

# **ADB RETA-6397: Strengthening Country Diagnosis and Analysis of Binding Development Constraints in Selected Developing Member Countries**

**4 June 2008**

**Juzhong Zhuang  
Assistant Chief Economist  
Asian Development Bank**

**Jasmine Rajbhandary  
Social Development Adviser  
DFID Nepal**

# **A. The Project**

# I. Background

- Paris Declaration calls for aligning development assistance with partner country priorities; and for supporting the development of their capacity for development planning and implementation.
- ADB has undertaken several initiatives to implement the commitments made under Paris Declaration. One initiative is to better align CPS with DMC's own planning processes and make greater use of their diagnostic and analytical work.
- ADB also recognizes the value of assistance to DMCs in strengthening their capabilities for undertaking diagnostic and analytical assessments.

## II. Objectives of the RETA

- The RETA was approved in May 2007, aiming to strengthen diagnosis and analysis of binding development constraints in selected DMCs:
  - **Impact** - Enhanced development impacts of the DMCs' own interventions and ADB's operations.
  - **Outcome** - Enhanced capacities of DMCs to undertake development diagnostics and formulate development plans/ strategies.
  - **Outputs** – Improved understanding of the selected DMC economies and their binding constraints to development.

# III. Country Diagnostic Studies

- Includes 4 country studies; Philippine study completed in 2007; Nepal for completion in 2008
- Nepal country study is unique as it will be jointly undertaken by Government of Nepal, ADB, DFID and ILO
- The Nepal study will involve:
  - Reviewing development performance and patterns,
  - Formulating a set of hypotheses and testing of binding constraints, and
  - Formulating policies to address the binding constraints.

# **B. Methodology**

# I. Concept of Inclusive Growth

- Defining inclusive growth requires a distinction between inequalities related to efforts and inequalities related to circumstances (Roemer 2006).
  - Inequalities due to differences in circumstances reflect inequalities in opportunities and are not acceptable.
  - Inequalities due to differences in efforts reflect functioning of market-based incentives, and should not be disregarded.

# I. Concept of Inclusive Growth

- This distinction enables differentiation between “inequality in opportunities” and “inequality in outcomes”.
  - Inequalities in opportunities are due to differences in circumstances and reflect social exclusion and injustice;
  - Inequalities in outcomes partly reflect differences in circumstances and partly in efforts.
- Inclusive growth is growth with equal access to opportunities.

# I. Concept of Inclusive Growth

- **Inclusive growth strategy needs two policy pillars:**
  - High and sustainable growth to create economic opportunities;
  - Social inclusion to ensure equal access to the opportunities by all.
- **Promoting social inclusion requires:**
  - Investing in education, health, infrastructure, and other social services to expand human capacities ;
  - Promoting good policy and sound institutions to advance economic and social justice and level playing fields ;
  - Developing social safety nets to prevent extreme poverty.

