

Cooperation with Middle Income Countries

Concept note

1. International Development Cooperation and Middle Income Countries

According to the World Bank, Middle Income Countries (MICs) are those with a Gross National Income (GNI) per capita between 1,036 USD and 12,615 USD; this category is in turn divided between lower middle income (\$1,036 - \$4,085) and upper middle income (\$4,086 - \$12,615).

MICs are a heterogeneous and diverse group by size, population and income level, development potential, and economic and social achievements and performance. They are home to 5 of the world's 7 billion people and 73% of the world's poor,¹ with poverty rates ranging from around 2 percent to more than 60 percent². MICs also represent about one-third of global GDP and are major engines of global growth.³

At a policy level, the current classification has had important implications because the thresholds are used in various ways by a number of bilateral and multilateral donors, as well as by various non-development actors (such as investment ratings agencies) in their decision-making processes to determine the terms of engagement with the countries included in this category.⁴

However, a concept that is based exclusively on an indicator as limited as GDP per capita overlooks the broadly recognized fact that development is a complex, non-linear process. On the one hand, it creates a group of countries that encompasses many different realities, both in terms of challenges and vulnerabilities, as well as in terms of capacities and potential. MICs differ greatly among themselves not only with regards to socioeconomic conditions, but also in structural circumstances that determine their potential for development and production performance.⁵ Some MICs (particularly in the lower tier of the classification), still have challenges and conditions similar to other country categories.

The Human Development Report in 2013 "The Rise of the South" describes the unprecedented speed in which the dynamics of power, voice and wealth in the world are evolving, while formidable challenges are faced in the Global South and that they represent a highly heterogeneous group of countries, with diverse challenges and country context.

In particular it is important to point to the fact that classifying countries according to their income level is related to the idea that countries need to assume the responsibility of their own development after reaching a certain level of economic activity ("graduation"). In this sense, using income as the main defining criterion has important consequences as it determines the amount of development assistance received, as well as the more or less favorable conditions with which it is delivered—the larger or lower degree of concessionality.

¹ World Bank, "Middle Income Countries Overview", <http://www.worldbank.org/en/country/mic/overview> [last accessed August 16, 2013].

² General Assembly, *Development cooperation with middle-income countries, Report of the Secretary-General, Sixty-four session, A/64/253*, August 5, 2009, para. 10.

³ World Bank, "Middle Income Countries Overview", *op. cit.*

⁴ Andy Sumner, "Global poverty and the 'New Bottom Billion' Revisited: Exploring the Paradox that Most of the World's Extreme Poor no Longer Live in the World's Poorest Countries", Working Paper, May 14, 2012, p. 3.

⁵ Economic Commission for Latin America and the Caribbean, *Middle-Income Countries: A Structural-Gap Approach, Note by the Secretariat*, Thirty-fourth session, LC/G.2532(SES.34/11), July 23, 2012, p. 13.

The rationale for Official Development Assistance (ODA) allocation in recent decades has been to channel the bulk of ODA towards Low Income Countries, including those classified as Least Developed Countries (LDCs). The logic behind this is that since MICs have higher average incomes, their needs should be relatively lesser,⁶ as suggested by the so-called “graduation” process. Thus, traditional donors tend to focus their aid activities on countries that have been identified as priorities, at the expense of MICs.⁷ ODA has fallen by 6% in real terms over the last two years, decreasing on two consecutive years for the first time since 1996-97⁸, with MICs being among the most affected by this falling trend.

The 2009 UN Secretary-General Report on Development Cooperation with Middle Income Countries acknowledges that the use of GNI per capita as the sole classification criteria has played its part in this problem, considering that “the legitimacy and relevancy of using this [World Bank’s] definition as the benchmark for guiding development cooperation policy of the United Nations system should be questioned.”⁹

Several MICs have the potential to catch up with High Income Countries, while many others face the risk of losing ground on previous achievements and falling into the low income category,¹⁰ as they are, in varying degrees, vulnerable to economic crises and external shocks.¹¹ The financial crisis of 2008 revealed the fragile capacity of MICs in dealing with the vicissitudes of external variables. Therefore, enhancing their capacity to cope with external shocks must be considered an integral part of their development strategy for maintaining sustained robust growth in the long run.¹²

On the other hand, many upper MICs face great domestic inequalities, with some geographical areas presenting problems similar to those of other categories of developing countries, while in others (such as urban areas) challenges are more related to income distribution. Such challenges are complex and structural, and relate to the intergenerational reproduction of poverty, only likely to be fully tackled by a combination of short, mid, and long term policies.

