Hanley, N. and C.L. Spash (1993) *Cost-Benefit Analysis and the Environment,* Edward Elgar, Aldershot, Hants.

Environmental costs and benefits broadly considered raise the *main* evaluation problems in affluent countries, where the *re-pricing* that is the central subject-matter of the UNIDO and LMST studies is less important. But environmental costs and benefits of course have also to be valued in developing countries.

Online
Learning Center

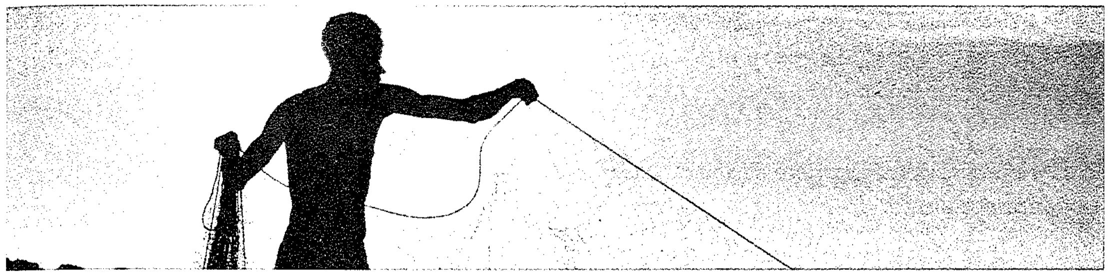
To help you grasp the key concepts of this chapter check out the extra resources posted on the Online Learning Centre at ***www.mcgraw-hill.co.uk/textbooks/huq***

Among other resources, there are four appendices available:

- Appendix 20.1 The equivalence 'in principle' of LM and UNIDO methods for appraising a car-production project
- Appendix 20.2 Determining distribution weights from a coherent welfare function
- Appendix 20.3 Fixing a shadow-wage for unskilled labour
- Appendix 20.4 Processes involved in an LMST appraisal – a hypothetical example

CHAPTER 21

Foreign Aid



Foreign aid – public and private – to developing countries has had some remarkable achievements to its credit, notably in disease control and the development of greatly improved crop strains. It has *probably* increased rates of economic growth. But it has not moved mountains as has sometimes been hoped. Is it that there was too little; or the wrong kinds; or bad administration; were the hopes misplaced; or was the whole structure wrongly conceived?

Introduction

The chapter starts by considering how inter-governmental aid compares in **scale** with other forms of capital inflow to developing countries; how the relative weight of aid among inflows has **changed**; why aid, namely official grants and concessional loans, nevertheless has its own special **importance**; and how aid is **distributed** across both donor and recipient countries, both absolutely and in relation to the size of their economies.

We then give **definitions** of terms and explain the various **distinctions of kind** in the aid business and some reasons for preferring one kind rather than another. We classify the **motives** behind official aid. We consider **expectations and aspirations** for the effects of aid when its motive is essentially humanitarian, and what might be (as against what have been) the implications for aid of taking seriously the *Millennium Development Goals.*

We consider the concept of **aid-absorptive capacity** and whether it is useful, and, if it is, why deficient absorptive capacity arises.

Then we consider the empirical **evidence for the impact of aid on economic growth** and next expound and examine **the recent debate on aid** between two prominent advocates, Jeffrey Sachs and William Easterly – one of them now a strong critic of the present aid scene – giving attention also to a third with a highly distinctive approach, Paul Collier; and from them we formulate ideas of how aid might serve its purpose better, some of which are foreshadowed in the section next following.

So finally we consider **new directions in aid**, both emerging and possible: first, potentially acceptable *sources of additional development finance* to match what appear to be urgent needs that are otherwise likely to remain unsatisfied; and second, new and prospective *arrangements for fruitfully channelling* additional or existing funds that are available internationally for development.

BOX 21.1 TOOLKIT FOR FOREIGN AID

Aid-absorptive capacity. How far a government or other recipient of aid can effectively use it (or how much it can effectively use).

Bilateral and multilateral aid. Bilateral (two-sided) aid is aid given by one government to another. **Multilateral** (many-sided) aid is aid given by an international institution representing a number of governments.

Concessional loans. Loans made on more favourable terms than those available in commercial markets.

DAC. Development Assistance Committee of the OECD (see below). This includes almost all the high-income member countries of the OECD who give substantial amounts of aid ('ODA' and 'OA': see below). It is essentially a source of public information and mutual consultation about foreign aid, but its members agree on certain targets in their aid, and the DAC as an institution monitors the attainment of those targets.

FDI. Foreign direct investment, which is private commercial investment in one country by an individual, company or other entity resident in another – by either starting a producing business or buying one (or shares in one) already in existence – provided the intention of the investor is to play an active role in management of the business.

FPI, PFI. Foreign portfolio investment, which is the purchase by a resident in one country of financial assets (taken to include company shares) issued in another, provided the purchaser of the shares does not intend to play an active role in the business whose shares they are.

Fungibility. In the context, this term refers to the capacity of resources given or appropriated for one purpose to be effectively used for another, for example when foreign aid received to finance a health project releases funds that would otherwise have been spent on the project so that the receiving government can spend more on weapons.

Grant element of a concessional loan is the proportion that the **grant equivalent** of the loan (see below) bears to its face value.

Grant equivalent of a concessional loan is the value of a free grant that would have the same net present value (NPV) to the recipient as the loan.

Multilateral aid. See '**Bilateral and multilateral aid**' above.

OA. Official Aid. For precise definition of the term is used by the DAC, see Appendix 21.2.

ODA. Official Development Assistance. As the terms are commonly used, this refers to **foreign aid.** For precise definition as the term is used by the DAC, see Appendix 21.2.

OECD. Organization for Economic Co-operation and Development. A Paris-based intergovernmental think-tank, source of information, and co-ordinator, formed by the governments of most of the high-income countries, and a few countries of upper-middle income.

Programme aid. See 'Project aid and programme aid' below.

Project aid and programme aid. Project aid is aid given exclusively to finance a particular project. **Programme aid** is aid whose use is less restricted, so that the recipient government has some discretion over the purposes for which it is spent. It may be either **sectoral aid** (which means that it may be spent at the discretion of the recipient but only within a specified sector such as education) or **general budget support** (which may be spent entirely at the discretion of the recipient).

Tied (source-tied) aid and untied aid. Source-tied aid (now normally called simply 'tied aid') must be spent on goods or services originating in the donor country. **Untied aid** is subject to no such restriction.

Aid in the context of capital inflows

Relative magnitudes of various flows

In the 1950s and 1960s official aid exceeded private capital flows to developing countries. This position has now long been reversed, at least *before* flows in the other direction (interest payments and profit remittances) are netted out, with the late 1960s the crossover period. Table 21.1 shows the magnitudes of official-aid flows and private commercial flows from those countries ('DAC countries') that are members of the Development Assistance Committee of the OECD (the Organization for Economic Co-operation and Development, a rich-country governments' think-tank). These DAC countries comprise nearly all of the *high-income* countries that give official aid, and between them give the overwhelming bulk of it. (Other donor countries *for which the DAC had evidence* – which *excluded* China and India – contributed about $5 billion a year around 2005, equal to about 5 per cent of the DAC total, with Saudi Arabia responsible for about a third of this. DAC statements in its 2006 Report suggest that the all-inclusive total could well have been substantially higher, probably $7 billion or more, and would be likely to grow faster than that from DAC countries.)

Clearly the private flows reported in Table 21.1 were well above official aid in both 2000 and 2005 and as far back as 1980. Both roughly doubled in nominal terms over the five-year period to 2005, but 2005 was regarded at the time as an exceptionally high year for aid because of extensive debt-forgiveness – and even so the proportional increase in the private flows over that period was slightly higher.

	Current prices						Constant 2000 prices					
	1960	1970	1980	1990	2000	2005	1960	1970	1980	1990	2000	2005
ODA (as % of donors'	4.67	6.81	26.78	54.08	53.75	106.78	31.11	32.17	44.51	57.61	53.75	84.43
GNP/GNI)	(0.52)	(0.34)	(0.37)	(0.35)	(0.22)	(0.33)						
Private	3.15	6.74	40.63	n.a.	80.78	178.64	20.99	31.84	67.53	..	80.78	141.25

TABLE 21.1 Official Development Assistance (ODA) and private capital flows from DAC members to developing countries, US$ billions in current and constant-2000 prices, 1960–2005

Note: Deflator as in Table 21.2 below, extended back beyond 1980 by a DAC deflator for GNI of DAC countries.

Source: OECD, *International Development Statistics Online*, at http://www.oecd.org/dac/stats, consulted May 2007; OECD, *Development Assistance Report*, various issues.

	1985	1990	1995	2000	2005
Current prices	61.8	95.7	227.4	228.1	443.4
Constant year-2000 prices	111.4	101.9	197.29	228.1	350.6

TABLE 21.2 Net resource flows to developing countries, 1985 to 2005, billion US dollars in current and constant-2000 prices

Notes: 1. Deflation is by an index compiled by the DAC for deflating dollar prices in international transfers from DAC donors

2. These figures do not deduct from the inflows interest paid abroad on long-term debt or profit remittances on inward foreign investment. They exclude short-term debt transactions, loans from the IMF, and technical-assistance grants. They also exclude migrant remittances and other private unrequited transfers.

Sources: World Bank, *Global Development Finance*, 2006, vol. ii, p. 2. OECD, Development Assistance Committee, *1998* and *2006 Reports* (for deflators).

	1985	1990	1995	2000	2005
Net inflow of long-term loans	59.1	44.8	33.5	7.2	20.7
FDI net	19.1	22.7	46.2	74.0	53.6
Portfolio equity flows	0.0	3.6	6.4	6.2	13.8
Grants	21.7	28.9	13.9	12.6	11.9

TABLE 21.3 Distribution of net resource flows into developing countries among forms of inflow, 1985 to 2005, % of the totals of Table 21.2

Note: See note 2 to Table 21.2 above.

Source: As in Table 21.2 above.

