5. Inclusive Growth

Inclusive growth encompasses both the Bank's focus on its twin goals of poverty reduction and sharing the benefits of growth, as well as the set of program interventions that contribute to achieving these goals in a sustainable fashion. These include: (i) the provision of social welfare and social safety nets that protect the poor and vulnerable; (ii) human development through education to raise the productivity of the poor and middle-income groups and health services; (iii) spatial programs of rural and urban development that focus on enhancing the quality of life and providing livelihoods opportunities for those who live in rural areas and urban slums; and (iv) the promotion of environmental sustainability.

The strategies adopted in the four review countries vary in the extent to which they have clearly internalized this set of challenges and made an informed choice about where to focus the Bank's efforts. The Bank program in **Mongolia** would seem to be a good practice example, with a strategic approach that is targeted to poverty reduction and shared growth; it very explicitly selects areas that will have the maximum impact. In other countries, Bank selectivity seems more arbitrary. In **Bolivia** and **Kazakhstan,** this seems to reflect the lack of interest of the government in Bank support in particular areas, whereas in **Zambia** it is mainly the lack of traction of particular programs that the Bank has supported in the past. In these countries however, there is a need to put the Bank program in this pillar into a clearer strategic framework to demonstrate the likely impact of the Bank's interventions on the achievement of the twin goals.

The implications of resource revenues for poverty reduction and social development in resource-rich developing countries (RRDCs) are not qualitatively different than the challenges that all developing countries face in promoting inclusive growth. However, the analysis of the four cluster Country Program Evaluations (CPEs) suggests the following five areas where the Bank needs to focus more intensively in RRDCs than in many other borrowing countries. The first area relates to the setting of the objectives, while the others are the four key program areas needed to address the objectives in RRDCs.

(a) **Poverty focus**. In the upward swing of the resource cycle, RRDC governments can become complacent about whether the benefits of growth are reaching the poor. Vested interests in sectors such as contracting and commercial transport become powerful and pressure the governments to undertake the kind of public construction works (airports, major highways, public buildings, and so on) which may have limited impact on poverty reduction over the medium- and even the long term. In this context, the Bank

needs to build on its diagnostic work to monitor progress and to advocate for a continued focus on poverty reduction and shared prosperity.

(b) **Social transfers**. RRDC governments are likely to be under more pressure than others to support cash transfers that allow the public at large to feel that they are deriving their share of the benefits that flow from resource exploitation. The risk is that these transfers are often poorly designed and do not meet their objectives. The Bank has an important role to play in helping governments design and implement cash transfer programs that are fiscally sustainable and that address the most urgent needs of the poor. This becomes particularly important during the downward part of the resource cycle when budgetary expenditures come under pressure. At such times, the Bank needs to advocate, and may need to provide direct support, for ensuring that the safety net for the most vulnerable is adequately funded and reaching those who are most in need.

(c) **Education and skills development**. Sustained poverty reduction requires investment in human development to build the skills and capacity needed to raise productivity and stay competitive. The availability of substantial revenues from mineral, oil, and gas resources in RRDCs has helped many of their governments achieve the Millennium Development Goal (MDG) of universal education coverage. Although the importance of this should not be underestimated, there needs to be more emphasis on enhanced education quality and skills development if the investment in human development is to have a significant impact on productivity, competitiveness, and poverty reduction. In this situation, the Bank needs to focus on and support improvement in the quality of the education system and put into place an effective monitoring system to assess quality issues.

(d) **Reaching the rural poor**. In many RRDCs, one sees the evolution of two different economies—a relatively prosperous, rapidly-growing urban economy with an expanding population, infrastructure, and large amounts of both public and private investment on the one hand, and a rural economy that is a backwater with stagnant productivity and little investment (other than for a primary school classroom) on the other. Most of the poverty is concentrated in the rural sector, where governments often lack the structures and instruments for reaching the rural poor. To support inclusive growth, the Bank needs to provide a focus on rural poverty, including piloting approaches for reaching the rural poor, and supporting the scaling up of successful approaches.