Taking these elements into account, it is possible to affirm that despite a welcomed general increase in economic growth and demographic potential, MICs are still developing countries with major domestic development challenges, such as inequality, lack of access to basic services

⁶ Economic Commission for Latin America and the Caribbean, *Financing for Development and Middle-Income Countries: New Challenges*, LC/L.3419, November 2011, p. 12.

⁷ In 1990, MICs received on average a greater portion of ODA than did low-income countries (55% versus 45%). By 2010, the share of MIC had dropped significantly, and they were receiving only half the volume of ODA flowing to low-income and least developed countries. Economic Commission for Latin America and the Caribbean, *Middle-Income Countries: A Structural-Gap Approach, Note by the Secretariat*, Thirty-fourth session, LC/G.2532(SES.34/11), July 23, 2012, p. 5.

⁸ Official Development Assistance has been steadily decreasing since the global financial crisis. From its crest in 2010, ODA has dropped almost 6% in real terms. The year of 2012 witnessed the most significant reduction of ODA since 1997. It is also the first time that ODA fell in two consecutive years since 1996-1997. In 2011, it dropped 2% with regards to 2010 levels, and 2012 registered a decrease of 4% with regards to 2011.

⁹ General Assembly, *Development cooperation with middle-income countries, Report of the Secretary-General*, Sixty-four session, *op. cit.*, para. 84.

¹⁰ In fact, several countries have moved between the MIC and the LIC category over the past two decades. Fourteen countries moved from the Low Income to the Middle Income classification, including India, Maldives, Sri Lanka, and China; seven fell back to the low income group, including Kyrgyzstan, Tajikistan, Uzbekistan, and Zimbabwe; and twenty-one temporarily dropped back to the low income group at least one time during the last two decades. *Ibid*, para. 18.

¹¹ *Ibid*, para. 6.

¹² *Ibid*, para. 30.

and vulnerability both at the individual and collective levels. As such, in order to avoid the “middle income trap”, MICs are still in need of international support to catalyze their own economic, social, and structural transformation.

The support required by MICs might be as diverse as MICs themselves. Recognizing that ODA flows remain essential in some cases, for others, particularly Upper Middle Income Countries, the main emphasis should be on capacity building in matters related to public policies, knowledge sharing, and exchange of experiences and lessons learned. While for some countries the aid of bilateral donors and agencies is still relevant, for others the support of international organizations in particular and focalized areas seems to be the more appropriate mechanism.

2. Diversity and inequality among and within Middle Income Countries

MICs diverge greatly in terms of the strength of their social, political, and economic institutions, representing important opportunities for international assistance; many countries are in great need of international assistance while some other are progressively becoming providers in the South-South Cooperation tradition or participate in Triangular Cooperation schemes.

MICs have performed very differently in their efforts to achieve the Millennium Development Goals (MDGs). Even in fast-growing economies, new prosperity and an expanding middle class often accompany high maternal and child mortality, malnutrition and inferior access to health care and sanitation in less developed regions, creating pockets of deprivation among disadvantaged groups and in certain geographic areas. Addressing the “residual traditional” development agenda is necessary for the full achievement of the MDGs and other internationally agreed development goals. It includes tackling challenges in economic and democratic governance.¹³

Inequality influences poverty through multiple channels; where inequality is high, growth is less effective in reducing poverty, as inequality decreases the extent to which the poor benefit from overall growth. There is also growing evidence that high levels of inequality, particularly in terms of opportunities and among regions or ethnic groups, may fuel violent conflict and jeopardize social stability, thereby undermining development and poverty reduction, as was recently experienced in parts of North Africa and the Middle East.¹⁴

One of the main problems of the World Bank’s classification system is that it does not account for the increasing inequality within and among MICs, both in terms of their ever-growing internal development gaps and of the differentiated treatment they are given as cooperation recipients. Income inequality represents a major challenge for MICs, with great development differences between those at the top of the category and those at the bottom. Domestic differences are also significant when weighing structural features related to poverty and performance in terms of productivity and participation in world trade, among others.¹⁵ The following table shows the differences between and among MICs using a few countries as examples:

¹³ “Middle-income countries: The role and presence of the United Nations for the achievement of the internationally agreed development goals”, Joint Meeting of the Executive Boards of UNDP/UNFPA /UNOPS, UNICEF, UN-Women and WFP, January 30-31, 2012, New York, para. 5.

¹⁴ General Assembly, *Development cooperation with middle-income countries, Report of the Secretary-General, Sixty-sixth session, A/66/220*, August 1, 2011, para. 16.

¹⁵ Economic Commission for Latin America and the Caribbean, *Middle-Income Countries: A Structural-Gap Approach...*, *op. cit.*, p. 13.