The DAC figures in Table 21.1 are not easy to reconcile in detail with those implied by Tables 21.2 and 21.3, where private flows (and total net resource flows) seem much higher, and aid (if we take it as 80–90 per cent comprising grants) much lower. Some, but not much, of the discrepancy is explained by the fact that Table 21.1 refers to flows from DAC members only. We can go some way to explaining the remaining discrepancy. In any case the broad private–official difference has the same sign throughout in Tables 21.2 and 21.3 as in Table 21.1.

However, the picture can be further elaborated by subtracting (2) interest paid out on long-term debt, and profit remittances on private investment, from (1) net inward 'resource flows', to give (3) *net inward 'transfers'*, as shown in Table 21.4. If these recurrent outward flows of interest and profit were to be deducted from the relevant parts of the data used in Table 21.3, which would overwhelmingly mean from the private-flow elements, official net inward transfers would exceed private at least as late as 1985.

Other features revealed by the tables are the large increase of direct investment in relation to loans from 1995, and the emergence of net portfolio equity investment: from nothing in 1985 to a substantial figure in more recent years.

The main element still missing for completing the picture is migrant remittances. There is great uncertainty about the magnitude of these flows, but we mention an estimate of $199 billion for 2006. Reasons are given in Chapter 24 why that is almost certainly a large

	1985	1990	1995	2000	2005
Net resource flows (1)	61.8	95.7	227.4	228.1	443.4
Outward interest & profit payments (2)	63.1	68.3	111.2	177.7	228.8
Net inward 'transfers'* (3) = (1) – (2)	–1.3	27.4	116.2	150.4	214.6

TABLE 21.4 Net transfers to developing countries, 1985 to 2005, US$ billion at current prices

Note: *The term 'transfers' as used here and by the DAC is both wider and narrower than in its standard use in balance-of-payments statistics, where it refers to all flows that are *'unrequited'* and no others. Unlike the 'transfers' presented here, it would *include* free grants from private sources and migrants' remittances (and also in principle technical-assistance grants, though they might be largely balanced by related outflows), but it would *exclude* movements representing investment and loans, or income therefrom.

Source: As in Table 21.2 above.

underestimate. As it stands, however, it would put remittances at nearly twice the DAC aid figures, even for 2005 and 2006, when aid was exceptionally high. See Table 24.6 in Chapter 24, which shows net ODA against net inward FDI and migrant remittances from 1995. According to that table remittances surpassed ODA from 1997. Other comparisons are given in Chapter 24, where the point is also made that remittances are *more reliable* than either official development aid or FDI.

The gist of the story is that aid has decreased in relative importance among financial inflows to developing countries fairly consistently since 1960, and especially in relation to direct investment, and almost certainly to migrant remittances.

Special function of 'aid'

Aid still has special functions, at least potentially. What will be treated here as 'aid' is Official Development Assistance (ODA) and Official Aid (OA) in DAC terminology (see definitions in Appendix 21.2). 'Official' indicates that it is given by governments directly or by international organizations ('multilaterals'). This means that it differs from the other flows we are considering – migrant remittances and all forms of commercial investment and lending – which are matters of private decision. So public policy enters directly into the aid-giving decisions. Any public aspirations to a less deprived, fairer, more equal world could admittedly be reflected also in changes in the *conditions*, the *rules*, under which commercial trade and investment and migrant transfers are carried on; and world public policy on these matters may arguably be *quite as important* as direct aid decisions; but, among the international financial flows, aid alone can ('in principle') be deliberately directed by public decisions to economic-growth and welfare objectives. In other words, governments and international bodies may use the aid lever directly for public-policy purposes, though in fact it is only to a very limited extent that they do so *by common arrangement.*

The idea of aid as filling several gaps

What was called **two-gap analysis**, explored in Chapter 5, implied that growth-generating investment was likely to require not only adequate proceeds of domestic saving but also foreign exchange, which might or might not be present in sufficient quantity for the savings to be converted into investment. Foreign aid in convertible currency, it was argued, would meet not only the 'savings gap' but also any foreign-exchange gap that might not otherwise be met by the equivalent savings. A further twist is that some crucial elements in economic growth – much physical and social infrastructure – require outlays by the state. Raising enough revenue to finance these outlays may face political obstacles. Almost all official aid passes not only *from* but *to* governments. By this reasoning that is an additional advantage, relieving a third limitation, the *fiscal constraint.*

Over time, two-gap analysis has come to feature less in thinking than it did in the earlier decades. This is in part because of greater trust in the possibilities of substitutability between resources through international trade. Emphasis on the fiscal constraint has also languished, possibly because there has come to be greater awareness of 'government failure' coupled with the belief that aid has often failed to deliver what has been expected of it by donors.

Distribution of aid by donor

Early in the post-war era the idea developed of an obligation among the rich countries to devote a proportion of their income to economic aid, something like a proportional tax. The aspiration originally set by the UN General Assembly was a uniform rate of 1 per cent of national income. France, with its large budget support to colonies and ex-colonies, was one of the few countries to reach that target in the 1960s. As the importance of private capital inflows grew, the target was relaxed by the General Assembly in 1970 to include these movements within the required 1 per cent, but still with a target, now of 0.7 per cent, for official aid. That 0.7 per cent has remained an aspiration, though, after France's performance dropped off from the late 1960s, only a few comparatively small countries – mainly the Netherlands, the Scandinavians, and Luxembourg – have fairly consistently met the target. In absolute amounts given, the US, with the world's third-highest population and one of its very highest incomes per head, has been the biggest individual donor in many, though not all, years; but, in spite of having started the aid fashion with its generous and extremely successful Marshall Plan, the US has dropped to a point at which, by the end of the century, it had long been at or near the bottom among the DAC countries in the proportion of its aid to national income.

Table 21.5 shows that the aid total rose considerably between 2000 and 2005: in real terms by about 58 per cent, and by about 32 per cent between 2004 and 2005 alone. The large debt-forgiveness of 2005 to poor countries, mainly consisting of big reliefs arranged through the Paris Club of rich creditor-governments with Iraq and Nigeria, amounted to $22.699 billion in current prices, which accounted for about half of that year's real increase in aid over 2000 (OECD, 2007, p. 132). Debt-forgiveness continued on a large scale in 2006.

The Sachs Report (UN, 2005) on strategy to achieve the Millennium Development Goals advocates increasing aid from high-income countries from around 0.25 per cent of donor national income in 2003 to around 0.44 per cent in 2006 (well ahead of what was actually to be attained in spite of the extra debt-forgiveness of that year) and 0.54 per cent by 2015. From ostensible future commitments made by DAC members in 2005, the DAC projected that ODA from the DAC would increase from $80 billion in 2004 to $130 billion (at 2004 prices) in 2010, and that aid to Africa would double over the same period. Staff of the Millennium Project, probably working from similar projections and in the same prices, calculated the difference between ODA needs and the lesser sums that had been projected by the donors at the time the report was compiled as $48 billion in 2006, $50 billion in 2010, and $74 billion in 2015.

	US$ billions at current prices			% of donors' GNI		
	2000	2005	2006*	2000	2005	2006*
DAC members total	53.749	106.777 (84.429)**	103.940	0.22	0.33	0.30
Australia	0.987	1.680		0.27	0.25	0.30
Austria	0.440	1.573		0.32	0.52	0.48
Belgium	0.820	1.963		0.36	0.53	0.50
Canada	1.744	3.756		0.25	0.34	0.30
Denmark	1.664	2.109		1.06	0.81	0.80
Finland	0.371	0.902		0.31	0.46	0.39
France	4.105	10.026		0.30	0.47	0.47
Germany	5.030	10.082		0.27	0.36	0.36
Greece	0.226	0.384		0.20	0.17	0.16
Ireland	0.234	0.719		0.29	0.42	0.53
Italy	1.376	5.091		0.13	0.29	0.20
Japan	13.508	13.147		0.28	0.28	0.25
Luxembourg	0.123	0.256		0.71	0.86	0.89
Netherlands	3.135	5.115		0.84	0.82	0.81
New Zealand	0.113	0.274		0.25	0.27	0.27
Norway	1.264	2.786		0.76	0.94	0.89
Portugal	0.271	0.377		0.26	0.21	0.21
Spain	1.195	3.018		0.22	0.37	0.32
Sweden	1.799	3.362		0.80	0.94	1.03
Switzerland	0.890	1.767		0.34	0.44	0.39
UK	4.501	10.767		0.32	0.47	0.52
USA	9.955	27.622		0.10	0.22	0.17

TABLE 21.5 Distribution of aid among DAC donors, 2000, 2005, and 2006: total ODA, net disbursements
Notes: * Provisional. ** Figure in brackets is in year-2000 prices.
Source: OECD, Development Assistance Committee, International Development Statistics Online; http://www.oecd.org/dac/stats, consulted June–August 2007.

Distribution of aid across recipients

Aid from the DAC members has gone to about 180 countries, which comprise almost all those of low and middle income. Their receipts *per head* have been notoriously unequal, with smaller countries having a strong tendency to get a higher rate. The poorer countries, moreover, have not necessarily done better on that measure than those less poor. DAC figures for 2004–5 (OECD, 2007) admittedly show that low- and low-middle-income countries received 96 per cent of the bilateral (direct government-to-government) aid; but the division between low-income (47 per cent) and low-middle-income (49 per cent) shows them as getting roughly the same amounts *per head*, when a decided balance in favour of the former (which have about three times as many people absolutely as the lower-middles *living at less than a dollar a day*) might have been expected. Of six world regions, sub-Saharan Africa received the biggest absolute share of bilateral aid at 32.5 per cent.

Figures for 2004–5 (OECD, 2007, pp. 15–17) are not typical, both because of the debt-forgiveness of 2005, heavily biased to Iraq and Nigeria, and also because of the special position at the time of Iraq and Afghanistan as theatres of war. In that two-year period, Iraq was by far the largest absolute recipient with about *an eighth* of the world total, though it has only about 0.4 per cent of developing-country population. Afghanistan took about 2 per cent. With the exception of Sudan and, surprisingly, Ghana, the rest of the ten largest recipients were all countries with large populations, but not all of the poorest: China and Egypt were included, while Bangladesh and Pakistan, decidedly poorer, were not. The world distribution of aid receipts, decided largely by donor governments working independently of each other, does not follow any clear principle of fairness or relative need. The source indicates that the identity of the ten largest recipients changes from year to year.

