

[26] See also IMF country report No. 11/65, February 2011 and United Nations News Centre, "Timor-Leste's Economy at 'Turning Point,' Says Top UN Envoy," 7 April 2010.

5.2. Central bank foreign exchange reserves

Foreign exchange reserves accumulated at central banks have increased dramatically in many developing countries over the past decade and offer creative possibilities to finance social and economic investments. On a global level, the accumulation of foreign exchange reserves more than quadrupled between 2000 and 2011, reaching 17 percent of global GDP as of March 2011.[27] Several developing regions, however, experienced elephantine growth. For example, total foreign exchange reserves leaped by 15-fold in Eastern Europe and Central Asia, by 12-fold in East Asia and the Pacific, and by more than seven-fold in South Asia and the Middle East and North Africa, on average, over the same time period (Figure 9).

Figure 9. Foreign Exchange Reserve Accumulation by Developing Region, 1993-2011
(in billions current U.S. dollars; excluding gold)



Source: World Bank's Global Economic Monitor database (2011)

The massive accumulation of foreign exchange reserves is largely attributed to two strategies. On the one hand, some countries build up large stocks of reserves to self-insure against economic and financial shocks, notably those that lead to capital flight and/or severe external imbalances. While this trend is most obvious in emerging market economies, especially in Asia, it is increasingly applicable to a number of low-income countries. In Sub-Saharan Africa, for example, more than one-third of foreign aid received between 1999 and 2005 was used to accumulate reserves (IMF 2007:42). On the other hand, countries also stockpile foreign exchange reserves as part of broader efforts to stabilize the macro-economy, especially exchange rates. This is most commonly linked to export-led growth strategies based on exchange rate regimes with *de jure* or *de facto* pegs to the US dollar or currency baskets.

[27] Authors' calculations based on the World Bank's Global Economic Monitor database (2011).

The strategy of reserve accumulation as self-insurance has been questioned by many, from the United Nations to the IMF. However, until better international solutions are put in place, some basic indicators point to the need to explore the use of foreign exchange reserves for economic and social development. For instance, according to the most popular gauge—the number of months for which a country could support its current level of imports if all other capital flows were to suddenly stop—62 developing countries with recent reserves data boasted more than one-and-a-half times the three-month safe level benchmark (e.g. more than 4.5 months) as of March 2011. Using another standard indicator—the ratio of short-term debt to foreign exchange reserves—58 developing countries had short-term debt-to-reserve levels that were under 25 percent as of March 2011, which far exceeds the so-called Greenspan-Guidotti rule of thumb that advises countries to hold enough foreign reserves to cover total short-term external debt obligations. When combining these indicators, 33 developing countries with corresponding data exceed both of the safe level benchmarks (Table 5).

Table 5. Foreign Exchange Reserve Adequacy by Developing Region, 2011 (or latest available)
(excluding gold)

Country	Reserves in months of imports	Short-term debt as % of reserves	Country	Reserves in months of imports	Short-term debt as % of reserves
Algeria	51.3	1.0	Lebanon	26.4	7.9
Angola	15.1	19.3	Madagascar	4.8	23.0
Azerbaijan	8.6	15.1	Malaysia	6.7	24.5
Bolivia	13.4	6.5	Mongolia	6.6	5.4
Brazil	17.9	16.7	Morocco	6.6	9.2
Burundi	5.0	2.3	Nigeria	8.2	7.7
Cambodia	5.2	8.1	Pakistan	4.9	10.8
Cameroon	8.2	0.6	Paraguay	4.5	19.5
China	20.4	9.8	Peru	15.2	14.2
Colombia	6.9	16.4	Philippines	10.3	9.1
Cote d'Ivoire	4.5	3.0	Rep. of Congo	16.7	5.6
Egypt	8.1	7.3	Russia	17.7	7.0
Gabon	7.6	5.4	Thailand	8.8	20.1
Guatemala	5.1	23.6	Uganda	10.4	7.9
India	7.9	15.1	Uruguay	8.5	14.0
Jordan	8.7	9.5	Yemen	6.9	6.3
Kyrgyz Republic	11.9	5.1			

Source: Authors' calculations using World Development Indicators (2011) and World Bank's Global Economic Monitor database (2011)

So what are developing countries doing with their vast arsenals of foreign exchange reserves? In practice, most governments invest their reserves in Treasury Bills issued by the US government due to their safety (they were considered the least risky investment available, at least until August 2011) and high liquidity (they have maturity dates as short as four weeks). However, given the extremely low yields that are offered on these investments, there is definitely room for central banks in some developing countries to re-assess their current risk

portfolios. It is also important for developing countries to question the logic of investing excess foreign reserves overseas when social and economic investments are needed at home.[28]

One strategy to foster local development using surplus foreign exchange reserves is to finance domestic projects. India stands as an innovative example, as it strategically uses a portion of its foreign reserves—without the risk of monetary expansion—to support one of the country's biggest development needs: infrastructure investment (Park 2007:21-22). To do so, India's government created two subsidiaries that borrow foreign exchange reserves from the central bank. The foreign exchange is then directly on-lent to Indian companies for capital expenditures outside India, used to co-finance the external commercial borrowings of Indian companies, or invested in highly rated collateral securities to enhance the credit ratings of Indian companies that raise funds in international capital markets. The central government plays an important role by guaranteeing the loans from the central bank, which, in turn, is assured a higher return on domestic highways, for instance, than would otherwise be achieved on short-term US government bonds. In addition to more traditional productive sectors, such as infrastructure, India's approach could also be applied to facilitate private sector borrowing for different social investments, such as education and health facilities.

In addition to financing domestic projects, developing countries can also seek to achieve longer-term investment returns on their excess foreign exchange through regional South-South cooperation. For example, since the major oil boom in the 1970s, many countries in the Middle East have invested surplus foreign exchange reserves in the Islamic Development Bank to foster economic development and social development in poorer Muslim communities (Ortiz 2008b). The CAF and the Bank of the South are two examples from Latin America in which countries are planning to channel extra foreign exchange reserves to support regional investments. And in Asia, 13 countries contributed US$120 billion to the Chiang Mai Initiative in 2010, which serves as a reserve-pooling mechanism to help manage short-term liquidity problems in the region.

In sum, fiscal and foreign exchange reserves present creative possibilities for governments to enhance fiscal space for social and economic investments, although a careful assessment of their potential impact on monetary expansion or public debt impact is warranted.

6. Borrowing and Debt Restructuring

Sound debt management is a key principle of a sound macroeconomic policy framework. Studies have shown that high debt distress or even debt crisis could lead to a loss of capital market access, a disruption of financial intermediation and hindering of economic activities. Yet for countries that have some scope for additional borrowing, this offers another source of financing for social and economic investments. For those countries that may have very high levels of sovereign debt, it may also be possible to restructure existing debt either by debt re-

[28] While central bank reserves are not "free" resources, they could be used as foreign currency liquidity guarantees to lower costs of external borrowing for financing domestic development projects or strategic businesses.

negotiation, debt relief/forgiveness, debt swaps/conversion or debt repudiation, especially when the legitimacy of the debt is questionable and/or the opportunity cost in terms of worsening child outcomes is high.

6.1. Borrowing

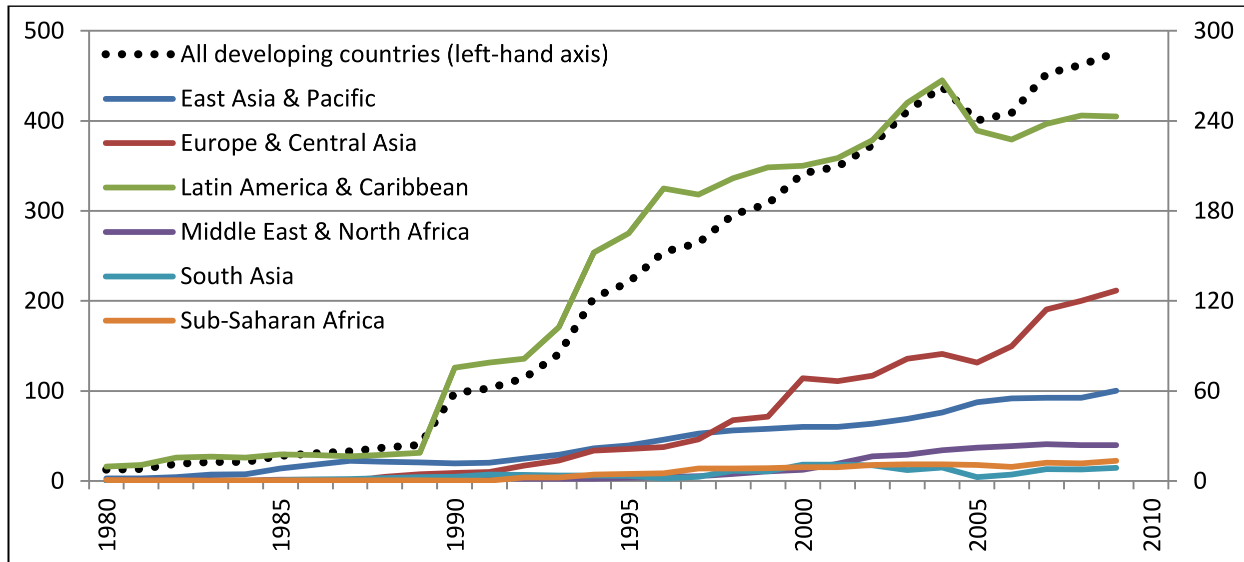
Many developing countries, having progressed in developing their local financial markets, show potential capacity to engage in further borrowing, both domestically and externally. These may include loans, either from commercial or development banks or funds, or through issuing government securities, such as bonds. International commercial bank loans are a least preferred option for governments to expand fiscal space due to associated fees and higher interest rates. Tanzania stands as one recent example, as its government borrowed US$1.5 billion from local and foreign banks to boost its 2011 budget and cover a deficit left by an unexpected withdrawal of donor support.[29]