(e) **Environmental impact**. In many RRDCs, the extractive sectors are often a direct cause of environmental degradation, which needs to be addressed through effective regulations and monitoring. The Bank therefore needs to supplement its regular

program of environmental support in these countries with a special focus on the environmental implications of extractive industries.

Outcomes and World Bank Group Contribution

POVERTY FOCUS

The evaluation period covers the upswing of the price cycle between 2004 and 2013 (except for the global crises in the years 2008–09), when buoyant prices for oil, gas, and minerals not only led to increased production, but also to exploration and development of new sources. Rapid expansion and growth in the extractive sectors contributed to relatively fast rates of growth in all four CPE countries, which led to significant poverty reduction and improvement in most human development indicators (table 5.1). The only area in which there was limited progress was made was inequality.

Table 5.1. Select Economic Performance, Poverty, and Human Development Indicators

	Bolivia		Kazakhstan		Mongolia		Zambia	
Indicator	2004	Latest[a]	2004	Latest[a]	2004	Latest[a]	2004	Latest[a]
GDP per capita (current US$)	955	3,151	2,874	12,276	798	4,170	557	1,802
Poverty headcount ratio at national poverty lines (% of population)	63	45	34	3	34	27		61
Urban poverty headcount ratio at national poverty lines (% of urban population)	54	37	23	1	29	23		28
Rural poverty headcount ratio at national poverty lines (% of rural population)	78	61	47	5	43	36		78
Primary enrollment (% gross)	107	91	105	106	109	109	106	108
Life expectancy	64	67	66	70	65	68	46	58
Infant mortality (per 1,000 live births)	46	31	30	15	39	26	81	56
Gini coefficient	55	47	30	29	33[b]	37[c]	51	57

Source: World Development Indicators, World Bank.
a. Latest data available.
b. Figure from 2002;
c. Figure from 2007.
Note: GDP=gross domestic product.

Kazakhstan made steady progress on all key indicators, including an increase in life expectancy; a reduction in maternal and infant mortality rates; and achievement of three of the MDGs (reduction of poverty by half; universal primary education; and gender equality in education). Poverty data show a very impressive decline from 34 to three percent[1], although the numbers are hard to confirm as the Bank's last poverty assessment in the country was conducted in 2004. In **Mongolia,** the decline in poverty was most impressive between 2010 and 2012, falling by an average of five percentage points per year. Whereas poverty has declined, the gap between rich and poor in Mongolia has widened, with the gains in income for the better-off outstripping the impact of rapid growth on the poor. **Bolivia** has seen the most impressive reduction in extreme poverty, despite slightly lower growth rates compared to the other three countries. This could be explained by the expansion of small businesses; growing employment in the services sector; direct transfers to the poor from an increased share of rents from natural gas; and shifts in the terms of trade in favor of agricultural products from which many of the rural poor derive their income. The outlier in this group is **Zambia**, where despite growth, poverty incidence remains very high. Rural poverty, at 74 percent, is more than double the level in urban areas. There was a steady increase in inequality over the review period, reflecting a high concentration of growth in urban areas and among the large commercial farmers and entrepreneurial and professional groups.

In **Bolivia**, **Mongolia**, and **Kazakhstan**, a number of factors contributed to poverty reduction, including a combination of: cash transfers; growth of employment in the services sector (urban poverty); and a sustained program of outreach to rural areas with the promotion of education, health, infrastructure, and support for livelihoods. Productivity improvements did not seem to have played a significant role. The story in **Zambia** is a complex one. Although the government did not derive much in the way of revenues from copper mines, a great deal of additional fiscal space was created through the country's Highly-Indebted Poor Countries (HIPC) completion in 2005, as well as higher revenues through the growth of the urban economy and commercial agriculture. While initially there was a major expansion of expenditures on health and education, in more recent years, resources have been used for a substantial increase in public sector salaries and for expanding the country's physical infrastructure. Very little growth has reached the small farmers in rural Zambia as government expenditures have targeted mainly the urban core of the country. As a consequence, the rural poverty headcount has increased with population growth.