The Sachs Report for the Millennium Project (UN, 2005) advocated a selective approach, with heavy concentration of aid on those recipient countries geared by the character of their governance to make good use of the resources provided.

Definitions and forms of aid

For definitions of terms and abbreviations not explained here, see Appendix 21.2.

Military and civil assistance

The DAC includes among the defining features of ODA (Official Development Assistance) and OA (Official Aid) that they have 'economic development and welfare' as their main objective. Whether as a statement of motivation this is in fact the case *with all that passes for aid* is a matter for investigation, but the definition is agreed *to exclude flows for military purposes*. Military aid was important particularly in the Cold War and Apartheid period and has continued to be so in some more troubled areas where great powers' objectives are affected, but it is not included within the totals in this chapter.

Grants and concessional loans in aid: grant equivalent and grant element in loans

Concessional loans are loans made on more favourable financial terms than are available in the commercial market. Where loans are sufficiently concessional, they are treated as part of aid.

The *net present value (NPV)* of a loan, as calculated from its capital inflows and the offsetting outflows required to service it – all discounted for time at some standard rate – is called the *grant equivalent* of the loan. This means the amount of outright grant to which its value in straight financial terms is equivalent. The discount rate used by the DAC for this purpose is 10 per cent. (Near the start of Chapter 20 is a brief account of how the NPV of a series of cash flows is calculated.)

The ratio of a loan's grant equivalent to its face-value is called its *grant element*, usually expressed as a percentage. It will be higher the longer the *maturity* of the loan, the lower the *interest rate*, and the longer the *grace period* before repayment has to begin.

Where a loan has *a grant element of 25 per cent or more*, it is treated by the DAC as part of aid from the lender to the borrower. In the DAC's valuation of ODA, concessional loans that meet the 25-per-cent test are included *at full face-value*. An alternative measure, *effective development aid (EDA)*, proposed in a World Bank publication of 1998, includes – perhaps more reasonably – *all* a country's official loans to developing countries, but each *valued only at its grant equivalent*. (A further way in which EDA differs from ODA is that EDA excludes technical-assistance grants and debt-forgiveness. The reasons for this are probably that technical assistance outlays typically consist largely of consultant fees paid to nationals of the donor country; while debt-forgiveness often entails additional net cash-flows to the recipient that are less than what is technically the grant-equivalent of the debt forgiven.)

The debt problems of developing countries in the 1980s – and more particularly those in the 1990s, which were commonly over loans from governments and multilaterals – have widely been taken as favouring the giving of aid in the form of grants rather than loans, and the recent trend has been in that direction. About half the donor countries over 2004–5 had grant-only aid programmes, with most remaining loans designed for infrastructure projects. Of the exceptions among donors, the most striking was Japan, with about 40–50 per cent of its aid in loan form. For the DAC in total over 2004–5, only 11 per cent of ODA consisted of loans, and these loans had a grant element on weighted average of about 70 per cent (OECD, 2007, p. 183).

Bilateral and multilateral aid

An element in the early aspirations for development aid was that it should be a world project administered impartially. This led to the hope that most of it might be 'multilateral' (many-sided), that is coming through international institutions, such as the World Bank and the UN Agencies. This is not what has happened. Most aid is 'bilateral': from one country's government to another's. Multilateral aid has never been more than a minor fraction of the total. Aid from multilaterals is included within the DAC's totals of ODA. The multilaterals (with respect to their grants and concessional loans) are largely, but not entirely, financed by DAC members.

If aid from the European Commission (EC), acting for the European Union, is included as multilateral, then multilateral concessional flows in 2005 are given as $26.7 billion, which is equal to 25 per cent of the total of DAC aid in 2005 (OECD, 2007, p. 175). DAC members' contributions to multilaterals was only a little lower than that total at $24.6 billion (ibid., p. 171).

Project and programme aid

Here the question is how far the use of the aid is determined by the donor government. *Programme aid* includes *general budget support*, which leaves the recipient government completely free over its use; and also *sectoral aid*, where the donor specifies the sector (such as education or transport) but leaves the recipient to decide on the use of the aid *within that category*. The term *'project aid'* is sometimes applied to all non-programme aid, but this would mean including humanitarian outlays made in emergencies. Better perhaps to use the term *'non-programme aid'*. There is a dilemma for donors over how restrictive they should be. Being over-prescriptive risks overriding responsibly determined recipient priorities and failing to use local knowledge and to respond to local perceptions of need. There is a particular risk of overlooking political factors, such as potential sources of conflict, that may have a large impact on how useful the aid can be. On the other hand, a hands-off policy, under which the aid could not be attached by agreement with the donor to any pre-agreed object and its use could not be monitored, might leave the donor without much assurance that the aid had been used well or even with integrity. However, for donor governments that wish to impose certain priorities (for example, to prevent their aid from being used for increasing armaments), there is the problem of what is called *fungibility* of earmarked funds: it can be hard to prevent aid earmarked for, say, health spending from being used to release resources *that would otherwise have been devoted to health* to be spent instead on, say, additional military aircraft, so that the effect of the aid is to increase military rather than health spending.

Latterly, the international community (encouraged by the UN in its Millennium Project) has been inclined to treat a certain number of developing countries, including several of the poorest in sub-Saharan Africa, as reliable in setting priorities and consistently translating them into spending commitments, and consequently to support those countries' own programmes and to direct funds differentially to them. Other recipients may be required to propose projects that can be evaluated in advance by the donor and specifically monitored as they proceed. The World Bank was designed to be a project-lender, but its Structural-Adjustment Loans, instituted in 1979, though tied to reforms, constitute programme aid, with the actual use of the funds fairly open.

The proportion of ODA in 2005 given as programme aid was 47 per cent, roughly half of this as general budget support and half as sectoral aid (OECD, 2007).

Source-tied and source-untied aid

Aid that is given by the donor *in kind*, or for which some or all of the purchases must be made from the donor country, is described as *source-tied* or simply *tied*. Most 'technical assistance' is tied aid in that the advisors (whose employment accounts for most of the cost of technical assistance) are almost always from the donor country.

Arguments used by donors in the past for source-tying are that their countries can afford more aid if it is given that way; or (for domestic consumption) that they can promote their own countries' products and tie the recipients into further purchases for maintenance and replacements. For the recipients, tying means that they can not obtain the goods or services to be financed by the aid from the cheapest supplier. This may substantially reduce the value of the aid, all the more so if it effectively binds them to future purchases from the same source. If the tied aid is given by way of a not-very-concessional loan, the deal may even be, in a straight financial sense, of negative value to the recipient country. In other words, the country might do better getting the inputs more cheaply and borrowing the cost in the market.

Source-tying by DAC countries is almost certainly less prevalent than it once was. Of the DAC aid *for which tying status had been reported*, the proportion *untied* in 2005 was given as 91.8 per cent (OECD, 2007, p. 184). However several important countries, covering nearly 25 per cent of the aid, had not reported on the subject, which leads to the suspicion that the true figure untied was in fact substantially lower. Aid from the UK and Ireland was 100 per cent untied, and that from Germany, France, and Sweden each well over 90 per cent. According to Easterly (2006, p. 192; citing OECD, 2001), the US, whose rate is not reported in the figures just quoted, *ties* about 75 per cent of its aid.

Motives of aid

Unless a country is a complete autocracy or oligarchy, what is meant by the motives of its aid has to include the motives not only of the politicians and officials who directly make the aid decisions but also the motives of all those who advocate it, lobby for it, or tacitly expect it. It would be very surprising if there were one single motive. The individual politicians and officials themselves, and public advocates of aid, may themselves each have a mixture of motives. As a rough guide to thinking about the matter while avoiding the worst over-simplifications, we could divide the motives four ways.

Humanitarian

There is a concern, however vague, to mitigate at least the worst extremes of poverty across the world; a sense of a shared responsibility for pursuit of that objective and a desire to have some part in it. Without some such concern among a significant proportion of donor populations, aid would surely be much lower than it is. The pro-aid campaigning groups are almost entirely humanitarian in their arguments. Even in the US, the rich country with the most vocal opposition to foreign aid, a survey of public attitudes showed a surprising level of support for it, coupled with a huge *overestimate* of the amount actually given, with a median choice of 5 per cent as the proportion it *should* bear to government spending (about eight times as high as the actual amount!) (Kull and Destler, 1999). The Landau Report (France, 2004b, p. 61) cites surveys as showing that 92, 79, 78, 74, and 74 per cent, of the public in respectively Germany, the US, the UK, France and Japan backed development aid in principle, and other surveys as finding that *increasing* aid was supported by 96 per cent in France, and 83, 81, 72, and 68 per cent, respectively in Germany, the US, the UK, and Japan. It would seem likely that the *public* support for aid in general, however ill-informed and removed from consideration of the opportunity costs some of it may be, is based largely on humanitarian grounds.

Political – general

Arguments are sometimes put for increasing aid on the grounds that a world with less poverty and faster economic growth is likely to be a more peaceful world. This may be at the backs of the minds of some decision-makers and campaigners, but the very long term over which any country's donations, unless highly concentrated in particular trouble-spots, can be expected – at best – to make a significant difference to the prevalence of unrest probably prevents this motive from carrying much weight. The rather small proportions of their resources that most donor countries now give indeed suggest that their politicians do not take this consideration very seriously. It may on the other hand have bulked quite large in the motivation of the very liberal US aid given to Western Europe (and offered to Eastern Europe) under the Marshall Plan in the late 1940s, when unrest and disaffection were expected to favour Soviet-aligned Communist parties.