Loans from development banks and funds, as well as bilateral loans from donors, may be at commercial or concessional interest rates. If debt is perceived as a strategic option to boost social and economic spending, concessional loans are a much better option than loans with commercial rates since they offer beneficial conditions to developing countries. For example, the World Bank's International Development Association (IDA) lends money to the poorest countries without interest along with long grace periods (usually ten years) and 35 to 40-year repayment periods. Concessional borrowing is generally available from regional development banks (e.g. the African, Asian, Inter-American and Islamic Development Banks), specialized funds (e.g. the OPEC Fund for International Development or the Arab Fund for Economic and Social Development) and from bilateral loans from donor countries.

Government bonds are another market-based borrowing option and generally cheaper when compared to regularly priced commercial bank loans. While European governments have been issuing bonds to support public spending since the dawn of modern history, financial liberalization coupled with the rise of creditworthiness among emerging markets has made the issuance of governments bonds increasingly popular since the 1990s. Total public bonds issued annually by developing country governments increased markedly during the 1990s, reaching close to US$500 billion in 2009 (Figure 10). Latin America is the region that has experienced the largest growth, issuing nearly double the amount of debt as the next highest region, Europe and Central Asia as of 2009. Although bonds appear less common in other regions, they are still viable options for many lower income countries. For example, Ghana and Senegal tapped international debt markets in 2007 and 2009, respectively (Gueye and Sy 2010). In addition to bonds at the national level, municipal or sub-national bonds are another alternative for local governments, which are typically issued for specific purposes, such as for developing an urban area or expanding school, water supply or transportation systems (Ortiz 2008b).

[29] See The Citizen, "Tanzania: World Bank Faults Govt's Borrowing Plan," 5 June 2010.

Figure 10. Public Bonds by Developing Regions, 1980-2009*
(in billions of current US dollars)



Source: World Development Indicators (2011)
* Includes public and publicly guaranteed debt from bonds that are either publicly issued or privately placed

How much public debt is unsustainable? The IMF (2010b) uses a 40 percent long-term debt-to-GDP ratio as the ceiling that developing countries should not exceed in order to ensure fiscal sustainability and macroeconomic stability. Others suggest a higher threshold (e.g. 60 percent according to Reinhart and Rogoff 2010). Still, another approach is to view an optimal debt-to-GDP ratio as arbitrary since public debt can be beneficial over the long term if interest payments are less than the annual increase in nominal GDP (see UNCTAD 2011 Chapter 3).

So which countries might have room to borrow? Applying even the most conservative parameters, many developing countries appear well-positioned to tap into debt markets. Figure 11 lists 29 countries that had total external debts under 20 percent of GDP through 2009. This list is, of course, only indicative, as debt levels have likely increased in countries due to debt-financed fiscal stimulus packages since then.

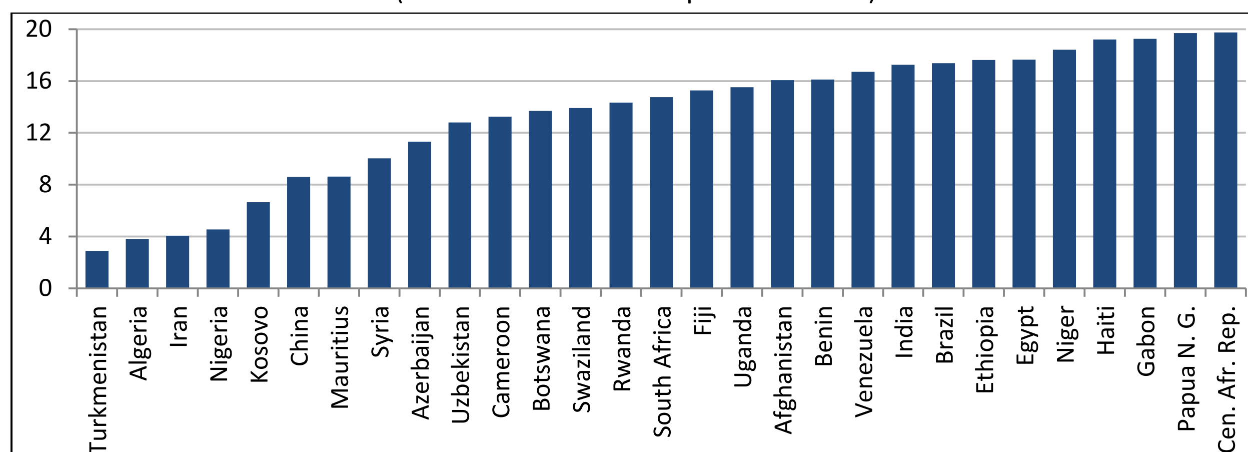
However, to determine the feasibility of increasing public debt for a given country, it is important to carry out a comprehensive and dynamic analysis, such as the IMF-World Bank debt sustainability assessments (DSA) framework. DSAs seek to determine, going forward, if a country's overall debt level would be too big to be serviceable under a given set of assumptions, which includes the projected fiscal and GDP growth paths.[30] However, findings of DSAs reflect the underlying assumptions, and depending on how conservative or ambitious the underlying assumptions are, a rather different picture on the level of debt distress may emerge.

[30] The DSA approach includes four steps: (i) a five-year forecast of variables that impact external debt (e.g. the primary account, GDP, interest rates, exchange rates and inflation); (ii) an examination of the evolution of debt as a percentage of GDP over the next five years; (iii) different stress tests to evaluate the impact of adverse shocks on the different forecasted variables in step i; and (iv) evaluation of whether current debt loads are sustainable based on the stress tests.

Another key limitation of DSAs is that GDP growth projections only take into account returns from investments in physical capital (roads, airports, etc.) but not returns from investments in human or social capital (spending on primary/secondary education, health, and social protection), which are vital to sustained growth in the longer run. Thus, while current DSA frameworks should be viewed as a good starting point of analysis, they can be enhanced by relaxing certain assumptions and accounting for both social and economic returns.

Figure 11. Possible Borrowing Candidates, 2009[31]

(total external debt as a percent of GDP)



Source: Authors' calculations using World Development Indicators (2011)