As experience in the four CPE countries shows, the direct impact of growth in extractive industries through employment generation (directly, or indirectly, through demand for inputs, or development of downstream processing) could be rather limited: for example, the Oyu Tolgoi copper mine in **Mongolia**, one of the largest in the world, is

expected to cost about $20 billion to develop (until 2019). It is expected to account for about 30 percent of the country's gross domestic product (GDP) at full production, but will have only 3,000 to 4,000 employees at that point. In addition, in most RRDCs, the extractive industries have made little use of tradable domestic inputs, or led to the development of downstream processing[2]. The multinational companies that develop these resources generally have facilities elsewhere that they use for the sourcing of inputs or processing of outputs.

The limited spill-over from extractive industries puts most of the weight on governments to meet the expectations of the public at large. During periods of new oil, gas, or mining development, there is increasing buildup of political pressure on governments to meet expectations that the resources will translate rapidly into higher incomes and provision of more and better public services. In **Mongolia** and **Zambia**, this has made it difficult to resist populist calls for the pro-cyclical use of resources. In both countries, governments have amplified the impact of the resource boom by running up sizeable budget deficits, using expansionary monetary policies, and borrowing abroad. The Bank's role in this situation is to ensure that government revenues derived from natural resources are used in ways that maximize their impact for achieving sustainable poverty reduction.

Effective advocacy requires both analytic work and policy dialogue on poverty reduction. Yet these have not been a prominent feature of the Bank program in most reviewed countries. In **Zambia**, where the issue is most urgent, the Bank's analytic work on poverty culminated in the 2012 Poverty Assessment entitled *Stagnant Poverty and Inequality in a Natural Resource-Based Economy.* In spite of wide dissemination, the report seems to have had little traction. In the other three countries, some work was done at the beginning of the evaluation period. However, there has been no subsequent poverty analysis. The last two strategies of the Bank Group in **Kazakhstan** do not mention poverty reduction as an explicit objective, nor do they track poverty indicators.

Effective poverty analysis requires reliable data on poverty, and this, in turn, implies arrangements for monitoring through regular surveys. The Bank has been active in both **Zambia** and **Mongolia** on supporting arrangements for collecting better poverty data, and aligning the surveys supported by the Bank with those of the national statistics bureaus. In Mongolia, this led to the adoption of a new methodology in 2012 to make a quantitative assessment of poverty rates and assess poverty dynamics. This is a noteworthy achievement compared to the mid-2000s, when the official poverty numbers were estimated using inconsistent poverty lines—and drawing erroneous conclusions on poverty trends over time.

SOCIAL TRANSFERS

Developing country governments provide cash transfers in several ways, among them: (i) the pension system to the elderly; (ii) unconditional cash transfers (which can be universal, but are usually social welfare payments to vulnerable groups); and (iii) conditional cash transfers that promote the achievement of various educational- or health-related goals.

The Bank has been actively engaged in policy advice and analysis on pensions in three of the four countries reviewed. Advice on pension reform was an important part of the Bank's policy dialogue in **Kazakhstan**, driven by strong demand from the government.[3] The Bank also conducted timely analytical work at the request of the **Mongolian** government to evaluate the pension scheme and propose policy reforms.

In addition to pensions, countries need to put into place comprehensive social safety nets. This is becoming an increasingly urgent issue in many RRDCs, where governments are under growing pressure to spread the natural resource wealth in the most direct and efficient manner. A key element in the Bank approach has been to advocate for programs targeted to the poor. This reflects the evidence that universal programs have substantial leakages of funds to the non-poor and are likely to be fiscally unsustainable. Moreover, targeted programs are difficult to administer, require information on incomes, and are subject to elite capture and diversion of resources. In addition to policy advice, this has meant that governments would need to put in place the administrative capacity for effective implementation.