HETEROGENEITY AMONG MIDDLE INCOME COUNTRIES: INCOME CONCENTRATION AND INEQUALITY							
	Country	GNI per capita 2012 ¹⁶ (USD)	Income share held by highest 10% ¹⁷	Income share held by highest 20% ¹⁸ (percentage)	Income share held by lowest 10% ¹⁹ (percentage)	Income share held by lowest 20% ²⁰ (percentage)	Classification by Human Development Index, 2013 ²¹
Higher MICs	Venezuela	12,470	33	49	1	4	71
	Hungary	12,390	25	40	4	8	37
	Seychelles	11,640	60	70	2	4	46
	Brazil	11,630	43	59	1	3	85
	Mexico	9,740	38	53	2	5	61
Countries between high and low MICs	Belize	4,180	42	58	1	3	96
	Tunisia	4,150	28	43	3	7	94
	Algeria	4,110	27	43	3	7	93
Lower MICs	Yemen	1,010	31	45	3	7	160
	Mauritania	1010	32	47	2	6	155
	Senegal	1,040	31	47	2	6	154

Taking these issues into consideration, the Economic Commission for Latin America and the Caribbean (ECLAC) has openly stated that the practice of allocating ODA on the basis of per capita income presents two main shortcomings. First, poverty alleviation is both cause and effect of development, which is a multifaceted process involving efforts by countries to overcome a wide range of structural gaps that constrain and hinder inclusive growth, and such a complex process cannot be appropriately reflected on a single indicator. Second, this practice presupposes that the categories of low, middle and high income countries are relatively homogenous in terms of their economic and social needs,²² when in fact they are very different in terms of poverty rates, social inclusion, and productive, institutional, and financial capacity.²³

ECLAC proposes a method based on a set of structural gaps: poverty, inequality, investment and savings, productivity and innovation, infrastructure, education and health, gender, the environment, and fiscal structures. The gaps-based approach stresses that there is no single hierarchy for needs and the identification and ranking of priorities must rely on individual decisions by countries. However, much work is still needed to reach consensus on a new set of criteria that focuses on the people in need instead of on the economic performance of their countries.

¹⁶ World Bank, *Gross national income per capita 2012, Atlas method*.

¹⁷ World Bank, *World Development Indicators 2013: Distribution of income or consumption*.

¹⁸ *Ibid.*

¹⁹ *Ibid.*

²⁰ *Ibid.*

²¹ United Nations Programme for Development, *Human Development Report 2013, The Rise of the South: Human Progress in a Diverse World*, New York, 2013, p. 143.

²² Economic Commission for Latin America and the Caribbean, *Middle-Income Countries: A Structural-Gap Approach...*, *op. cit.*, p. 3.

²³ *Ibid.*, p. 5.

3. MICs and the Development Effectiveness Agenda

In the context of decreasing aid and continuous development and poverty challenges, the quality of international cooperation becomes paramount. The Global Partnership for Effective Development Cooperation (GPEDC) can be an important platform for MICs to put forth their call not only for more development cooperation in terms of volume, but for better cooperation and enhanced effectiveness. The development effectiveness agenda focuses on maximizing the impact of cooperation on the ground, or put another way, increasing value for money. Its objective is to ensure that cooperation flows act as catalyzers for national development efforts, and that they are strategically directed where they are most needed.

As for the role of MICs as Southern providers, the GPEDC is a space to engage in discussions regarding the rightful place of MICs within the new development cooperation architecture, for it brings together all the relevant stakeholders in search of constructive dialogue. It is essential to open this debate and promote a more integral classification system that appropriately addresses the differences between the countries that are currently classified as MICs, as well as their specific needs in terms of cooperation and the new roles that some of them are now in a position to assume, particularly in the global financing for development dialogue in the post 2015 framework.

It should be clear that this discussion is not intended to increase cooperation flows to MICs at the expense of Low Income Countries or Least Developed Countries, which rightfully are at the center of the international community's efforts. The focus is rather set on the most effective way to integrate the different actors and cooperation traditions, building on their comparative advantages and exploiting synergies, to maximize their joint efforts towards the achievement of our common goal: global sustainable development.