Political – particular

Yet, undoubtedly much aid has been targeted on particular countries with the idea of supporting their regimes or recruiting their support. This has been recognized in Japan's apparent inducements to small countries, often without any whaling interests of their own, to become members of the International Whaling Commission, where they can support Japan's position. Taiwan's aid has often been linked, explicitly or implicitly, to recognition of its legitimacy. The fact that Israel and (after 1977) Egypt have for so much of the time been around the top of the lists of US aid recipients reflects strong attachment within the US to maintaining the position of Israel and seeking allies in the 'Middle East'. France has used military and civil aid to retain the attachment of independent states from its former African empire. In the Cold War both sides plainly used aid to keep specific developing-country governments onside or at least neutral.

Commercial

Commercial objectives are not always explicit, and they seem to play a larger part in the motivation of some countries' aid than in that of others. Japan has been regarded as more commercially motivated than most in the direction of its aid, favouring destinations likely to be important markets for its goods or sites of its direct investment. However, only 10.4 per cent of its aid was reported as wholly or partly tied in 2005 (OECD, 2007, p. 184). It is probable that any commercial objectives sought through Japan's aid are pursued largely through maintaining good relations rather than by using the aid for what is in effect marketing. China similarly in most recent years has apparently used aid to facilitate secure supplies of energy and minerals, as in Sudan and elsewhere in Africa, but its more important instrument for that purpose is probably political support (Sudan again). There is competition among arms-exporting countries over purchase terms on supply contracts for weapons, but any loan concessions given for these purposes are excluded by definition from ODA.

Expectations and aspirations of humanitarian aid

Insofar as humanitarian motives rule, aid may reasonably be hoped or expected to do one or both of two things: to **contribute funds** for promoting economic growth and poverty reduction; and to **influence policy** in directions favourable to these same two objectives or others of a humanitarian nature. Aid is only one of the ways in which rich countries may enhance the resources available to poorer countries for growth and poverty reduction. Their own *foreign-trade policies* too are highly relevant. Aid is also only one of the ways in which they can influence developing countries' own policies toward effective pursuit of these ends. Appropriate trade agreements, in which each side agrees to be more open, *can be* a win-win game, as can agreements on tax co-operation (see the last part of Chapter 19).

Millennium Development Goals

The eight Millennium Development Goals (MDGs), adopted by the UN General Assembly in the year 2000 for fulfilment by 2015, are set as world objectives. The Goals, with their 'Targets' and 'Indicators' are listed in Appendix 21.1 at the end of this chapter. Most of the Goals are fairly concrete and specific, all (except arguably the last) concerned with present material welfare rather than economic-growth rates, and each (except the last) having as sub-heads at least one quantified 'Target' out of 18 Targets more detailed than the Goals, and each with a varying number of Indicators, summing to 48 in all, mostly quantitative, to measure how far the Goals are being achieved. Several of the quantified targets are expressed as proportional changes in specific welfare variables between 1990 and 2015

(see the table in Appendix 21.1). This indicates how far the various regions of the world had already gone from the base year of 1990 toward achieving the MDGs by around the year 2000, when the Goals were adopted by the UN, and how the rate of improvement might or might not need to be increased if each Goal was to be reached by 2015.

Though the proportional changes are expressed as changes in world totals, they have generally been taken (for example, by the UN Millennium Project) as to be applied also to each country individually. Attention has been given to the information necessary for each country (the 48 'Indicators') and the organization needed in each, with a proposal that each should mobilize, for pursuit of the goals, *increased domestic resources 'by up to four per cent of GNP* by 2015'. They are also enjoined to calculate the need for ODA (UN, 2005, '10 key recommendations', p. 1).

Promulgation of the goals shifts the emphasis in 'development' and 'aid for development' decisively from increasing growth rates (however necessary that may be as a means) to concrete reduction in poverty and general deprivation, notably in health, education, nutrition, access to water and sanitation, and gender equality, as well as in the cutting of straight income-poverty (in its most extreme expression: life on less than a dollar a day). Many of the direct poverty-reducing measures may themselves serve to increase growth rates, but the effect will often be long delayed, and there may be other spending projects, as on transport, that could be expected to increase growth rates more immediately for a given volume of resources employed. So, for the developing-country governments, and civil-society bodies prodding them, and consequently also for foreign governments and NGOs providing assistance, there will be *trade-offs over time* among different ways of promoting the desired benefits for the poorest, as well as *trade-offs between income classes*. The choice is perhaps eased if the results found by Clemens, Radelet, and Bhavnani (2004), mentioned below, are supported by subsequent research.

Baulch (2006) explores the extent to which the MDGs have influenced the character of aid funds. He finds that World Bank and UK aid goes predominantly to low-income countries, and US and European Commission aid predominantly to middle-income countries. Specifically on the extent to which aid is concentrated on populations most deficient in four of the MDG indicators (one-dollar-a-day poverty, young-child malnutrition, under-5 mortality, and non-attendance at primary school), he finds that among the nine major donors the World Bank and the UK tend to concentrate on countries that are worst on these indicators, as to a less extent do the Netherlands and the UN, while the US and the European Commission concentrate on those already best, followed in this by Japan, Germany, and France. However, all donors, including the World Bank and the UK, contribute much less to the very populous and deprived countries than those countries' shares of global poverty, child malnutrition, and under-5 mortality suggest is needed (ibid., p. 944). Altogether this does not suggest any strong influence of the MDGs on the setting of priorities. If there had been, we should expect a consistent bias among donors towards those lowest on the Millennium targets, and contributions to countries in rough relationship to their shares in the world's extreme poverty.

Aid-absorptive capacity

A country's absorptive capacity for aid means **the maximum amount that it can effectively use.** The idea of absorptive capacity, if it is valid, can serve as a guide to allocation of aid among potential recipients. But is it valid? Can there be simply too much aid, or at least more than enough? Doubts may well arise over whether an absorption limit can usefully be estimated *on aggregate aid to a whole country* rather than to particular sectors and kinds of project. A country's administration may be able to deal with no more major road-building projects but plenty of additional health-service workers. However, if further spending of particular kinds or in particular sectors can not adequately be managed, even though the objects to which it might be allocated may undoubtedly be important needs, it seems fair perhaps to refer to limits of absorptive capacity *in those areas.*

There are four linked or overlapping possibilities for explaining limits where they exist: dysfunctional formal institutions; unsuitable informal institutions (habits and expectations); lack of expertise; or failures in integrity. The question then arises whether further aid or consultation in some form could be provided to generate changes that might **relax the limits** – through, say, advising on improvement of the formal administrative institutions; through formal and motivational training courses; and through use of the influence that comes with aid to discourage corruption and encourage performance. There may be possibilities of concentrating aid in the sectors that work best and by-passing faulty arms of local administration. Judgements of the capacity of recipients to deal with certain amounts and forms of aid may be inevitable, but, where additional resources are ostensibly seriously needed, attempts might be made jointly among the donor community to help *expand the capacity*. This might be one of the ways in which more co-operation among donors could add value.

The experience of one of the present authors, mainly in the Pacific Islands, however, confirms that absorptive capacity can indeed be a problem for the donors and points to some of the apparent anomalies and dilemmas in aid relationships, and the expedients adopted to resolve them. Many donors active in the Pacific try to standardize projects across countries in order to simplify project management. The European Commission sets 'themes', narrowly defined, to which the local representatives are meant to adhere (even when projects may not be entirely suitable). The Asian Development Bank works in much the same way. There is some sense in this in that it gives the representatives some applicable expertise, but it may mean that projects on offer are not tailored to the recipient's circumstances or expressed choices. There is also tacit agreement across most donors that each of them will have its own country or sector 'specialisms', one of the reforms proposed by Easterly as mentioned later in this chapter. Recipients then know to which donor they should go first over say health projects. This is in order to minimize competition or duplication between donors. Another phenomenon encountered in some African countries and in the Pacific is that an aid representative of a donor country will often end up acting as a covert ally of the host country and trying to outmanoeuvre the donor organization back home. (This may be one reason why three years is usually the maximum length of stay for a representative.)

A possible source of waste and friction is the widespread practice of allocating local donor offices specific amounts to spend, often obliging them to unload the funds on what they know to be non-viable projects. At least until the mid-1990s the World Bank was quite willing to go along what was often an obvious fiction that loans for a project could be serviced and repaid from the increased tax revenue resulting from the growth in GNI that would be brought about by the project. Where part of the justification for the project was in the form of non-financial benefits, the problem raised by this pretence could be especially serious. Much the same was true regarding running costs; donors were often fully aware that the recipient country had no capacity for (and sometimes no intention of) *maintaining or using* a proposed new asset, such as a highway or hospital, adequately – but gave the funds

to construct it anyway. It seems that motivations on the ground, generated by the institutions for the giving and receiving of aid, may work against the aid's efficient allocation and effective use.

Empirical evidence on the bearing of aid on economic growth

Here there is a profusion of empirical studies, with apparently conflicting results, reaching back over at least four decades. Their results are usefully summarized by Mark McGillivray, Simon Feeny, Niels Hermes, and Robert Lensink (2006), who manage to organize them, and, without resolving the contradictions, draw from the studies one seemingly important conclusion. McGillivray *et al.* divide the studies into those up to the year 1996, and those after it. The watershed is the publication of the papers that fed into the World Bank report, *Assessing Aid* (World Bank, 1998).

The studies they summarize *before* the watershed are all concerned directly with whether aid does or does not appear to favour growth, or with closely related questions such as whether aid, or the presence of foreign-capital inflows generally, has a negative impact on domestic savings.

Of four studies *concerned with effects on domestic savings*, three find a negative impact, and one, no impact. (If there were indeed a negative impact on domestic savings, this would not be *conclusive* evidence that there could be no positive impact on growth. Total resources for investment might still be higher than if there had been no aid or inward capital flows. Some of the public-sector 'consumption' expenditures that might have increased as a result of the aid – as on education and health – could have had favourable long-term effects on growth. On the other hand, a finding of a *positive* impact or none on domestic savings would *enhance* the case for a positive impact on growth.) Of those seven studies from this period *concerned directly with effects on growth*, three find a positive impact, and four, no impact. So far, there is little conclusive one way or the other.