The difficulty of moving in this direction is evidenced by the Bank's engagement with the **Mongolian** government over its universal Child Money Program (CMP). In 2005, the CMP was introduced on a targeted basis, and in 2006, it was expanded to universal coverage. The Bank's analytical work clarified for policy makers the limited impact of the universal program on poverty reduction—and its fiscally high and unsustainable cost. As a result, the government adopted the Social Welfare Law (SWL) in 2012 to overhaul the system through the introduction of the Poverty Targeted Benefit (based on a proxy means test), and a substantial consolidation of benefit programs. However, this became a contentious issue in the subsequent election and, to date, the law has still not been implemented.

Given its importance for both fiscal stability and poverty reduction, the Bank needs to be involved in supporting the design of appropriately scaled and efficient cash transfers in RRDCs. Politically, it is often difficult to withdraw a benefit once it has been given. Therefore, it is important that the Bank engage with governments during the early phases of resource exploitation when significant revenues begin to flow into the budget. In this way, it can help governments design a modular approach that can be expanded

over time in relation to fiscal affordability. In addition, the Bank needs to assist governments in carrying out periodic monitoring and evaluation regarding the poverty impact of fiscal transfers. Bank engagement in this area with RRDCs is especially important given the inherent instability of mineral and oil resource revenues, and the likelihood that when price or production shocks occur, poorly designed transfer programs will not be sustainable. [4]

EDUCATION AND SKILLS DEVELOPMENT

All of the CPE countries were making substantial progress toward achieving the access to education objectives of the MDGs. The growing concern (especially in the poorer countries) was that the system was not meeting the needs of the labor market (producing the new skills that a rapidly growing and diversifying economy was likely to require) and achieving the productivity gains necessary to escape poverty and reduce vulnerability. Bank programs in all countries concentrated on improving education quality, mainly primary and secondary. However, there were very few attempts to address skills development and vocational training.[5]

In spite of a relatively limited role for the Bank in **Kazakhstan,** it has had a visible impact in basic education, where it focused on supporting the government's efforts to improve quality. The Bank's contribution is widely credited by IEG interlocutors in introducing universal pre-school education. The Bank has made a major contribution to enhancing the quality of primary education in **Mongolia** through policy dialogue and its lending program. Bank projects introduced reforms in rural primary schools that are now being scaled up at the national level through government policies. In **Bolivia**, the Bank had traditionally successfully supported primary education reform, as well as education decentralization. During the evaluation period, the Bank shifted its support from national reforms to smaller scale municipal pilots, as the then new government showed little interest in policy reform and Bank assistance. The possibility of the pilot programs to serve as a testing ground for broader reforms has not materialized, as the government has not been interested in sectorwide reforms.

The Bank's involvement in improving the quality of education has achieved an important first step of building awareness, but it now needs to move to a second stage. The Bank is playing an important role in keeping the focus on quality and on helping governments develop programs in this area. This would seem to be a major comparative advantage of the Bank. However, to move beyond advocacy, the Bank needs to strengthen its analytic work to identify the steps needed for better quality and curriculum reform, help put monitoring systems in place, and evaluate the structure of secondary and tertiary educational institutions and the policy framework for skills development.

REACHING THE RURAL POOR

In most of the reviewed countries, poverty is becoming more and more concentrated in the rural areas. The key cities and mining towns benefit more directly from the earnings from natural resources. Their incomes rise with the demand for labor in construction and services. The traditional farming population is often poorly placed to meet the additional demand for more and better quality foodstuffs and other crops. As a consequence, they benefit little from this growth, except through labor migration and remittances. The evidence suggests that an active program of rural development and the promotion of agricultural value chains is needed to achieve a significant impact on rural poverty.