6.2. Debt restructuring

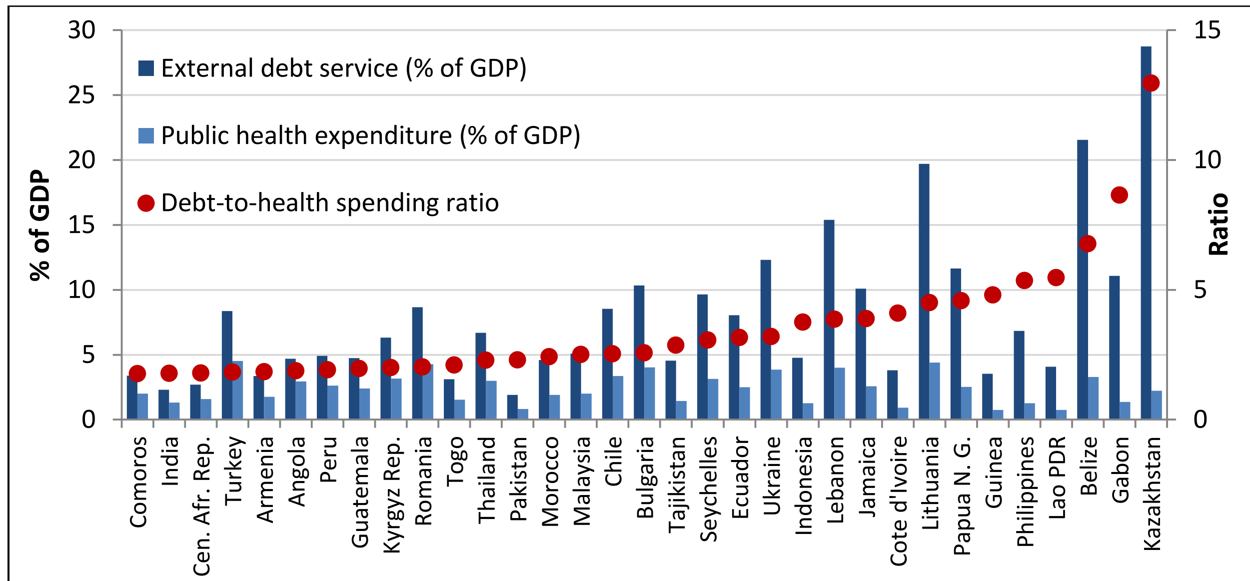
Debt restructuring is the process of reducing existing levels of debt or debt service. While some developing countries have space for additional borrowing, debt restructuring has become an increasingly common strategy to alleviate fiscal pressures for other countries, especially those suffering from exorbitant sovereign debt levels. Figure 12 highlights the gravity of the external debt burden facing some developing countries. All of the 33 countries listed have a three-year average external debt-to-public health spending ratio greater than 1.75; in other words, debt payments in each of these countries is nearly double or more than the amount of public money invested in the health of their populaces, with Kazakhstan spending a staggering 13 times more on external debt than on health. When sovereign debt payments crowd out essential social expenditures, there is a strong case for countries to re-examine their obligations to their creditors. As Tanzania's President once called out, "Must we starve our children to pay our debts?"[32]

[31] This figure only includes external public debt. While domestic debt is generally a smaller proportion of total public debt in developing countries, this is certainly not true for all countries. It is, however, more difficult to assess domestic debt levels since they are not tracked by major databases (e.g. by the IMF or World Bank) and detailed information is often unavailable to policymakers and analysts (Panizza 2008). Moreover, the gravity of domestic debt can be high in developing countries, many of which have replaced external debt with more expensive domestic debt in recent years. When performing country level analysis, it is therefore imperative to assess the composition of both domestic and foreign public debt.

[32] See The Independent, "Appeal: Children in Africa should not Starve to Repay Debt," on 3 January 2003.

Figure 12. Debt and Health Spending, 2007-09*

(average values, based on current US dollars)



Source: Authors' calculations using World Development Indicators (2011)

* This figure only includes external public debt (see footnote for Figure 11)

In recent years, many—including some official creditors such as Norway—have raised the issue of creditor co-responsibility as a way of promoting responsible lending practices. The Monterrey Consensus additionally opened up the debate on the issue of creditor co-responsibility for what is termed "illegitimate debt," as well as the need to find a fair and durable solution to the debt crisis. In particular, the United Nations Secretary-General and the United Nations Independent Expert[33] note that creditor and debtor countries are both equally responsible for preventing and resolving unsustainable debt situations.

The concept of illegitimate debt refers to a variety of debts that may be questioned, including: debt incurred by authoritarian regimes; debt that cannot be serviced without threatening the realization or non-regression of basic human rights; debt incurred under predatory repayment terms, including usurious interest rates; debt converted from private (commercial) to public debt under pressure to bail out creditors; loans used for morally reprehensible purposes, such as the financing of a suppressive regime; and debt resulting from irresponsible projects that failed to serve development objectives or caused harm to the people or the environment (United Nations 2009a).

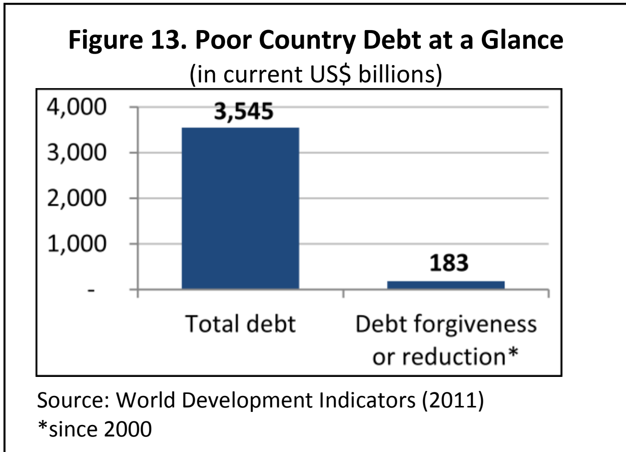
In practice, there are five main options available to governments to restructure sovereign debt, which include: (i) re-negotiating debt, (ii) achieving debt relief/forgiveness, (iii) debt swaps/conversions, (iv) repudiating debt and (v) defaulting.

[33] The United Nations Independent Expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights.

- *Debt re-negotiation:* A first option is to restructure debt via voluntary negotiations and collective action clauses. Voluntary negotiations have mostly applied to bank loans, as demonstrated by the more than 60 countries that have successfully re-negotiated terms between 1990 and the early 2000s (Bai and Zhangy 2010). These processes, however, take an average of five years, which carry a high re-negotiation cost since governments cannot resume international borrowing during that time. Collective action clauses are most commonly used to restructure government bonds and take much less time than voluntary negotiations (about one year on average); through collective action clauses included in bond contracts, many countries have successfully reached agreements with commercial creditors to lengthen the maturity and lower the coupon of outstanding bonds.

- *Debt relief/forgiveness:* A second option is to negotiate debt forgiveness. This has happened through creditor-led forums, such as the Paris and London Clubs, which are used to restructure or cancel bilateral and commercial debt, respectively, as well as the Heavily Indebted Poor Countries Initiative (HIPC) executed by the IMF and World Bank. HIPC has been the most prominent option for debt relief. Launched in 1996, 32 low-income countries had reached their completion points as of mid-2011 by meeting debt relief criteria. While earlier these countries were spending more on debt service than on health and education combined, on average, social spending now accounts for roughly five times their amount of debt-service payments (IMF 2011a). However, debt forgiveness has been slow to deliver (Figure 13), and the benefits of agreed debt reduction have proven far less than hoped for in most cases (UNCTAD 2008:139-141).

Figure 13. Poor Country Debt at a Glance
(in current US$ billions)



Source: World Development Indicators (2011)
*since 2000

- *Debt swaps/conversions*: A debt swap or debt conversion is the sale of a debt by a creditor to an investor (usually a non-profit organization) who purchases the debt at a discounted price and then exchanges it with the indebted government for shares in a state-owned company or for domestic currency to finance a specific project. More than 50 developing countries have undertaken debt swaps with different aims. They emerged in the 1980s as a strategy to improve the fiscal solvency of governments, mostly in Latin America, and to give them access to new international finance. Countries such as Argentina and Chile carried out debt-for-equity swaps, exchanging external private debt for shares in state-run companies. Debt-for-nature swaps soon followed in which a portion of a developing country's foreign debt was exchanged for investments in environmental conservation measures. During the 1990s, UNICEF facilitated numerous private debt swaps to support child aid programmes. Although most swaps have been conducted within the framework of the HIPC initiative, there are a variety of swap options available to governments to enhance fiscal space. The

Debt2Health initiative of the Global Fund is a recent debt swap initiative which converts debt repayments into health expenditures in countries that are ineligible for debt relief.[34] For smaller island states, there are debt conversions for climate change adaptation (Hurley 2010). There are also opportunities to negotiate other types of swaps/conversions to enhance fiscal space, including: debt-for-children/education/health/environment, debt-for-equity, debt-for-exports, debt-for-offsets and even debt-for-debt (Ruiz 2007).

- *Debt Repudiation:* Another option is repudiation. History shows examples of governments repudiating debt, such as the United Kingdom after the Boer War or the United States' repudiation of Cuban debts owed to Spain following the Spanish-American War. Given that the high cost of debt servicing limits public investments in essential social and economic goods and services, repudiation is increasingly considered by developing countries in recent years. Christian Aid (2007) outlines a number of practical steps that debtor countries can follow to determine if debt repudiation is a sensible option: (i) assess the impact that debt servicing has on the financing of basic services; (ii) carry out a full debt audit to identify which parts are odious or illegitimate; (iii) identify what portion of the legitimate debt can be serviced without jeopardizing essential public services; (iv) hold a moratorium on servicing illegitimate debt and discuss with creditors; (v) depending on the progress of discussions, examine the possibility of withholding payments in order to increase investments in basic services; and (vi) open debt contraction processes to full democratic scrutiny. The recent referendum in Iceland (Box 4) and public debt audits, such as in Ecuador (Box 5), underscore the idea that citizens have concerns about illegitimate sovereign debt and the high social costs.