The change from 1997 is that the impact question was in most cases posed differently: *on what does any favourable effect of aid on growth depend?* This followed the approach of Burnside and Dollar (1997), on which, with related studies, *Assessing Aid* drew. These studies tested whether the positive impact of aid depended on a particular compound policy-variable; and they found that it did. The policy variable was designed to reflect the fiscal surplus, the inflation rate, and trade openness. In the estimation, explanatory variables included both (a) aid and (b) the product of aid and this policy index. Most subsequent studies on the question adopted a broadly comparable approach. McGillivray *et al.* list a further 17 whose answers can be readily compared, and review others. Of the 18, all have as explanatory variables *aid (per head)*, together with one or more of: a *squared* aid term (to test the hypothesis of diminishing returns to aid); a term that is *a product of aid and a policy variable* (not necessarily similar to that used by Burnside and Dollar); and a term that is *a product of aid and some other variable*. Three of the 18, all three involving as researchers either or both of David Dollar and Paul Collier, found that the effectiveness of aid depended on the policy environment. Nine concluded that it did not. Other variables on which aid-effectiveness was found to depend included political stability (two studies); institutional quality; democracy; climate (aid more effective the *worse* the climate); and whether or not the country was in the tropics (aid *less effective* in that case). (A study outwith the 18 found aid less effective the more *volatile* it was.) Seven found diminishing returns to aid; one, by contrast, that it was effective only *above* a certain threshold; and, beside this last, four of those that used the squared term to test for diminishing returns did not find evidence of any. However, of the 18, only one found that 'aid is not effective in stimulating growth'. The implication of all the others' findings was taken by McGillivray *et al.* – on the supposition that the possibility of reverse causation had been excluded – to be that aid *would* be effective in stimulating growth, at least in certain circumstances.

The lack of consensus about what those circumstances are leaves a big gap in our understanding of what is needed to make aid 'work'; but the studies strongly suggest that it is worthwhile persevering with aid, even if *only* for the sake of growth. The conclusion from seven of them that aid's effectiveness depends on policy or institutions *in some form* is after all plausible.

As McGillivray *et al.* conclude:

> One controversy has, it seems, been settled: one way or another, aid does appear to work. By that, it is meant that growth would be lower in the absence of aid. One can reasonably infer from this finding that poverty would be higher in the absence of aid.

Consideration of *the mechanism by which aid may become 'effective'* leads to the obvious possibility that different forms of aid will have different effects, that some forms will be more effective than others, and that the period over which the effect is measured will have a bearing on which forms register as effective and how much so. Clemens *et al.* (2004) follow up the hunch that the growth impact of aid will vary with the kind of aid and the period over which the effect is assessed. They divide aid into three types: (a) humanitarian and emergency aid, which they expect to be negatively correlated with growth since it comes when and where things are going wrong; (b) aid that is likely to affect growth only over a long period, such as for health and education; and (c) aid 'that plausibly could stimulate growth in four years'. In this last category, which they say comprises 53 per cent of all aid, they include support for investments in infrastructure; budget and balance-of-payments support; and aid for productive sectors such as industry and agriculture. They examine the impact of *this third class* within a period of four years after it is received; and they find a positive causal relationship between this aid and *growth within the four-year period after it is received*. The estimated impact of this form of aid on growth is two or three times as large as the effect estimated from studies that use *aggregate* growth for the explained variable. This perhaps suggests that quite potent effects on growth can occur simply from the release of spendable funds and its multiplier effects, with any foreign-exchange constraint relaxed by the fact that the aid comes in foreign-exchange form. (So perhaps, we may speculate, it is the fact of extra spending rather than the object of the spending that is mainly responsible for the extra growth within the four-year period.) The growth result does not depend 'crucially' on the recipient country's level of income or quality of institutions and policies. The result itself, however, was questioned by further testing of the same data (Rajan and Subramaniam, 2005).

The Olympian debate on aid: Easterly vs Sachs

Jefferey Sachs's *The End of Poverty: how we can make it happen in our lifetime* (2005) and William Easterly's *The White Man's Burden: why the West's efforts to aid the Rest have done so much ill and so little good* (2006) are rightly treated as two sides of a debate, though it is wrong to see the sides as for and against aid. Yet Easterly comes out strongly against the approach embodied in Sachs's book, in the Millennium Development Goals with whose implementation Sachs has been charged, and in the publications of the Millennium Project under his direction. Both books are extremely readable, passionate, and reasoned. Both authors write from extensive experience of developing countries.

First: **some elements in the rhetoric tending to exaggerate the disagreement**, and **some lines of agreement**, between them. When Easterly talks of 'aid', he is not referring only to financial aid but to the whole complex of ostensibly benevolent *intervention* by 'the West' in the rest of the world: policy advice, policy conditions for aid and co-operation, past colonization and imperialism, modern regime change. Set aside the fact that it may be loading the dice against to include nineteenth-century European policies in India or exploitation of Java and the Congo as 'aid'; the point here is that he is by no means against financial aid and there is nothing to indicate that he is keen to reduce it. He is rather concerned for its better use, as he sees it, with more realistic goals: 'I and other like-minded people keep trying, not to abandon aid to the poor but to make sure it reaches them' (2006, p. 5).

Sachs for his part is not arguing for aid *indiscriminately*, rather for its importance at a number of crucial points in recent history, when it was or was not provided, and for a number of crucial purposes now – purposes which between them require much more aid than is currently forthcoming, though amounts that are nonetheless easily manageable by the developed countries. Both are highly critical of some of the policies, past or current, of the World Bank and IMF and consequently of the governments of the large developed countries that ultimately control those institutions. Both believe in the value of markets and are certainly no enemies of globalization, but they recognize the critical need for enforced and internalized rules to control the abuses to which unrestrained private enterprise is prone, and institutions to compensate for the adverse fall-out from globalization. Both have a considerable measure of faith in the capacity of ordinary people to take advantage of opportunities for material betterment under certain conditions, though Sachs places greater hope in the possibility that benevolent and informed outsiders can and will help to create these conditions. The two agree that there is no single Big Idea, no key that will unlock the door to 'development'. Both are concerned principally to relieve human misery and powerlessness: to reduce poverty.

What Sachs attempts is evident from the audacious title of his book. 'We can end poverty by 2025 . . . and change the world forever', says its back cover. Like the UN Millennium Project, which he directs, it starts with the premise that certain objectives *must* be achieved, and proceeds to say in broad terms what actions could make this possible: how much extra finance, what international co-ordination, what deployment of expertise, what local co-operation. There are plenty of tried-and-tested technical devices – against the mass-killer and mass-debilitating diseases, for child nutrition, for family planning, for mini-power-generation, for getting investment finance to be used by the very poor – none of them vastly expensive in relation to their pay-offs, and well within the combined capacity of local effort and foreign donors to pay.

Much of the early part of the book draws on Sachs's previous experience as an adviser and seems intended to show that the *giving or withholding* of what seemed at the time to be large sums (in debt-forgiveness, stabilization backstops, and other forms) at critical points has made enormous differences: *giving for better, or withholding for worse*. The latter part counters arguments for despair; puts flesh onto the idea of breaking local vicious circles of poverty; gives ten examples of achievements on a world scale (seven of the ten concerned with health or reproduction); and takes us to various localities in the developing world to show how, with an open mind about the specific needs of particular times and places – the diagnostic approach – big improvements can be made on the ground.

The clear hope, explicit in the account of the Sauri project, mentioned below, is that this kind of experience can, with enough support, be replicated so as virtually to end extreme poverty and economic decline worldwide and to release every country for continuing material improvement. He does appear to see extreme poverty as involving people in a vicious circle which has to be, and can be, broken *with the help* of outside action, and he treats economic growth as a matter of stages through which now-very-poor countries can be expected to pass: Bangladesh at present, for example, with its big, though extremely low-paid industrial workforce, a step ahead of much of Africa.

Easterly counters with what is really a different view, not just of financial aid but of development and indeed of how the world works. Briefly, it's no good starting with the idea that some end *must* be met, regardless of experience of what is possible, and then letting the Planners work out how to do it. Reducing poverty is the work of 'Searchers', who tease out better ways of solving immediate problems, rather than of 'Planners'.

> I was among the many who have tried to find the answer to the question of what the end of poverty requires of foreign aid. I realized only belatedly that I was asking the question backward: I was captive to a planning mentality. Searchers ask the question the right way around: What can foreign aid do for poor people?'. . . . Aid agencies cannot end world poverty, but they can do many useful things to meet the desperate needs of the poor and give them new opportunities. For example, instead of trying to 'develop' Ethiopia, aid agencies could devise a program to give parents cash subsidies to keep their children in school. . . .
>
> *(Easterly, 2006, p. 11)*

Improvement involves varied and piecemeal processes – building on existing expectations, social relations, and habits of mind – that emerge over time to enable markets to work, and governments to work, for the general good. People from outside, unaware of the way existing systems, however imperfectly, operate, and trying to impose models from the West, may easily damage what there is without achieving what they intend. 'Planners' can not create markets; nor can they create democracy and the rule of law. So Planners cannot use quantities of cash to generate sustained, fast economic growth. What can be done with aid is help meet a variety of desperate human needs. Aid ought to be used to serve the world's poor, they are its customers; but aid administered, as it mainly is, by 'Planners' lacks feedback from, and accountability to, those customers. That is why, very little, so Easterly claims, seems to have been accomplished with the help of financial aid over 50 years, despite a series of past targets (as for universal access to water or primary schooling) similar to the Millennium Development Goals. Easterly is against the whole approach of fixing visionary (in his view utopian) targets and then working out centrally what they entail.

Quite apart from the fact that we don't know how to generate 'development' (by which he means economic growth), there is, Easterly argues, a serious obstacle in the way aid is currently organized even to meeting much more specific needs. This is typified in the way the implementation of the Millennium Project is envisaged, with the UN Secretary-General 'coordinating the actions of officials in six UN agencies, the UN country teams, the World Bank, the International Monetary Fund, and a couple of dozen rich-country aid agencies . . .' (2006, p. 6), for the adoption by myriad bodies across the world of 449 named kinds of intervention. This must lack the accountability – of specific people for specific results – that is necessary to ensure that anything happens. 'Collective responsibility for Millennium Development Goals or any other goals does not work' (2006, p. 205).