The most striking example of Bank support for rural development comes from **Mongolia**, where rural living conditions have dramatically changed for the better since the mid-2000s. The Bank's program covers several activities that seem well coordinated on the ground and have jointly produced important learning and synergies. Mission evidence suggests that the rural program as a whole merits recognition as best practice. Bank-supported projects created synergies that reinforced support for higher living standards for herder households, and the adaptation of the traditional nomadic way of life in a modern, growing economy[6].

Some important lessons for future livelihood support can be derived from these country studies. The **Mongolia** experience shows the impact that the Bank can have through a holistic approach to rural development, capturing the synergies from a number of separate programs focused on rural development. The Bank is following a similar approach in its program in **Bolivia**. The poverty assessment in **Zambia** takes the opposite line, arguing that: "marginal improvements in economic and social indicators can be accomplished through targeted interventions in the rural economy, but enduring, structural income growth and the widespread reduction of poverty will only be achievable through broad-based employment creation in the urban industrial and service sectors." The cross-country view which this cluster CPE enables, would strongly support the argument that this is not an either/or proposition. An entirely urban-focused program would leave a large reservoir of rural poverty in countries such as **Zambia,** and some of the newly-emerging RRDCs for many years into the future.

ENVIRONMENTAL IMPACT

The four countries in the cluster have all been richly endowed with natural resources, including land, forests, water, and biodiversity. In every case, their rich natural endowment has been gradually degrading under a variety of pressures arising from their unregulated economic development, ranging from overgrazing and the expansion of the agricultural frontier, to the growth of air and water pollution from industrial and

extractive activities. Some of these pressures have been aggravated by the countries' vulnerability to climate change, with the attendant increase in the frequency of extreme weather events. In every case, the countries' response had been limited by inadequate policy frameworks and weak institutional capacity to enforce the applicable environmental laws and regulations. Underlying these common elements, each country was facing a set of very specific challenges.

The mitigation of extractive industry environmental impacts was a major focus in Zambia and Mongolia, and was addressed through safeguards in Kazakhstan. In **Zambia**, the Copperbelt Environment Project mitigated environmental liabilities to facilitate the privatization of the copper industry. However, continuing reports about mining sector chemical spills have raised concerns about the long-term sustainability of the benefits. In **Mongolia**, a wide array of complementary components in various projects have helped to deepen the understanding of the potential impacts of mining development, strengthen the policy and institutional framework, and prepare the infrastructure for managing the environmental and social impacts of mining. In addition, the International Finance Corporation's (IFC) involvement with Mongolia's two largest mining projects provides comfort that their environmental and social management provisions are in line with international norms. In **Kazakhstan**, the Bank and IFC's early petroleum projects helped to: successfully update enterprise environmental and social policies and procedures; introduced sophisticated pollution abatement technologies; and cleaned up past damage.

The strengthening of the institutional and policy framework for the environment was part of every Bank intervention. In **Bolivia**, the Bank helped create institutions and organizations needed to manage and conserve biodiversity. In **Zambia,** Bank projects helped strengthen national park management and environmental control capacity. Nevertheless, the long-term sustainability of these projects' achievements has been affected by a lack of general support from the government for policy, legal, and institutional reforms. In **Mongolia**, the Bank directly contributed to the expansion of the Ministry of Environment's mandate and power, and helped promote the development of a vibrant civil society constituency. In **Kazakhstan**, the successful remediation of past legacy issues[7] helped strengthen the capacity of key environmental agencies. Indeed, their continuing sustainability appears assured by their very visible success and continuing government support.