- *Default:* Overall, some 20 countries have defaulted on their sovereign debt since 1999, which includes debt denominated in both local and foreign currencies.[35] At US$82 billion and US$73 billion, Argentina and Russia, respectively, stand as the largest sovereign defaulters in history. The widely used term "haircut" refers to investor losses as a result of debt restructuring. While this was an estimated 75 percent in the case of Argentina in 2005 and 55 percent for Russia in 1999-2000, the average haircut in more recent forced restructurings has been 25-40 percent (Sturzenegger and Zettelmeyer 2005). Outright default may be viewed as disorderly debt restructuring since the immediate aftermath can be severe as foreign investments flee and capital inflows cease, which could hurt domestic employment and economic activities, the extent of which depends on the openness of the economy. However, history shows that countries that defaulted have been able to regain capital market access, achieve stable macroeconomic conditions and increase fiscal space for social and economic development (Lora and Olivera 2006, Weisbrot and Sandoval 2007).

[34] See Global Fund's Debt2Health.

[35] According to Standard & Poor's (2011) and Moody's (2008), this list includes: Antigua (2006), Argentina (2001), Belize (2006), Dominican Republic (1999, 2005), Ecuador (2008), Gabon (1999, 2002), Grenada (2004), Indonesia (1999, 2000 and 2002), Ivory Coast (2000), Jamaica (2010), Moldova (2002), Pakistan (1999), Paraguay (2003), Peru (2000), Russia (1999), Seychelles (2008), Ukraine (2000), Uruguay (2003) and Venezuela (2005).

Box 4. Debt Repudiation: Iraq and Iceland

Two recent examples of sovereign debt repudiation are Iraq and Iceland. Iraq's 80 percent debt cancellation was a result of international political pressure; the United States was at the forefront of negotiating for a full-scale write-off of loans undertaken by foreign creditors to the Saddam Hussein regime after its overthrow in 2003. In Iceland, a national referendum was held in March 2010 that allowed its citizens to vote on whether and how the country should repay its debts claimed by the Netherlands and the United Kingdom. This was not a sovereign debt issue; a private Icelandic bank held €6.7 billion in deposits from British and Dutch savers, and, when it collapsed, the respective governments decided to make public this debt. In the referendum, Icelandic voters delivered a resounding "no" (more than 90 percent) to reimburse the Dutch and British governments and the orthodox policies that would have accompanied the debt repayment plan (de Bruijn et al. 2010).

Box 5. Debt Audits: The Case of Ecuador

Some developing countries have re-examined their accumulated debt from the 1970s in order to decrease outstanding obligations. In 2008, Ecuador became the first country to hold an official audit to assess the legitimacy of its sovereign debt. The government-commissioned, two year-long investigation concluded that some of its foreign debts had broken multiple principles of international and domestic law and were therefore deemed "illegitimate"—these were mostly private sector debts that had been nationalized by former governments. While Ecuador respected all of the debt that had contributed to the country's development—the so-called "legitimate" debt—it defaulted on its alleged illegitimate debt in November 2008 and bought this back at 35 cents to the dollar just a few weeks later. Based on the experience of Ecuador, as well as Norway, a special United Nations Commission of Experts on Reforms of the International Monetary and Financial System came out in support of public debt audits as a mechanism for transparent and fair restructuring of debts (United Nations 2009b:125). Debt audits are ongoing in several other countries, such as Bolivia, Brazil, Greece, Ireland and the Philippines.

Box 6. The Need for an International Debt Work-out Mechanism

In practice, all of the different sovereign debt restructuring options are politically difficult, as governments that initiate such processes are often under enormous pressure by creditors. This reality, coupled with the increasing prevalence of sovereign debt crises, underscores the pressing need for an international judicial body that can resolve issues between sovereign borrowers and their lenders. Since the pioneering proposals for an International Chapter 9 Insolvency by Raffer (1993), the IFIs, the United Nations and different civil society organizations have been advocating for an international debt-work out mechanism. More recently, the IMF proposed a Sovereign Debt Restructuring Mechanism, which would have created a process for "sovereign bankruptcy" to give states a new beginning, much like a corporation or individual who files for bankruptcy. In the same line, the Jubilee Campaign (Pettifor 2002) and Eurodad (2009) have identified principles for a sovereign debt work-out procedure, many of which are supported by the United Nations. Current proposals to operationalize these principles include an International Debt Court and/or an International Mediation Forum (United Nations 2010b).

7. A More Accommodating Macroeconomic Framework

The goals of macroeconomic policy are multiple, from supporting growth, price stabilization or inflation control, to smoothing economic cycles, reducing unemployment and poverty, and promoting equity. In the last decades, macroeconomic frameworks have placed a strong emphasis on short-term stabilization measures, such as controlling inflation and fiscal deficits, as part of broader efforts aimed at economic liberalization, integrating into global markets and attracting investment. While these macroeconomic objectives are not necessarily problematic, there is an increasing risk in many developing countries that other important objectives, such as employment-generating growth and social development, become secondary and underemphasized.

Many of these orthodox approaches have since been questioned, including through UNICEF's work on "Adjustment with a Human Face" in the 1980s and the broader advocacy efforts of the United Nations to advance human development and human rights since the 1990s. Others (e.g. Chowdhury and Islam 2010) have argued that higher fiscal deficits do not necessarily lead to higher interest rates, inflation rates or current account deficits if there is unemployment or spare capacity in an economy. More recently, as the multiple shocks of the global economic crisis unfolded and intensified, support shifted from restrictive and narrow macroeconomic frameworks to a more accommodating one, a change that has since been reflected in the pronouncements by senior leaders in various organizations, including the IMF (2009 and 2011b). In practice, this means that the conditions for more maneuver in policy-making and resources could be achieved through both fiscal and monetary policy, both of which are described in the following.

7.1. More accommodative fiscal policy

The first channel to achieve a more accommodative macroeconomic framework is through expanding government expenditures to influence the economy. As part of the crisis response, there has been a growing recognition of the need to ease budget constraints and allow for an increasing degree of deficit spending, especially to support socially relevant investments. By doing so, more resources can be allocated to address the impacts of the crisis and support poverty-reducing and employment-generating economic growth (IMF 2009).

To demonstrate the potential size of resources that could be freed up for social spending through larger—albeit reasonable—fiscal deficits, consider Sub-Saharan Africa. Of the 42 developing countries in the region for which there is fiscal balance data, 35 are forecasted to run fiscal deficits during 2011 (Table 6). If each of these countries increased the size of their current deficit by two percentage points, public health spending could jump by more than four percent, on average (Column C). Some countries, however, could experience vast increases in available resources for public health. For example, a two percent increase in the fiscal deficit in 2011 could lead to a roughly ten percent increase in Cote d'Ivoire, Guinea, Sierra Leone and Uganda, all of which have some of the highest infant mortality rates in the world (Column D).

Table 6. Real Fiscal Deficits and Health Spending in 35 Sub-Saharan African Countries, fiscal year 2011

Country	(A) Fiscal balance, including grants (% of GDP)	(B) Health expenditures (2007-09 avg.)		(C) 2% real increase of deficit (in % of health budget)*	(D) Under-5 mortality rate, 2009 (per 1,000 live births)
		% of GDP	% budget		
Eritrea	-16.2	1.3	3.2	25.8	55
Lesotho	-14.5	4.9	8.2	5.9	84
Cape Verde	-11.8	3.2	10.4	7.4	28
Swaziland	-9.0	3.7	9.3	4.8	73
São Tomé and Príncipe	-7.4	3.1	13.2	4.8	78
Congo, Dem. Rep.	-7.1	3.8	16.1	3.7	128
Uganda	-6.8	1.6	10.6	8.7	128
Mozambique	-6.7	3.7	12.6	3.6	142
Tanzania	-6.5	3.5	18.2	3.7	108
Senegal	-5.7	3.1	11.8	3.6	93
South Africa	-5.7	3.4	10.2	3.4	62
Kenya	-5.4	1.5	5.9	7.0	84
Burkina Faso	-4.3	3.7	15.8	2.3	166
Ghana	-4.3	3.8	9.5	2.3	69
Namibia	-4.3	3.8	12.5	2.2	48
Mauritius	-4.2	2.0	8.6	4.2	17
Sierra Leone	-4.0	0.9	4.2	9.3	192
Botswana	-3.9	6.7	17.2	1.2	57
Guinea	-3.9	0.8	4.3	10.4	142
Cote d'Ivoire	-3.9	0.9	4.5	8.5	119
Liberia	-3.6	4.0	17.2	1.8	112
Mali	-3.0	2.7	10.5	2.2	191
Zambia	-2.9	3.1	13.2	1.8	141
Burundi	-2.6	5.5	11.8	0.9	166
Togo	-2.6	1.5	7.8	3.4	98
Ethiopia	-2.5	2.3	11.9	2.2	104
Guinea-Bissau	-1.9	1.6	4.0	2.4	193
Gambia, The	-1.8	2.7	11.6	1.3	103
Benin	-1.7	2.2	9.1	1.5	118
Madagascar	-1.3	2.9	14.8	0.9	58
Niger	-1.3	3.2	13.7	0.8	160
Comoros	-1.0	2.0	8.0	1.0	104
Cameroon	-0.6	1.3	7.3	0.9	154
Malawi	-0.2	3.9	12.1	0.1	110
Central African Republic	-0.1	1.6	11.0	0.1	171
Average	**-4.6**	**2.9**	**10.6**	**4.1**	**110**