On the other hand,

> Searchers could find ways to make a specific task – such as getting medicines to dying children – work if they could concentrate on that task instead of on Big Plans.
>
> *(2006, p. 7)*

How can these two rational and informed writers with such largely shared values differ so radically? **Three underlying differences of basic approach** – closely linked – stand out: about *realistic public targets*, about *scale* in action for improvement, and about *the right location for initiative*.

First, Easterly does not accept that *speeding economic growth* is a reasonable policy objective, let alone one in which targets can realistically be set. Foreign aid can help meet some concrete, 'desperate needs' of great human importance. We simply don't know how it could be used to bring about rapid growth. We know a certain amount about what the requirements for sustained growth are. What we don't know is how 'Planners' can generate those requirements. (Certainly, we might agree, where fast and long-continued growth has occurred, as in much of East and South-East Asia, and more recently in India, this to all appearances has had little or nothing to do with any international plan or donation directed at bringing it about. Much has often been made of the fact that South Korea and Taiwan received substantial US aid in the 1950s and 1960s. This was used to disparage their achievement. But all that is long-past history. Their rapid growth is not. The Korean and Taiwanese industrial revolutions were no more deliberately concocted by outside benevolence than those of Japan and China.) By implication Easterly also seems to be rejecting the need for world co-ordination and scale even in certain specific welfare programmes – although he admits successes for aid in some of the major health achievements called in evidence by Sachs that depended heavily on international projects. His apparent aspiration that all aid should go through an 'open market' for the sponsoring of projects – submitted individually for help by their immediate beneficiaries – seems to rule out the co-ordinated application locally of a number of different inputs as in Sachs's example of the Sauri villages in Kenya (see Box 21.1), let alone the big world efforts against smallpox, polio, and malaria.

Sachs, by contrast, seems to believe that economic growth is a natural state. If it is not occurring, we should look for *obstacles* of various types that may be blocking it. No less than Easterly, he disavows a belief in any single expedient for bringing growth about. Instead, he proposes a clinical diagnostic approach: look and test for *which of the various possible factors may have gone wrong*. He also seems to believe, or hope, that using foreign help in dealing comprehensively and sustainably with the diverse material-welfare needs of individual poverty-stricken rural communities, each for a limited period, opens possibilities of aggregating up to produce comparable economic growth for the whole rural economy. This seems to follow from the implications he draws from experience with the Sauri area (2005, pp. 226 ff.). There need be no conflict: in a virtuous circle, economic growth, *bringing poverty reduction in its wake*, can and will also *follow from* appropriate forms of poverty reduction.

The **second** major difference, not unrelated, refers to the potential of aggregate planning, with aggregate targets, worked out in New York or Washington or national capitals, and more broadly with *the advantages of co-ordination and scale*. Easterly, as we have seen, opposes 'Planners' to 'Searchers'. The Searchers are people working on the ground and finding better ways of doing things. He cites a number of examples of successful Searchers. One, for example, is Mohammed Yunus, who found a way of making micro-lending viable (as outlined in our Chapter 19 under 'Lending to the very poor: microcredit'). No planner can make such new ideas, generated as they are from hands-on experience, happen by propounding a target.

Sachs, on the other hand, believes that many targets such as those in the MDGs *can* be achieved if enough resources are devoted to them, and that having a global plan, with the goals propounded and universally agreed, gives a handle for screwing out the resources. His examples of how world-scale projects, such as the elimination of smallpox, or the near-elimination of polio, or what at one time seemed a close approach to the elimination of malaria from much of its range, can take place with a technical lead from the World Health Organization (WHO, a UN agency), and with funding from multilaterals or private foundations, throw doubt on some of Easterly's assertions of impossibility. Co-ordinating projects on a national or regional or world scale is sometimes necessary. It may also be possible. Often there is no need to wait around for Searchers. The techniques are known. Granted that implementation may require respectful co-operation with local partners – state or non-state – to take account of local attitudes and circumstances, achievements – with smallpox, polio, river-blindness, family-planning, child mortality, green-revolution foodgrains – are nevertheless there to see.

A **third** arguable difference, though at most one of degree, is related to how far decisions over the spending of aid should be peripheral rather than central: both how far they should be taken or influenced by authorities outside the receiving country, and how far they should be determined by governments at all rather than by people closer to the action and to those affected by it. Easterly is impressed by how often the actors in 'the West', multilaterals and all, have got it wrong: through ignorance or ideology, they have given what was not wanted, or else they have pressed policy conditions that were dysfunctional on the recipient countries. He deplores also the way aid agencies have mostly refused to extend aid to recurrent expenses that follow from the capital projects they have financed, resulting in unmaintained roads, clinics without medicines, and schools without teachers. He highlights also the extent to which recipient governments become smothered in administration by aid relationships.

> The 'growth industry' in Tanzania is actually bureaucracy. Tanzania produced more than 2,400 reports a year for its aid donors, who sent the beleaguered recipient one thousand missions of donor officials per year.
>
> *(2006, p. 166)*

Most significantly he discusses how receiving governments have misused and diverted aid given, and how far aid from certain donors including the IMF has even been concentrated on highly corrupt and brutal governments (who of course often rule over the poorest countries, which surely helps to explain why). From these experiences he draws the conclusion that it is futile to use aid *as a way of reforming bad governments*.

To these apparent pieces of evidence about the ineffectiveness of aid, however, there are *prima facie* interpretations different from those Easterly gives. Could it be that there has not been *enough* aid to have a reasonable prospect of effectiveness? The huge sums that Easterly cites for total aid since the business began need to be divided by something over 50 for the years over which they have been spread, and then perhaps by say 3 billion to get the average annual amount per head of the people in the recipient countries. If the resulting amount per recipient head per year turned out to be say 30 dollars in present prices, perhaps we should not so readily have expected miracles from it and, as we saw in Chapter 2, there have in fact been big improvements in longevity, young-child mortality, nutrition. No one

could or does claim that they are all due to aid or to anything governments have done, but to deny *any* contribution from external aid and international projects would surely be equally unreasonable.

Sachs for his part clearly believes that the rich world has resources of expertise which, properly mobilized and financed and with local support, can make huge differences on the ground. Witness the Sauri project again, where a programme of improvements worked out by Columbia University's Earth Institute seemed, at relatively low cost, to be radically transforming the material position of a community of 5000 poor people, whose poverty had previously been extreme and deepening (*Economist*, 9/6/2007, p. 60, see Box 21.1.) Sachs does not believe that all recipient governments are a dead loss at dealing with priorities and administering funds, and in fact proposes, in the UN Millennium Project documents (UN, 2005), that certain governments, including some in Africa, should have aid in 'programme' form, that is, to spend according to their own priorities. Though he may have some hope of *reforming governance* by selective aid allocation, that is presumably not the only or main reason for it. At the same time he would probably not entirely disagree with Easterly's proposal for winding down some forms of interference in recipient countries' policies,

Paul Collier, whose book, *The Bottom Billion* (2007), has been mentioned in Chapter 10, takes a different view of the role of aid from either Sachs or Easterly, mainly because he has a somewhat different position on the priorities in world development. He sees the urgent task as that of *setting on a growth path* those countries – most of sub-Saharan Africa, Central Asia, and a few others – whose incomes per head have been stagnant or falling. He sees each of them as caught in one or more of several 'traps'. The urgency of breaking those traps is that they easily generate vicious circles: poverty begets coups and armed conflict, which aggravate poverty, and between them they readily exacerbate the decline by worsening governance. Aid can have a role in helping to break open the traps, but when and where it is needed and in what form varies with the precise situation. Too much in the wrong form or at the wrong time may do harm rather than good. Collier relies heavily for his conclusions on empirical research in which political factors play a large role. No simple statement of his view of the roles of aid could do them justice.

BOX 21.2 TRANSFORMING SAURI: A GROUP OF VILLAGES IN WESTERN KENYA

Jeffrey Sachs (2005, pp. 234–5) outlines a list of inputs compiled by technical experts from Columbia University, as means for this miserably and increasingly poor rural community of 5000 people to emerge from its extreme poverty into continuous growth. These inputs – to be provided initially through outside finance at a cost roughly estimated in 2005 at $70 per person per year for about five years – would, it was hoped, reduce malaria transmission by about 90 per cent, cut mass deaths from AIDS, double or triple food yields per hectare, improve school attendance, reduce water-borne disease, and raise cash incomes (through crop sales, food processing, carpentry, clothes production, horticulture, aquaculture, and animal husbandry), in consequence drastically reducing chronic hunger and malnutrition.

An *Economist* correspondent with past Kenya experience made the following judgement in 2007:

> In the rural areas [of Kenya], the prospects are often grimmest, as the population swells and landholdings shrink. But a stirring and original experiment is being conducted by the UN, in

cahoots with Columbia University's Earth Institute and spearheaded by Jeffrey Sachs to stimulate a clutch of Millennium villages as models for emulation elsewhere. The early results of Kenya's prototype village, in Sauri in Western Kenya, where two-thirds of the people . . . live on less than $1 a day, are astonishing.

With an annual budget amounting to $50 a head administered by a UN team consisting mostly of bright young Kenyans, the Sauri villagers have apparently seen their rate of malaria go down from 43% to 11% (due to the provision of bed-nets), while school results have leapt (due partly to proper lunches). Maize production has soared five-fold (due mainly to fertilisers) and receipts from crop sales have steadied thanks to a cereals bank.