Conclusions

In all four RRDCs, the commodity price boom and economic growth led to broad improvements in poverty and human development indicators, but also led to a

widening income gap and rising inequality. The outcomes of Bank Group activities aimed at helping countries share the benefits of growth with the wider population and improve human development outcomes were generally positive (with the exception of Bolivia, because of a fundamental mismatch with the interests of the line ministries). This occurred despite the generally small (and declining) size of Bank programs in these areas and the diminishing interest of the authorities. The reasons for a given country's lack of enthusiasm varied from general skepticism about the utility of Bank advice on poverty and education to the unwillingness to acknowledge the persistent poverty problem for political reasons. However, the high impact of Bank activities in these areas relative to their size serves as proof of the Bank's comparative advantage and global expertise. Further, it also underlines the importance of this aspect of the Bank's mandate as a global development institution. The following findings emerge from the experience in the four countries reviewed:

- There is a need to design a program of advocacy for poverty reduction and better sharing of the benefits of growth. It should be based on poverty analysis, support for improved data collection, and poverty monitoring.
- Early and sustained engagement in the design of targeted cash transfers is necessary. The Bank has sometimes been reluctant to intervene in this area because it tends to be highly politicized. Subsequently, when the fiscal situation deteriorates, the International Monetary Fund and the Bank have little choice except to condition support on a government's agreement to change the system of poorly-designed transfers.
- There is a need to emphasize education quality and skills development as a key factor in raising the productivity of the poor. Although governments in all of the reviewed countries are putting substantial resources into the education sector, the benefits are less clear at this stage.[8] The Bank's focus on quality is well founded. An effective start has been made through creating a consensus around the need for quality improvements. These efforts need to be taken to the next stage through broad-based programs that start with good analytic work and better monitoring of education outcomes. Good practice interventions such as the Rural Education and Development (READ) project in Mongolia should be widely disseminated.
- A well-designed rural development program should be a key feature of Bank involvement in RRDCs. Whereas the growth generated by extractive industries development generally reaches the urban areas through demand for construction workers and the services sector, it does not trickle down to the rural economy at a pace that is likely to impact poverty and living standards. Bank programs can help steer government expenditures and focus toward the rural economy. What is particularly encouraging is how successful many of the Bank rural

development interventions have been. The Mongolian rural program is a major achievement and merits wider dissemination in the Bank and other countries.

- Continued support for the mitigating environmental impacts of extractive industries and dealing with past legacy issues is important. This has been an area of satisfactory Bank Group interventions, as it had successfully brought both the public and private sectors to a realization of the costs of neglect—as well as the impact of a better environment on the population's quality of life.

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[1] The current poverty line in Kazakhstan is set at $2.25 per day, which is considered very low for an upper-middle-income country (approaching high-income country threshold).

[2] An exception is Botswana, where the government has required De Beers to move its headquarters and also a significant proportion of diamond cutting and polishing to the capital of Gaborone.

[3] A report of the World Bank offered guidance on tackling the issue of income adequacy for future pensioners in a sustainable way. It was used by the Bank and the government to inform a high-level brainstorming session in 2012 on the topic of pension reform.

[4] Chile is an example of a resource-rich country that has set aside funds generated by the sale of natural resources to act as a hedge against the fluctuations of global commodity prices and provide a buffer to economic crises. During the global crises of 2008–09, a large part of the resources drawn from the Stabilization Fund allowed financing of bonus (direct unconditional transfers) for the bottom 40 percent of the population.

[5] There was only one Bank project on technical and vocational training and it was in Kazakhstan. The Technical and Vocational Education Modernization Project (FY10: ongoing, expected to close in 2015) was too early to evaluate.

[6] The Bank's projects have changed the way herders provide for livestock pasture and fodder needs; have access to the closest source of water; receive warnings about bad weather; buy livestock insurance; benefit from improved primary education for their children; receive better medical services; participate in local planning and investment decisions; and use energy to watch television, store food, and communicate with their families by mobile telephones.

[7] The most famous one is the partial restoration of the Northern Aral Sea that transformed a massive region that had become uninhabitable into one where people are returning and restoring their livelihoods.

[8] In Botswana, the Finance Ministry has become increasingly frustrated by the lack of improvement in education quality outcomes despite steady increases in expenditures in the sector. It has decided to stop increasing outlays until the Ministry of Education can demonstrate better quality outcomes.