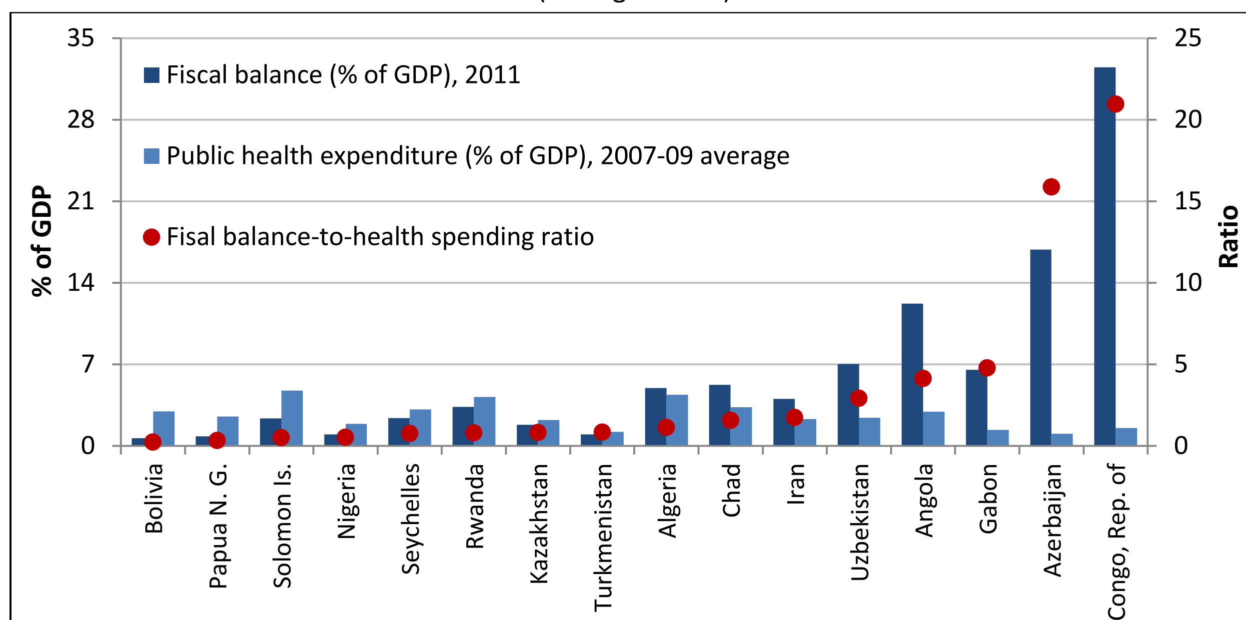
Sources: IMF's World Economic Outlook (April 2011) for fiscal balance, real GDP and inflation estimates; World Development Indicators (2011) for health expenditure; and UNICEF (2011) for under-5 mortality data

* Estimate based on the real value (local currency value/average consumer price) of fiscal balance and health expenditures

While many developing countries are already running deficits, a number of others are forecasted to have fiscal surpluses in 2011 (Figure 14). In these cases, allocating surplus funds to public health could lead to extraordinary gains. In the Republic of Congo, for example,

significant progress in health outcomes could be made if even a small portion of surplus funds was directed to the health sector together with appropriate reforms to strengthen service delivery institutions. And for the 16 developing countries that are projected to benefit from a positive fiscal balance during 2011, surplus budget funds could ramp up health spending by about four times the current levels, on average.

Figure 14. Fiscal Surplus and Health Spending, 2011
(average values)



Sources: Authors' calculations using IMF's World Economic Outlook (April 2011) for fiscal balance data and World Development Indicators (2011) for health expenditure

The analysis of Sub-Saharan African countries serves to illustrate the potential of any government's fiscal position—deficit or surplus—to impact essential social and economic spending. However, it is important to carry out a rigorous assessment of fiscal sustainability within a country, taking into account not only economic aspects such as debt burden, revenue generation capacity and likely GDP growth trajectory, but also the potential opportunity cost of foregoing spending on children and other vulnerable populations.

7.2. More accommodative monetary policy

The second channel to achieve a more accommodative macroeconomic framework is through expansionary monetary policy. There are two schools of thought regarding how authorities should control a country's money supply. On the one hand, some argue that the ultimate aim of monetary policy should be to achieve low inflation.[36] Here, since high inflation creates uncertainties about the future and depresses investment, low inflation is viewed as a key

[36] This view is more controversial, as it has been found that a certain amount of inflation (moderate inflation, not very high inflationary episodes) may be necessary to fuel more economic activity.

ingredient to macroeconomic stability and growth, and is a goal in itself. Moreover, in terms of poor households, high levels of inflation erode disposable incomes, making it more difficult for them to purchase essential goods and services.

On the other side of the spectrum are those who view excessive inflation control as a danger to poverty and economic growth. This camp argues that certain measures, such as higher interest rates or reserve requirements, can lead to increasing unemployment, lower aggregate demand and weaker growth. High interest rates are especially bad for small producers and those who already have limited access to finance, including women and persons with limited assets. The resulting declines in output and employment can also weaken workers' bargaining positions and depress wages, therefore indirectly increasing poverty. All of these, in turn, weaken the capabilities of households to provide for and invest in children. Acknowledging the potential risks of low inflation on growth and poverty, the IMF advised governments to raise inflation above the standard five percent benchmark during 2009 in order to respond to the food, fuel and financial shocks (IMF 2009). However, it is important to underscore that there are diverse views on what constitutes an "acceptable" level of inflation (Table 7).

Table 7. Safe Inflation Thresholds for Developing Countries

	Author(s)	**Inflation Threshold (%)**
Academic Papers	Fischer (1993)	15-30
	Bruno (1995)	20
	Barro (1996)	10-20
	Bruno and Easterly (1998)	40
	Gylfason and Herbertsson (2001)	10-20
	Rousseau and Watchel (2002)	13-25
	Burdekin et al. (2004)	3
	Gillman et al. (2004)	10
	Sepehri and Moshiri (2004)	5-15
	Pollin and Zhu (2006)	14-16
	Li (2006)	14
	Vaona and Schiavo (2007)	12
	US GAO (2009)	5-12
	Bick (2010)	12
	Kremer et al. (2011)	17
IMF Papers	Sarel (1996)	8
	Ghosh and Phillips (1998)	>5
	Kochar and Coorey (1999)	5
	Khan and Senhadji (2001)	11-12
	Selassie et al. (2006)	5
	Espinoza et al. (2010)	10
	Blanchard et al. (2010)	4

Source: Authors' literature review

In general, flexibility to pursue expansionary monetary policy is strongly related to the extent to which wages and incomes are "indexed"—in other words, automatically adjusted to changes in overall prices, at least to some extent. In developing countries where most incomes, including wage incomes, tend to move along with prices, there can be social tolerance of fairly high rates of inflation, especially if it still allows people to continue to consume essential goods and services. But in other developing countries where wage incomes and the earnings of the self-employed do not increase much when overall price levels rise, even relatively low rates of inflation can cause social havoc, especially if the inflation is not accompanied by higher employment. They can also immediately and directly affect the well-being of children; this is especially true for food inflation, which continues to be a significant challenge to many developing countries (Ortiz et al. 2011b).

Ultimately, this means that inflation thresholds are policy choices based on particular conditions in different societies, and monetary policies should be designed to encourage employment creation. Bearing this in mind, the IMF forecasts that nearly 50 developing countries will have inflation rates below five percent during 2011, half of which exercise independent monetary policy (Table 8). In such cases, an expansionary monetary policy could be explored as a potential option to support increased social and economic investments among the poorest and most disadvantaged populations. For other developing countries that are also experiencing low inflation rates but belong to monetary unions—such as the Eastern Caribbean Currency Union, the Economic and Monetary Community of Central Africa, and the West African Economic and Monetary Union—there may be scope to discuss the loosening of monetary policy as a block of countries.