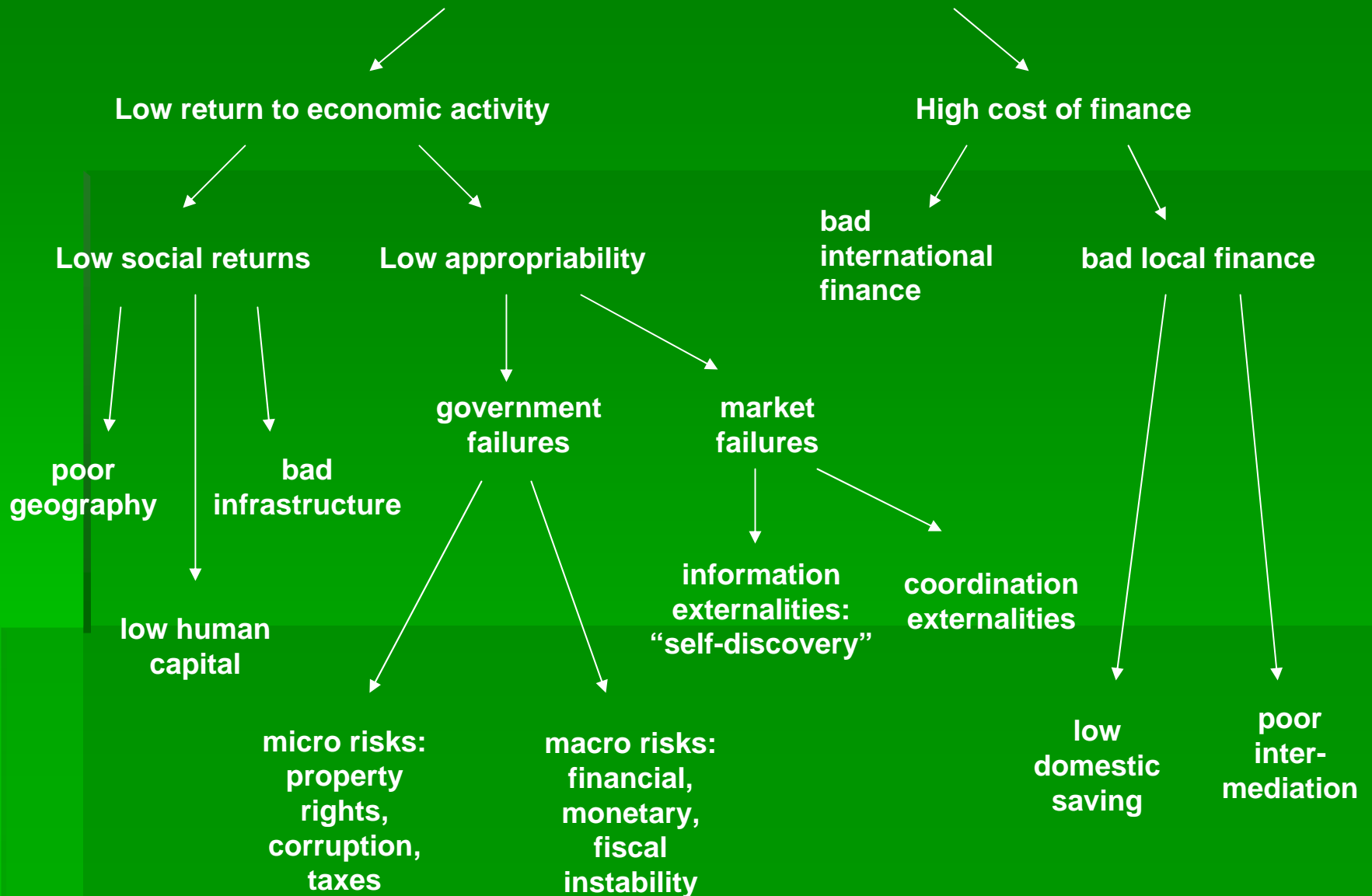
# I. Concept of Inclusive Growth



## II. Growth diagnostics

- What does growth diagnostics do?
  - Identify the most binding constraints and figure out policy priorities.
- How to identify the most binding constraints?
  - Identify proximate determinants of growth.
  - Figure out which of those post the greatest impediments to higher growth.
  - Identify the specific distortions behind the impediments.
- Using the following problem tree as a roadmap.

# Low levels of private investment and entrepreneurship



## II. Growth diagnostics

- Searching for price signals: Return to education, interest rates, cost of transport:
  - If low education is a serious problem, returns to skill/education should be high and unemployed skilled people should be low.
  - If investment is constrained by savings, interest rates should be high and growth respond to changes in available savings (e.g., inflow of foreign capital).
  - If poor transport links is a constraint, there should be bottlenecks and high private cost of transport.