The big question is what happens after the projected five-year span of tutelage when the overseers go away – not to mention the extra help from an American philanthropist, George Soros, and sundry Norwegian and Japanese donors. That fragile and rotten thing, the Kenyan state, will have to help sustain those dramatic improvements, by providing decent teachers, doctors and farm advisers – just what Kenyans have most lacked. (*Economist*, 9/6/2007, p. 61)

Is there **a reasonable resolution between the Sachs and Easterly positions**? The most 'extreme' suggestions of the two sides each has its appeal. Sachs's vision that something comparable to the Sauri experiment might be repeated, with variations following diagnoses of local needs, right across the 22 million or so people of rural Kenya, provided only the initial funds can be obtained from outside the country, is irresistible before we come to nuts and bolts. It might take say $1.5 billion for each year of the initial five-year periods if all were taken simultaneously – perhaps a third as much a year if they were staggered over 15 years: large as an *addition* to Kenya's aid receipts, but not right off the scale. Social cohesion in each area might, as Sachs suggests, ensure enough accountability (of the recipients to each other and to the donors). Yet it is when we think of the mechanics of drawing up so many individual local plans with comparable expertise to that of the Earth Institute that courage wavers; and part of the apparent success in Sauri surely depends on by-passing the government. Yet – wherever the funds come from – if the government bureaucracy is to be by-passed, there must be an external body to dispense the funds and to co-ordinate with each group of villages, even if that body is a locally-based NGO or alliance of NGOs, one that must be able in that case to operate on a considerable scale. There may also be worries about the *fallacy of composition*: for example, fears that a radical increase in food or cash-crop production over such a wide field will lead to drastic falls in prices received. (Great to have lots more corn *if* the urban economy is poised for explosive growth, and great *if* the farmers can find new export products with buoyant world markets.) Scaling up further to cover the whole of sub-Saharan Africa – not mentioned by Sachs but hard not to consider if we are thinking of 'ending world poverty' by 2025 – multiplies all the doubts many times, even though *funding* at the Sauri rate might not be completely out of the question.

Easterly's more extreme suggestions are made tentatively; but one, clearly following from much of the argument, is to take aid as far as possible out of the hands of governments in recipient countries. This is the same direction as is suggested by Sachs's Sauri experiment. It would raise the same questions about the need for a parallel bureaucracy, except that Easterly's vision would not require everything to be done at once or in a co-ordinated fashion. He envisages also something like a market for aid, with the donor agencies, including NGOs, accepting bids (he sees them as competing for bids) from a variety of bodies on the spot. These would presumably be individual villages, town councils, clinics, schools, companies, cooperatives – proposing to provide water, sewerage, electrification, schools, teachers, equipment, medicines, health-workers, feeder roads, maybe even conditional cash grants to the poorest. He looks at ways, some already tried on a small scale, in which this might be done: an Internet exchange site, for example, or vouchers (pp. 376 ff.) A difficulty in all these decentralized schemes might be getting the necessary information, about the proposal and the proponents, to the donor agencies or clearing-sites. He proposes that the various agencies might specialize, presumably on either individual recipient countries or particular branches of welfare such as health or even particular diseases, which might both increase the total effective stock of useful expertise and make the individual agencies more readily answerable for results. (Yet the awkwardness of this persuasive suggestion for the rest of his thesis is that it ostensibly requires the co-ordination that he elsewhere seems to reject or to regard as impossible.) He suggests also that the various agencies might jointly fund a system of completely independent evaluation.

Two forms of vicious/virtuous circle: Sachs and Collier

Though Collier and Sachs are not ranged against each other in the way that Easterly opposes Sachs, their emphases are different, with Collier's models explicitly involving political variables. Both, as we've seen, invoke *vicious-circle* (or virtuous-circle) mechanisms. However, the circle that **Sachs** sees is that, properly chosen, *measures directly improving welfare will also release economic growth* and it is the choice, from among these measures, of those appropriate to the situation that is important. **Collier**, on the other hand, seems to suppose that it is growth on which attention should be concentrated; that welfare improvement will follow; and that (apart from the case in which a country is landlocked, about which not much can be done) *the key interaction is between growth and essentially political factors* such as how bad government is, how malign the effect of any resource bonanza is likely to be, and especially the risk of violent conflict.

So in Sachs's instances the key ingredient in the circle seems to be *funding*, with the precise use of the funding to be determined from one situation to another. Collier tries to find more general guidance *on the circumstances in which outside funds are likely to be helpful and what their uses should be.* He is also wary of the possibility that financial aid in the wrong amounts or wrong political junctures may have the often undesirable effects of a natural-resource bonanza (though his empirical estimate is that the effect of financial aid is likely on the whole to be better than that). In his view – if we may interpret – *bad government* and *violent conflict* should be seen as candidates for points at which the circle must be broken.

In the case of conflict there is a possible solution: international peacekeeping forces. In a recent co-authored paper, using numbers based on experience of recent conflicts and estimation of the effect of conflict on income and of income on the likelihood of further conflict, he and his colleagues compare the cost-effectiveness to be expected from peacekeeping as against typical financial assistance as a way of contributing to growth; and they find a peacekeeping force superior (Collier *et al.*, 2008; as reported in the *Economist*, 17/5/2008, p. 77). Where UN-type peacekeeping is an available option, that is an encouraging finding, because avoiding violent conflict is of course good in itself, and can be regarded as a highly desirable by-product of that way of pursuing economic growth.

It might be good if paying for genuinely multilateral peacekeeping could be treated as development aid.

This is not in conflict with Sachs's approach but it is more specific over the most useful way of breaking the circle for some of the poorest countries; and the emphasis on conflict seems only too relevant in much of sub-Saharan Africa.

BOX 21.3 TWO OF A NUMBER OF LARGE-SCALE SUCCESSES OF AID IN HEALTH

The following are two of the ten highly fruitful large-scale projects financed and undertaken through foreign aid of various kinds that are outlined by Jeffrey Sachs (2005, pp. 259–65).

'The Global Alliance for Vaccines and Immunization

'By the late 1990s, the campaign for childhood immunizations needed fortifying in two major ways. First, many new immunizations had been developed and adopted in the rich countries, but because of costs and lack of training and facilities, they had not been introduced into poor countries. Second, coverage rates achieved by the early 1990s had slipped, often the result of intensifying poverty and economic crisis in sub-Saharan Africa and other regions. Bill Gates stepped up to the effort, announcing an initial gift of $750 million from the Bill and Melinda Gates Foundation to reenergize the effort. The Global Alliance on Vaccines and Immunizations was launched in 2000 to guide the new effort. In the first years of its operation, the alliance made commitments of $1.1 billion to poor countries, and it had achieved a series of striking results. As of 2004, the alliance reported 41.6 million children vaccinated against hepatitis B; 5.6 million children vaccinated against Haemophilus influenzae type b (Hib); 3.2 million children vaccinated against yellow fever; and 9.6 million children vaccinated with other basic vaccines. . . . Its strategy has depended on the coupling of standardized technologies with systems of mass distribution . . . .

'The Campaign Against Malaria

'During the 1950s and 1960s, the World Health Organization launched a series of efforts directed at eradicating malaria. Sometimes judged to have been a failure, since malaria was certainly not eradicated, these efforts can be seen as a stunning success for certain parts of the world where the scourge of malaria was eliminated or brought dramatically and decisively under control. Well over half the world's populations living in endemic regions in the 1940s were largely freed of malaria transmission and mortality as a result of WHO's concentrated efforts . . . Africa, alas, was neither part of the program at the time, nor a beneficiary of its results until today. The standardized technologies that produced these regional, if not global, successes were two: the use of DDT and other pesticides to reduce the transmission of the disease and the use of chloroquine and other new antimalarial drugs to treat cases of it. (Newer technologies, especially antimalarial bed nets and artemisinin-combination therapies to treat the disease, combined with DDT where appropriate, can dramatically reduce the burden of the disease in Africa but will not eliminate the transmission entirely.)'

Source: Jeffrey Sachs, *The End of Poverty: how we can make it happen in our lifetime*, Penguin, London, 2005, pp. 261–2.

A resolution?

Reserving judgement on the more extreme hopes or suggestions on all sides, we may perhaps look for **developments along the following lines that might be accepted by all three protagonists**, though some of them would have implied 'ifs', and the question of policy 'conditionality' – in other words policy intervention – is evaded.

- *More funds* for aid, provided the way is cleared for them to be used for meeting welfare needs;
- Less subordination of aid to the priorities of particular *donor governments*;
- Less reliance in administering aid programmes on *recipient governments*;
- More *concrete, attainable, and testable objectives*;
- More *specific responsibilities* accepted by individual foreign governments, and other donors;
- Aid flows *more reliable*;
- Reduced *burden of aid-bureaucracy* on recipient governments;
- More effective ways of pursuing *co-ordination on the donor side*;
- A very high priority, in the use of potential aid funds, to UN-type *peacekeeping* – where that is relevant and possible – undertaken at a level likely to be effective.

It will be suggested below under 'New directions' how some of these pointers might be, or have already begun to be, followed.

New directions in aid: new sources and new channels

Objectives

From the general discussion and consideration of the arguments put by Sachs, Easterly, and Collier, we have tentatively defined in the paragraph above nine objectives as (largely) uncontroversial.

We shall discuss first ways of increasing funds available for development through international action; and then the ways, already present in embryo or possible, in which aid might be managed better from the donor side.

Additional development finance from international action

We confine the discussion in what follows to devices that might be used to increase funds available for public objectives, to be used by governments or multilaterals or by NGOs, with exclusively social goals. So we omit here ways of encouraging and supporting migrant remittances and private investment, important as they both are. We also omit for the present ways that may be found of increasing budgeted transfers from foreign governments, though it may turn out that most of the increased aid will have to come from that source. Instead, we look for ways that may be less fiscally costly or politically difficult for the governments of the rich world than simply increasing their own outlays on ODA, and that may help fill the gaps when the governments' willingness for increasing their own bilateral aid or their budgeted contributions to multilaterals has reached its limit.

Global tax co-operation

In the last section of Chapter 19, we discussed the ways in which tax co-operation could increase the revenue of developing countries. The tactical advantage of these methods is that they may well be, in fact often will be, of fiscal benefit rather than cost to the rich countries as well.