Table 8. Developing Countries with Low Inflation Rates, 2011 forecasts

(in percent change of average consumer prices)

Country	Inflation Rate	Country	Inflation Rate
Peru	2.70	Comoros	3.88
Malaysia	2.80	Vanuatu	3.95
Belize	2.87	Tunisia	4.00
Morocco	2.90	Thailand	4.02
Samoa	3.00	Cape Verde	4.37
Lithuania	3.11	Albania	4.50
Rwanda	3.11	Djibouti	4.63
Seychelles	3.14	Bulgaria	4.76
Solomon Islands	3.35	Zimbabwe	4.83
Colombia	3.56	Philippines	4.91
Chile	3.61	South Africa	4.93
Mexico	3.63	China	4.99
Fiji	3.82		

Source: IMF's World Economic Outlook (April 2011)

8. Concluding Remarks

As the number of countries expected to adopt fiscal contraction in 2012 increases dramatically, there are grave concerns that many are doing so prematurely and even excessively (Ortiz et al. 2011a). Aside from the direct impact on essential social expenditures, the different austerity measures being considered pose immense risks to vulnerable populations whose need for public support has never been greater. Above all, the limited window of intervention for fetal development and for growth among infants and young children means that deprivations today, if not addressed promptly, can have irreversible impacts on their physical and intellectual capacities, which will, in turn, lower their productivity in adulthood; this is an extraordinary price for a country to pay. Providing immediate and adequate support for children and their families is therefore an urgent imperative.

This paper has shown that governments, even in the poorest countries, have multiple options to support those most in need. The broad areas that warrant further exploration by governments and development partners include: (i) re-allocating public expenditures, (ii) increasing tax revenues, (iii) lobbying for increased aid and transfers, (iv) tapping into fiscal and foreign exchange reserves, (v) borrowing or restructuring existing debt, and (vi) adopting a more accommodating macroeconomic framework. While specific options are unique to each country and have associated risks and trade-offs, they should be carefully examined at the national level and considered in an inclusive dialogue.

Some questions for policymakers to consider in terms of public spending trends may include:

- Are current spending priorities and decisions considering the longer-term impacts of high unemployment, rising food and energy prices, and social inequities on children and poor households? What are the long-term opportunity costs of not scaling up equity-based interventions, social protection programmes and productive social sector investments during the economic recovery?

- Is the current fiscal adjustment trajectory—in terms of scope and pace—conducive to adequately investing in the most vulnerable groups and achieving the Millennium Development Goals (MDGs)? Are current and medium-term expenditure frameworks based on both social and economic indicators that are sufficiently disaggregated to capture the conditions of the poor and the most disadvantaged, including children?

- Have all possible fiscal scenarios been fully explored—or fiscal sustainability assessment exercises been carried out—and discussed in an open, national dialogue in order to support a socially responsive recovery? More specifically:

  i. Can government expenditures be re-allocated to free up additional space for high-priority socio-economic investments that benefit poor households? Are current military expenditures, or expenditures to support the commercial sector, justified in light of existing poverty rates and overall levels of vulnerability among poor populations,

especially during the recovery? Is it possible to enhance the efficiency of existing investments?

ii. Have *all* tax codes and possible modifications been considered and evaluated to maximize public revenue without jeopardizing private investment? Are personal income and corporate tax rates designed to support equitable outcomes? What specific taxation collection methods could be strengthened to enhance overall revenue streams? Could minor tariff adjustments increase the availability of resources for social investments? Can tax policies better respond to “boom” and “bust” cycles? Have financial transaction taxes been considered to support productive and social sector investments?

iii. Is the government lobbying for increased North-South (ODA) or South-South transfers? Are there efforts to fight and re-channel illicit financial flows?

iv. Are there fiscal reserves, for example, sitting in sovereign wealth funds that could be invested in children and poor families today? Are excess foreign exchange reserves being maximized and fostering local and regional development investments?

v. Have debt options been thoroughly examined for increased social and economic investments today? Have different maturity and repayment terms been discussed with creditors? Has a public audit been carried out to examine the legitimacy of existing debts? What are the distribution impacts of financing government expenditures by borrowing?

vi. Could increasing the fiscal deficit by just a few percentage points lead to a significant ramping up of health and education spending allocations and better protect the most vulnerable? Are current inflation levels unduly restricting employment growth?

The urgency for exploring fiscal space options for socially-responsive economic decisions that support the most vulnerable has never been greater.

Annex. Selected Fiscal Space Indicators for 182 Countries

(in percent of GDP for 2009, unless otherwise noted)

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010**	(v) External debt (% of GNI)		(vi) Inflation (% change), 2011*
	Total*	Health	Educ.	Military	Total*	Tax			Service	Tot. stocks	
Afghanistan	22.0	1.6	...	1.8	20.6	7.3	41.9	...	0.1	19.6	9.8
Albania	33.6	2.8	...	2.1	26.2	...	3.0	21.0	2.2	40.3	4.5
Algeria	41.7	5.0	4.3	3.8	36.3	34.3	0.2	101.5	0.7	3.8	5.0
Angola	39.5	4.1	2.6	4.2	30.9	...	0.3	23.1	5.2	28.2	14.6
Antigua and Barbuda	39.7	3.8	2.7	...	20.2	...	0.5	12.4	...	...	3.7
Argentina	39.9	6.3	4.9	0.8	36.1	...	0.0	13.4	4.1	40.1	10.2
Armenia	28.9	2.0	3.0	4.0	21.1	16.4	6.1	19.8	4.8	55.3	9.3
Australia	37.7	5.6	4.5	1.9	33.5	22.1	...	3.1	...	...	3.0
Austria	52.3	8.2	5.4	0.9	48.8	18.7	...	2.5	...	...	2.5
Azerbaijan	34.8	1.4	2.8	3.5	41.6	16.7	0.5	11.8	1.0	12.1	10.3
Bahamas	23.0	3.2	...	...	18.0	16.7	...	13.9	...	...	2.0
Bahrain	30.4	3.1	2.9	3.6	23.8	1.5	...	...	...	...	3.0
Bangladesh	14.5	1.1	2.4	1.1	10.5	8.6	1.4	10.1	1.0	24.0	7.6
Barbados	45.3	4.4	-6.6	...	38.0	33.2	0.3	21.0	...	...	6.1
Belarus	46.1	4.1	4.5	1.8	45.7	19.4	0.2	6.3	2.6	35.6	12.9
Belgium	54.1	8.1	6.0	1.1	48.1	24.0	...	3.5	...	...	2.9
Belize	28.2	3.6	5.7	1.1	27.0	...	2.1	15.6	8.9	89.4	2.9
Benin	24.8	2.3	3.5	1.0	21.6	16.1	10.3	18.5	0.6	16.1	4.2
Bhutan	38.6	4.5	4.8	...	40.4	9.1	9.8	63.1	5.7	57.7	6.5
Bolivia	35.5	3.1	...	1.6	36.1	17.0	4.2	42.0	3.5	34.5	10.4
Bosnia & Herzegovina	50.4	6.7	...	1.5	44.7	19.6	2.4	14.1	3.7	54.6	5.0
Botswana	45.8	8.2	8.9	3.1	34.8	...	2.4	56.2	0.4	14.1	7.8
Brazil	38.8	4.1	5.1	1.6	35.6	15.6	0.0	13.7	2.8	17.9	6.3
Brunei Darussalam	38.7	2.6	...	2.6	42.6	...	...	10.4	...	...	1.2
Bulgaria	36.2	4.4	4.1	2.3	35.3	20.9	...	32.3	11.2	90.4	4.8
Burkina Faso	24.0	3.9	4.6	1.3	19.4	12.9	13.3	14.8	0.5	22.9	2.0
Burundi	50.7	6.0	8.3	3.8	109.2	...	41.4	22.2	1.5	38.9	8.4
Cambodia	19.0	1.6	2.1	1.2	15.6	9.6	6.9	28.0	0.5	45.0	5.1
Cameroon	18.4	1.6	3.7	1.5	18.4	...	2.9	16.4	1.8	13.6	3.0
Canada	43.8	7.5	4.9	1.4	38.3	11.8	...	3.6	...	...	2.2
Cape Verde	35.3	2.9	5.9	0.6	29.0	20.4	12.6	22.2	2.2	47.2	4.4
Central African Rep.	16.1	1.6	1.3	1.8	16.1	...	11.8	10.4	1.6	20.0	2.7
Chad	30.1	3.9	3.2	6.4	20.0	...	8.2	7.9	1.3	28.6	3.0
Chile	26.4	3.8	4.0	3.1	22.0	15.3	0.0	13.7	10.0	46.7	3.6
China	23.1	2.3	...	2.0	20.0	10.3	0.0	48.8	0.8	8.7	5.0
Colombia	29.4	5.4	4.8	4.1	26.8	11.9	0.5	9.7	3.9	23.6	3.6
Comoros	22.4	2.1	7.6	...	24.8	...	9.5	27.2	2.2	51.0	3.9
Dem. Rep. of Congo	28.5	4.9	...	1.1	24.3	...	22.3	9.9	7.1	121.4	12.0
Republic of Congo	24.7	1.6	1.8	1.2	29.5	6.2	3.0	33.0	2.4	83.8	5.9
Costa Rica	26.5	7.1	6.3	...	22.5	13.9	0.4	12.9	4.3	28.1	5.6
Côte d'Ivoire	21.1	1.0	4.6	1.6	19.5	16.4	10.2	14.3	4.9	53.0	5.0
Croatia	42.8	6.6	4.6	1.8	38.7	19.1	0.3	23.3	...	...	3.5