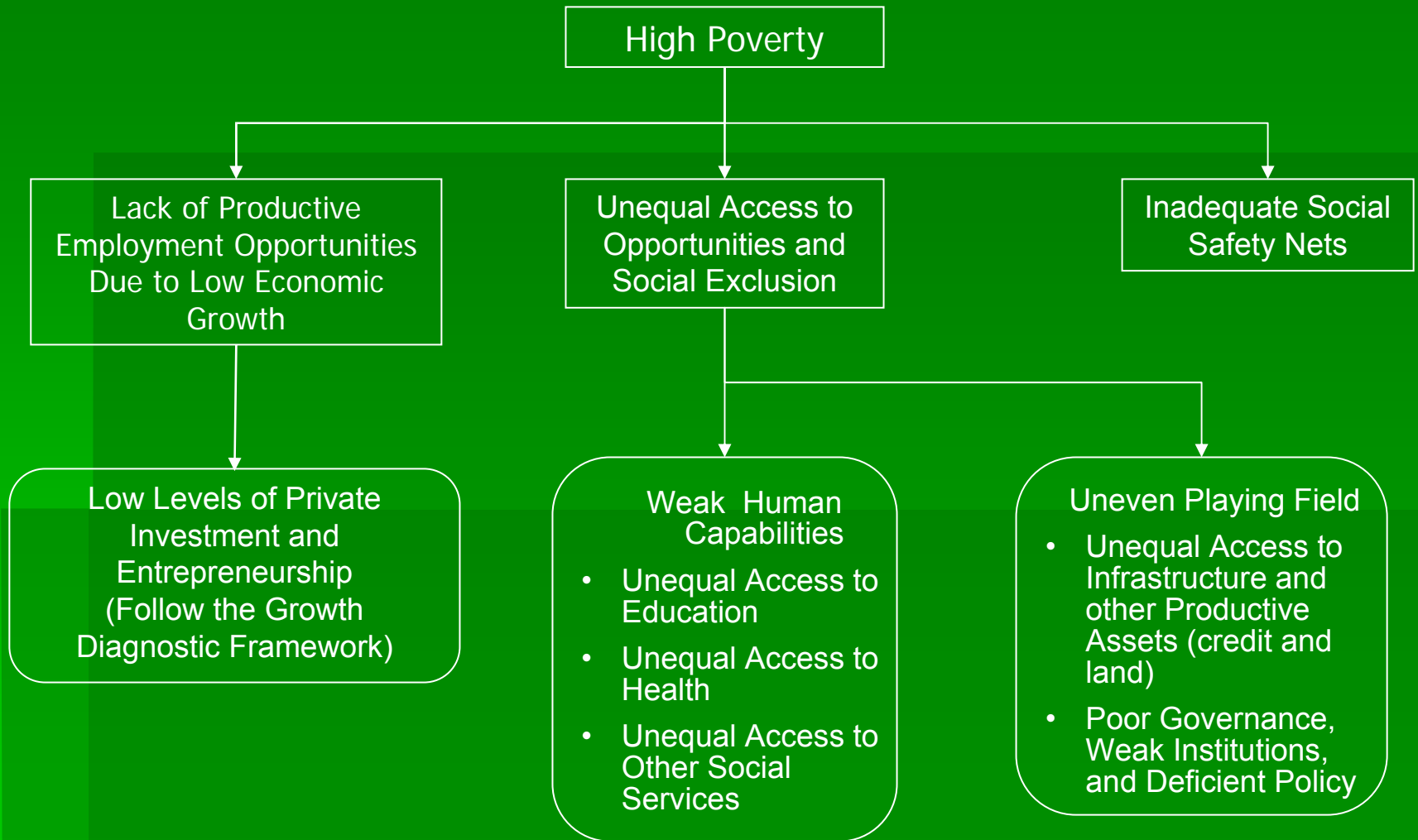
# II. Growth diagnostics

- Searching for non-price signals:
  - The camels and the hippopotamus.
  - When a constraint binds, it results in activities designed to get around it:
    - ❖ High tax → high informality.
    - ❖ Poor legal institutions → high demand for informal mechanisms of conflict resolution and contract enforcement.
    - ❖ Poor financial intermediation → internalization of finance through business groups, etc.

## II. Growth diagnostics

- Searching for historical growth episodes.
- Finding out what the business community says.
- Bench-marking with other countries and other periods.
- For fast-growing economies, focusing on constraints to sustaining growth and lagging regions.

# III. Diagnostic Framework for Inclusive Growth and Poverty Reduction



# Inclusion issues

1. Inclusive growth and poverty reduction
  - Are their objectives different or the same?
  - Can one analytical framework address both?

# Inclusion issues contd.

## 2. Integration in diagnostics of “informal barriers”

- Historical and structural exclusion
- Power, political and social relationships
- Informal incentives

# Proposed way forward on inclusion

- Separate sub-study on social exclusion
- And ensure exclusion perspective across the diagnostics study

Thank You