There are many actions that all stakeholders can engage in to improve the effectiveness of their cooperation exchanges with MICs, which can be assessed through the Global Partnership's Monitoring Framework:

- As recipient countries, MICs must play an active role in establishing their development objectives, identifying the areas where their needs and challenges are greatest. This key principle of *country ownership* was adopted and emphasized by the Paris Declaration, and after that by the Busan Final Document.
- They must also work together with development partners and other important actors to ensure better coordination of their efforts, guided by a determined *focus on results*. With over half of the world's poor population concentrated in these countries, effective development actions that yield tangible results may have a significant impact on the achievement of the Millennium Development Goals.
- For these joint efforts to succeed, it is essential that all parties participate according to their own capabilities, and on the basis of *inclusive development partnerships*. Innovative schemes that build on comparative advantages to create added value. Triangular Cooperation or public-private partnerships should also be multiplied and continuously enhanced.
- Finally, a major area of opportunity lies on the improvement of transparency schemes for mutual accountability, not only for its importance in order to build trust and lasting cooperation relations, but also because timely evaluation and monitoring provides the necessary tools to identify gaps in development assistance programs and development challenges that may have gone undetected, allowing actors to avoid repeating mistakes and enhancing the effectiveness of their development interventions.

There are also many positive externalities of assisting MICs. As providers of cooperation (particularly Upper MICs) the strengthening of their institutional capabilities can have a multiplying effect for development at the regional and global levels. MICs are critical drivers of the world economy, with knowledge and resources to share. For example, MICs played a decisive role in supporting the poorest countries through the latest financial crisis on account of well-developed trade relations and remittances, contributing to about half of the post-crisis recovery of the world economy.²⁴

Investment on MICs may serve as a catalyzer to achieve more global development objectives, not only because of the direct impact it may have on millions of the world's poor, but also because it can facilitate the necessary capacities for higher MICs to assume responsibilities within the international cooperation architecture (South-South tradition and Triangular Cooperation), promoting the development of other MICs and Low Income Countries. As well as offering stable trading opportunities, these spillover effects also include debt relief, technical assistance and cooperation to support infrastructure investment, trade finance, institution building, public administration reform and humanitarian assistance.²⁵ Inclusive and sustainable growth and development in MICs provide positive spillovers to the rest of the world in terms of poverty reduction, international financial stability, and improvement on cross-border global issues, such as climate change, energy, food and water security, and international trade.²⁶

Middle income countries are of systemic importance in key areas that have the characteristics of global public goods including among others the reduction of poverty, global economic and financial stability, orderly flows of trade, protection of the environment, creation of knowledge, disease prevention. Growth and stability in MICs therefore posts a considerable potential benefit for the rest of countries and works towards global stability and peace.

While the focus may vary from country to country, the priorities for cooperation with MICs as a group must be centered on areas such as poverty eradication, improvement in governance, reduction of economic and social inequality, greater diversification to reduce vulnerability of trade and external financial shocks, improved capacity for South-South cooperation, and technology transfer and finance to tackle climate change.²⁷

The development effectiveness agenda can play a major role in ensuring that cooperation with MICs is efficiently focused on improving these countries' living conditions by targeting their most pressing needs and improving the way in which national and international efforts complement and reinforce each other, and additionally promoting MICs' ability to become positive agents of change for other country categories.

²⁴ General Assembly, *Development cooperation with middle-income countries, Report of the Secretary-General, Sixty-sixth session, op. cit.*, para. 7.

²⁵ Jonathan Glennie, "The role of aid to middle-income countries: a contribution to evolving EU development policy", Overseas Development Institute, Working Paper 331, June 2011, p. 12.

²⁶ World Bank, *Middle Income Countries Overview*, *op. cit.*

²⁷ General Assembly, *Development cooperation with middle-income countries, Report of the Secretary-General, Sixty-four session, op. cit.*, para. 79.

Guiding Questions

Participants of the session on “Cooperation with Middle Income Countries” should focus their discussion on the following questions:

- What is the role of the international community in supporting MICs? Can the support of the international community to MICs have an impact in their own role as South-south Cooperation Providers?
- How can Middle income countries have a prominent role in the system of international cooperation in line with their importance in the international economy and their development needs?
- How can they become effective development actors, while at the same time struggling with important domestic challenges?
- What should a new set of criteria for country classification look like? How can the Global Partnership contribute to the discussion of a new classification system that truly reflects development needs and priorities, without affecting the most vulnerable?
- In the context of fiscal constraints for donor countries, how can MICs ensure that the cooperation they receive is effectively channeled to achieve maximum results?
- What are the most important challenges facing cooperation with MICs from the point of view of other relevant actors (donor countries, recipient countries, non-traditional actors)?
- How can MICs engage in innovative partnerships with other relevant stakeholders to generate action-oriented synergies?
- What kind of incentives can motivate countries to avoid slipping back or stuck in the middle-income trap, as well as for MICs to make effective use of cooperation in managing the transition effectively?
- What are the means and methods to identify gaps and effective ways to address the political dialogue between donor and beneficiary?