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010**	(v) External debt (% of GNI)		(vi) Inflation (% change), 2011*
	Total*	Health	Educ.	Military	Total*	Tax			Service	Tot. stocks	
Cuba	...	11.0	13.6	3.2	...	...	0.2	...	...	...	...
Cyprus	45.8	2.5	4.1	2.2	39.8	25.8	...	2.2	...	...	3.9
Czech Republic	45.9	6.1	4.2	1.5	40.2	13.5	...	21.8	...	...	2.0
Denmark	58.3	9.0	7.8	1.4	55.4	34.5	...	23.7	...	...	2.0
Djibouti	41.6	5.3	8.4	3.7	37.0	...	15.5	21.8	2.6	67.2	4.6
Dominica	47.7	4.1	4.7	...	47.6	...	9.6	20.2	5.0	69.9	3.6
Dominican Republic	17.2	2.4	2.3	0.6	13.7	14.9	0.3	6.7	2.9	24.6	6.1
Ecuador	34.5	2.9	...	3.3	29.8	...	0.4	2.4	11.4	23.3	3.5
Egypt	34.6	2.1	3.8	2.1	27.7	15.7	0.5	15.4	1.6	17.6	11.5
El Salvador	21.0	3.8	3.6	0.6	15.4	12.5	1.3	11.8	6.0	54.3	3.5
Equatorial Guinea	49.0	3.4	...	...	41.0	...	0.3	22.5	...	...	7.3
Eritrea	30.6	1.0	2.0	...	15.9	...	7.7	2.7	1.2	58.6	13.3
Estonia	47.6	5.3	4.8	2.3	45.5	17.6	...	12.9	...	...	4.7
Ethiopia	17.2	2.0	5.5	1.3	16.3	8.8	13.4	6.0	0.4	17.6	12.9
Fiji	29.4	2.5	...	1.4	24.8	23.2	2.5	22.9	0.9	14.2	3.8
Finland	56.3	7.0	5.9	1.5	53.4	21.3	...	3.1	...	...	3.0
France	56.0	9.0	5.6	2.4	48.4	19.6	...	2.2	...	...	2.1
Gabon	25.1	1.7	...	1.1	32.6	...	0.7	15.3	4.9	22.3	2.3
Gambia	21.2	3.0	...	0.7	18.7	...	17.5	21.0	3.7	75.3	5.9
Georgia	35.8	2.9	3.2	5.6	29.3	23.2	8.5	19.4	2.5	40.0	12.6
Germany	47.5	8.6	4.5	1.4	44.5	12.0	...	1.9	...	...	2.2
Ghana	22.2	3.1	5.4	0.4	16.4	12.5	6.0	...	0.9	37.3	8.7
Greece	53.2	6.7	4.0	4.0	37.8	19.1	...	0.4	...	...	2.5
Grenada	33.5	3.8	...	...	27.2	...	7.7	17.7	3.5	92.0	5.8
Guatemala	14.2	2.6	3.2	0.4	11.1	10.4	1.0	13.6	4.7	38.8	5.1
Guinea	24.1	0.9	2.4	...	16.8	...	5.2	...	3.5	48.3	19.6
Guinea-Bissau	21.9	1.6	...	2.1	24.8	...	17.4	20.1	1.2	253.2	4.0
Guyana	32.8	7.2	6.1	...	29.3	...	8.6	35.3	1.0	72.4	6.2
Haiti	22.1	1.4	...	...	17.7	...	17.3	19.5	...	...	6.4
Honduras	29.7	3.4	...	0.8	25.1	14.4	3.2	17.4	3.0	25.9	7.6
Hong Kong	17.5	...	4.5	...	19.1	13.0	...	119.4	...	...	5.8
Hungary	50.4	5.1	5.2	1.3	46.1	23.5	...	34.8	...	...	4.1
Iceland	50.0	6.7	7.4	0.1	41.1	21.4	...	45.3	...	...	2.6
India	27.3	1.4	3.1	2.7	18.0	9.8	0.2	17.9	1.2	18.2	7.5
Indonesia	18.3	1.2	2.8	0.9	16.5	11.4	0.2	13.1	5.2	30.2	7.1
Iran	27.8	2.2	4.7	2.7	25.8	9.3	0.0	...	0.8	4.1	22.5
Iraq	93.6	2.8	...	6.3	71.7	...	4.2	61.3	...	...	5.0
Ireland	48.6	7.8	4.9	0.6	34.2	20.8	...	0.9	...	...	0.5
Israel	44.3	4.5	5.9	6.9	38.7	23.0	...	33.3	...	...	3.0
Italy	51.8	7.3	4.3	1.7	46.5	23.0	...	2.3	...	...	2.0
Jamaica	37.9	2.8	5.8	0.6	27.0	21.9	1.2	15.2	12.7	77.8	9.0
Japan	40.1	6.7	3.5	1.0	29.8	9.2	...	19.4	...	...	0.2
Jordan	33.2	6.0	...	5.5	25.1	16.2	3.0	47.4	2.3	28.3	6.1
Kazakhstan	23.9	2.7	2.8	1.2	22.5	8.1	0.3	18.2	39.3	113.0	9.1
Kenya	29.1	1.5	7.0	1.9	23.7	19.6	6.1	13.4	1.3	26.5	7.2

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010**	(v) External debt (% of GNI)		(vi) Inflation (% change), 2011*
	Total*	Health	Educ.	Military	Total*	Tax			Service	Tot. stocks	
Kiribati	91.0	10.3	...	...	78.4	...	21.2	...	...	...	2.5
Korea	24.0	3.5	4.2	2.9	24.0	15.5	...	28.9	...	...	4.5
Kosovo	30.0	...	4.3	...	29.3	21.1	14.6	...	4.1	6.4	8.2
Kuwait	41.9	2.8	3.8	3.2	65.5	0.9	...	16.2	...	...	6.1
Kyrgyz Republic	33.4	3.5	5.9	3.6	32.3	15.4	6.9	34.7	8.2	65.8	18.8
Lao PDR	24.5	0.8	2.3	0.4	17.7	12.5	7.1	12.6	4.2	95.5	5.7
Latvia	44.0	3.9	5.0	2.6	36.2	12.6	...	30.2	...	...	3.0
Lebanon	32.5	4.0	1.8	4.1	24.4	17.3	1.9	80.3	12.0	70.7	6.5
Lesotho	65.5	5.6	12.4	2.8	62.8	60.0	7.8	...	1.9	33.2	5.4
Liberia	41.9	5.3	2.8	0.8	29.9	0.3	57.6	38.2	9.9	257.5	9.7
Libya	52.3	2.6	...	1.2	59.3	...	0.1	134.2	...	...	...
Lithuania	44.1	4.5	4.7	1.7	34.9	13.8	...	18.1	17.5	85.3	3.1
Luxembourg	42.2	5.8	...	0.7	41.5	24.4	...	1.4	...	...	3.5
Macedonia	33.3	4.6	...	2.1	30.6	19.7	2.1	21.6	6.1	62.2	5.2
Madagascar	15.0	2.8	3.0	1.1	12.2	13.0	5.2	14.0	0.5	22.2	8.9
Malawi	39.9	3.6	...	...	34.2	...	16.3	3.0	0.8	24.7	6.6
Malaysia	33.0	2.2	4.1	2.0	27.0	15.7	0.1	44.1	5.9	35.8	2.8
Maldives	50.1	5.2	11.2	...	27.3	14.1	2.3	18.7	4.9	60.0	6.5
Mali	25.8	2.7	4.4	2.0	22.5	14.7	11.0	17.3	0.9	29.6	4.5
Malta	43.2	5.6	6.4	0.6	39.5	28.2	...	6.5	...	...	3.0
Mauritania	30.6	1.6	2.9	3.8	25.5	...	9.5	5.9	2.6	66.6	7.3
Mauritius	26.2	2.1	3.2	0.2	22.7	19.2	1.8	25.1	1.4	8.4	7.4
Mexico	26.9	3.1	4.8	0.5	22.0	...	0.0	11.6	4.6	22.3	3.6
Moldova	45.2	6.4	9.6	0.5	38.9	17.8	4.5	29.6	6.8	59.7	7.5
Mongolia	35.2	4.0	5.6	1.4	30.2	18.0	8.9	35.9	2.8	55.8	16.4
Montenegro	48.9	6.7	...	1.4	42.4	...	1.8	...	1.7	56.4	3.1
Morocco	29.0	1.9	5.6	3.3	26.4	23.8	1.0	21.9	3.8	26.4	2.9
Mozambique	32.2	4.1	5.0	0.9	26.7	...	20.6	21.8	0.4	43.0	9.5
Myanmar	9.7	0.2	...	...	6.1	...	...	...	...	...	8.0
Namibia	30.7	4.0	6.4	3.3	29.0	27.3	3.5	14.3	...	...	5.9
Nepal	19.8	2.1	4.6	1.6	16.8	12.2	6.8	...	1.4	28.7	9.9
Netherlands	50.6	8.3	5.3	1.5	45.2	22.7	...	2.4	...	...	2.3
New Zealand	34.4	7.8	6.1	1.1	31.1	30.8	...	11.9	...	...	4.1
Nicaragua	30.5	5.4	...	0.7	28.5	17.8	12.6	27.5	8.3	76.2	8.7
Niger	24.4	3.5	4.5	1.0	19.1	11.5	8.7	11.8	0.8	18.8	3.8
Nigeria	30.4	2.1	...	0.9	19.9	0.3	1.0	16.1	0.3	5.1	11.1
Norway	46.1	7.6	6.8	1.5	56.5	25.4	...	12.8	...	...	1.8
Oman	39.3	2.4	3.9	8.7	40.2	...	0.5	23.4	...	...	3.5
Pakistan	19.9	0.9	2.7	3.0	14.7	9.3	1.7	8.2	2.1	31.3	15.5
Panama	25.5	5.9	3.8	...	24.5	...	0.3	10.1	4.3	52.5	5.0
Papua New Guinea	37.1	2.5	...	0.5	27.5	...	5.2	31.4	6.9	19.9	8.3
Paraguay	22.7	3.0	4.0	0.9	23.2	13.0	1.0	22.4	3.2	29.5	9.6
Peru	21.0	2.7	2.7	1.2	18.9	13.4	0.3	27.9	3.1	24.8	2.7
Philippines	18.6	1.3	2.8	0.8	14.6	12.8	0.2	29.3	6.1	39.2	4.9
Poland	44.4	4.9	4.9	2.0	37.3	16.4	...	19.0	...	...	4.1

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010**	(v) External debt (% of GNI)		(vi) Inflation (% change), 2011*
	Total*	Health	Educ.	Military	Total*	Tax			Service	Tot. stocks	
Portugal	48.2	7.9	5.2	2.0	38.9	19.7	...	1.6	...	...	2.4
Qatar	29.7	2.0	...	2.2	43.8	19.8	...	23.6	...	...	4.2
Romania	38.7	4.3	4.3	1.4	31.4	17.9	...	26.8	10.0	71.6	6.1
Russia	41.4	3.5	3.9	4.3	35.1	12.9	...	30.3	5.6	31.9	9.3
Rwanda	25.9	3.9	4.1	1.4	27.4	...	17.9	14.5	0.5	14.9	3.1
Samoa	35.9	6.1	5.7	...	32.1	...	15.6	37.7	1.8	49.0	3.0
São Tomé & Príncipe	51.6	2.9	...	...	32.4	...	16.1	...	1.8	94.8	10.6
Saudi Arabia	45.7	3.3	5.6	11.0	41.1	...	...	100.2	...	...	6.0
Senegal	26.6	3.1	5.8	1.6	21.7	...	7.9	16.5	1.6	27.1	3.9
Serbia	44.3	6.3	4.7	2.2	40.7	21.0	1.4	32.8	11.0	79.7	9.9
Seychelles	36.7	3.1	5.0	0.8	39.7	28.0	3.0	25.2	9.6	247.8	3.1
Sierra Leone	22.9	0.9	4.3	2.3	19.7	10.8	22.5	21.3	0.4	23.4	14.7
Singapore	19.6	1.6	3.0	4.3	18.8	13.8	...	101.4	...	...	3.3
Slovak Republic	41.5	5.7	3.6	1.5	33.6	12.4	...	0.8	...	...	3.4
Slovenia	46.3	6.4	5.7	1.8	40.7	18.3	...	2.0	...	...	2.2
Solomon Islands	48.2	5.1	...	...	49.8	...	31.3	37.3	2.1	32.4	3.3
South Africa	32.4	3.4	5.4	1.4	27.3	25.4	0.4	10.7	2.7	15.1	4.9
Spain	45.8	7.0	4.3	1.3	34.7	8.5	...	1.4	...	...	2.6
Sri Lanka	24.9	1.8	...	3.5	14.5	13.3	1.7	13.0	3.4	41.5	7.9
St. Kitts and Nevis	46.5	3.6	9.6	...	42.7	22.3	1.0	31.8	8.1	44.3	3.5
St. Lucia	35.3	5.4	4.5	...	31.0	...	4.3	20.9	5.1	47.7	3.2
St. Vincent & Gren.	39.0	3.2	6.6	...	35.2	...	5.3	20.1	5.6	37.2	5.0
Sudan	20.0	2.0	...	4.2	15.4	...	4.2	1.6	1.0	40.5	9.0
Suriname	32.9	3.7	...	...	29.9	...	5.2	17.4	...	...	17.9
Swaziland	43.1	4.0	7.8	2.1	36.6	...	1.9	21.3	1.5	15.4	7.9
Sweden	53.0	7.8	6.6	1.3	52.2	21.5	...	9.3	...	...	2.0
Switzerland	34.4	6.7	5.2	0.8	35.2	10.9	...	42.7	...	...	0.9
Syria	26.8	0.9	4.9	4.2	23.9	...	0.5	29.3	1.3	10.3	6.0
Tajikistan	28.6	1.8	3.5	...	23.4	...	8.2	...	9.6	51.2	13.9
Tanzania	26.1	3.8	6.8	1.0	21.3	...	13.7	17.2	0.8	34.0	6.3
Thailand	24.0	3.3	4.1	1.8	20.8	15.1	0.0	52.5	5.0	23.3	4.0
Timor-Leste	108.7	8.8	16.8	11.8	347.9	...	38.8	...	...	...	6.0
Togo	21.3	1.7	4.6	2.0	18.5	17.0	17.5	22.0	1.9	57.5	6.2
Tonga	31.0	4.9	...	...	28.4	...	12.7	28.8	1.2	32.8	5.9
Trinidad and Tobago	39.6	2.7	...	...	30.6	31.6	0.0	44.6	...	...	11.5
Tunisia	30.8	3.4	7.1	1.4	29.3	21.9	1.2	21.4	5.6	58.2	4.0
Turkey	37.3	5.1	...	2.8	31.7	18.9	0.2	10.9	10.1	41.2	5.7
Turkmenistan	14.7	1.2	...	...	22.4	...	0.2	...	0.9	3.0	6.1
Uganda	17.5	1.6	3.2	2.2	15.1	12.0	11.1	17.4	0.5	16.2	6.1
Ukraine	48.5	3.8	5.3	2.9	42.2	16.4	0.6	24.4	19.2	83.8	9.2
United Arab Emirates	25.8	1.9	1.2	5.6	25.3	...	...	14.2	...	...	4.5
United Kingdom	47.1	7.8	5.5	2.7	36.8	26.0	...	3.0	...	...	4.2
United States	43.5	7.9	5.5	4.7	30.8	8.2	...	0.8	...	...	2.2
Uruguay	32.3	4.7	2.8	1.6	30.6	18.8	0.2	19.0	6.2	34.5	7.2
Uzbekistan	33.6	2.5	...	...	36.7	...	0.6	...	1.9	12.5	11.6

Country	(i) Government expenditures				(ii) Revenue		(iii) ODA received	(iv) Foreign reserves, 2010**	(v) External debt (% of GNI)		(vi) Inflation (% change), 2011*
	Total*	Health	Educ.	Military	Total*	Tax			Service	Tot. stocks	
Vanuatu	27.6	3.3	4.8	...	26.8	...	15.9	23.3	0.9	20.7	4.0
Venezuela	33.0	2.4	3.7	1.3	24.9	15.5	0.0	4.5	1.2	16.7	29.8
Vietnam	33.4	2.8	5.3	2.2	24.4	...	3.9	15.9	1.2	32.3	13.5
Yemen	35.2	1.6	5.2	4.4	25.0	...	1.9	18.8	1.1	25.5	13.0
Zambia	21.4	2.5	1.3	1.7	18.9	17.1	9.9	12.9	1.5	26.8	9.0
Zimbabwe	19.6	...	...	2.8	16.7	...	13.1	...	1.9	131.4	4.8

Source: World Development Indicators (2011), unless otherwise noted

* IMF’s World Economic Outlook (April 2011)

** World Bank's Global Economic Monitor (2011)

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