Private donations

An estimate in the early years of the century was that there was $8.37 trillion held in private fortunes of more than $30 million each. Tapping more of that wealth for world poverty-reduction presents a tantalizing challenge. Funding by private individuals and foundations of activities with an international-development purpose is not new, though it has been of increasing importance around the turn of the century. The crop research behind the 'green revolution' that bore abundant fruit from the late 1960s was funded by the Rockefeller and Ford Foundations. By 2003, the Bill and Melinda Gates Foundation had committed more than $2 billion to 'alliances in global health'; its most notable contribution has been in immunization of children, paying at one time three-quarters of the finance for the Vaccine Fund associated with the Global Alliance for Vaccination and Immunization. Rotary International at the same time had raised $450 million, together with the services of large numbers of volunteers, toward the final eradication of polio (Stansfield, 2002, pp. 94, 99). There are plenty of other examples in the health field. Attracting finance from such sources may depend largely on the capacity of health or education or food-research 'entrepreneurs' to present 'packages' of manifest human value to those who have the funds to dispense (see Micklewright and Wright, 2004).

Special Drawing Rights (SDRs)

We have outlined in chapter 12 the role of the IMF's SDRs and the rules applying to them. This was in the discussion of their use in stabilization through enabling developing countries to obtain almost costlessly additional international reserves. At the end of the section in that chapter on SDRs, we explained why further issues of SDRs might also permit the rich countries to transfer their receipts of SDRs to developing countries. While the recipients simply held the SDRs as reserves, it would be at no cost to either party on the (inevitable) assumption that the recipient countries would pay the interest due *to* the IMF on the SDRs from the countries that were their original recipients, while they (the secondary recipients) themselves would be receiving interest of the same amount *from* the IMF for so long as they continued to hold the SDRs. If, however, these secondary recipients wanted to *spend* these assets rather than using them to expand reserves, they would cease to receive the interest from the IMF and would in effect be financing that spending with loans that charged the (low) SDR interest-rate and had no maturity date. Where these countries already had debts contracted on less favourable terms, they would be able to buy these debts out through the SDRs and so reduce their servicing obligations. Thus, issue and transfer of SDRs could have a role in 'development finance', but not as the equivalent of free grants unless the recipients were simply to hold the assets as reserves.

Global lottery or 'premium bond'

A further possibility is that one of the international organizations might raise funds by running a lottery, or by issuing 'premium bonds' (bonds paying little or no real interest but giving the holder the possibility of a large prize) as the UK Treasury does. This is examined by Addison and Chowdhury (2004).

Global taxes

The term *global taxes* refers here to taxes collected by national governments under some form of international agreement and for some global purpose. No international organization yet in existence has taxing powers, or of course any tax-collecting mechanism. Making the tax global can only be by consensus of all the governments taking part. This has to be said because of the hysterical and misleading propaganda sometimes directed at any idea of a global tax.

The forms of global tax seriously discussed are all of them *indirect* taxes on particular transactions or activities. It could always be argued that an income tax levied on every country (or every high-income country) at rates progressive in relation to the countries' incomes per head would be administratively simpler and plainly more equitable than any of the indirect taxes considered. That would be relevant if such a direct tax had the slightest chance of being generally accepted. However, we have seen how patchy compliance has been among the rich countries with an analogous obligation to devote 0.7 per cent of income to foreign aid. The hope is that some form of indirect tax for the purpose of supplementing existing aid might prove more acceptable to those who have to draw up government budgets and to the public opinion that they have to consider. One appealing idea is that the tax might be acceptable because it is levied on a negative externality: some polluting or otherwise undesirable activity. So taxing would kill two birds with one stone; a 'double dividend'. One problem here is that the two functions may become to some extent competitive: the rate of tax suitable for one function may be less than ideal for the other. More serious is that, if the anti-pollutant tax would have been applied anyway, government and public may not see any strong reason why the revenue should not be used domestically like that from any other tax. We consider four such taxes with, at first glance, obvious appeal.

Tax on arms sales or arms traded internationally This is mentioned because it is one tax instrument specifically supported by the Quadripartite Report from the Governments of France, Brazil, Chile, and Spain in 2004 (France, 2004a, pp. 36–41). The Report advocates a tax (effectively a VAT) on all arms sales, not only those internationally traded, though its discussion mainly calls attention to the tax's disadvantages and difficulties. (The Report also argues for a currency-transaction tax – discussed below – and for the development use of SDRs; and France at the time was advocating, and was itself about to join others in applying, a tax on air tickets.) One awkward feature of an arms-sales tax is that governments would largely be taxing themselves and their activities. (The legal arms trade, the only part of it that is taxable, will mainly have governments as the buyers, and often too as the sellers.) Governments all over the world, rich and poor, are buying arms and obviously try to get them as cheaply as possible. Other governments are selling them or exerting themselves to support the sales of resident arms producers. We might wonder how much zeal they will show in taxing themselves and their favoured producers. There will be great opportunities for fudging, especially when governments are producing arms for their own use. Moreover, whoever formally pays the tax, buyers or sellers, it is hard to say who will bear most of the burden. It is not improbable that the buyers will bear a large part, and this could easily mean that the poorer countries, which often spend heavily on arms in relation to their incomes, will be paying a higher proportion of their income on this tax than the rich.

A carbon tax This is attractive not only because of its double-dividend character but also because a very small rate of tax applied uniformly across the world on carbon content (or its greenhouse-effect equivalent) would raise considerable revenue. (It was worked out recently that a tax equivalent to 5 US cents per US gallon of gasoline would raise about $130 billion a year if – as seems likely – the tax did not significantly deter consumption. High-income countries alone at the same rate would raise about $60 billion.)

As has just been implied, tax at that level would make very little difference to carbon use. A compromise reached to implement both arms of the 'double dividend' by taxing much more highly (which over a considerable range *would* very probably yield more revenue, not less) might also set a limit to the proportion of the revenue that would be used for global purposes and let the country collecting the tax keep the rest. If poor as well as rich countries submitted globally all (or equal proportions) of what they collected, and the tax rate was uniform, poorer countries would often be submitting higher proportions of their incomes than richer ones, because the poorer often have relatively high carbon-intensities in their output, but the worst of the injustice of this could be avoided by directing proceeds from the rich countries alone to global development.

However, as with arms sales, it might be difficult to keep all collecting governments steady in the resolve to submit the whole or a large part of the revenue internationally, or indeed difficult to get the agreement in the first place. At the same time, it may be worth persevering with this idea, especially as concern over global warming is increasing, so that the unthinkable may become thinkable. Taxing is an *efficient* way of pursuing the objective of reducing greenhouse emissions. Those unduly hurt by the tax may be compensated in other ways. Funds received internationally might be earmarked, wholly or partly, for emissions-reducing investments, or for measures to protect from, or to remedy, or at least palliate, the adverse effects of global warming (such as inundation in some areas, persistent drought in others).

Tax on air travel This is mentioned because an air-ticket levy was floated in 2004 by the government of France as a possible universal tax for international development, and was approved by around 40 governments at the time. At least 19 governments have taken measures to apply it, including France, Norway, South Korea, the UK, and a number of developing countries. At the rates applied by France, the estimated annual revenue would be about 200 million euros, or $250 million dollars, and it was to be used to combat HIV/AIDS, malaria, and tuberculosis. There is a strong case on negative-externality grounds for taxing air travel, principally because of its very high carbon emissions and the fact that, by longstanding international agreement, aircraft fuel has not been taxed. Taxing tickets rather than fuel is a definite second-best but is administratively easy and watertight. Taxing aircraft fuel generally at rates comparable to the highest applied in Europe to fuel for road travel would presumably make a big contribution to filling the funding gaps of the Sachs report, but, to be effective on international flights in or out of any particular country, it would have to be applied fairly generally across the world.

A currency-transaction tax (CTT) This device, proposed as a universal tax on currency exchanges in the wholesale market, came out of the shadows from the late 1990s, with the recognition that institutions were by then such that it could be effectively collected through financial clearing and settlement systems, and the further recognition that taxing foreign exchanges for *stabilization* purposes could be operated (by individual countries, temporarily, and *ad hoc*) quite independently of any universal and regular revenue use of a CTT (Schmidt, 1999, 2000, 2001). Systematic empirical estimation of the elasticity of activity in the markets with respect to rates of tax has suggested that a tax rate of 0.005 per cent – chosen conservatively, because of its relationship to the observed variation in the market

'spread', as highly unlikely to disturb the market fundamentally, could be expected to raise over $30 billion a year, provided the monetary authorities of the US, the Euro area, Japan, and Britain co-operated in collecting the tax (Schmidt, 2008). If they co-operated in the venture, collection could be very close to complete. There would, it seems, be no sense in imposing and collecting it any other way. The burden of the tax would be borne across the world, and we might hope that it would be completely out of the question for the four collecting authorities to regard themselves other than as performing this task (at very little cost to themselves because of the mode of collection) for the world at large. The tax – collected other than as an emergency currency-stabilization measure on transactions in one particular currency by that currency's own issuing authority – would rightly require substantial world approval; it would be raised for global purposes, or it should not be raised at all. This distinguishes it from the other tax devices mentioned here, all of which could be collected by individual jurisdictions and plausibly claimed to be their own.

New channels

Certain developments that have already occurred since the late 1990s begin to meet some of Easterly's criticisms by emphasizing specificity of attainable objectives and accountability of particular agents; real possibilities, rather than paper aspirations, of concerted action by donors; and reduction of the bureaucratic burden of aid on the recipient governments. Other devices that *might* do so are not remote from possibility, particularly if reasonably large funds from new sources – either of undeniable global provenance or earmarked by agreement for global purposes – can be tapped.

Promulgation of the **Millennium Development Goals** (see this chapter's Appendix 21.1) in 2000 fixes attention on variables *directly impinging on welfare and capable of being directly and measurably altered* by official action, rather than on the elusive target of higher economic growth.

Formation of **Global Funds** and associated alliances – such as the Global Fund to Fight AIDS, Tuberculosis and Malaria (GFATM), started in 2001, and the Vaccine Fund, associated with the Global Alliance for Vaccination and Immunisation (GAVI) – has *tempered the generalism of the aid business* by giving particular bodies specific and limited responsibilities, for which they can call on technical advice wherever it is to be found. These funds have been called 'multiactor global funds' (Heimans, 2008) in that they involve, as participants in funding or control or both, governments and international organizations on the one hand, and, on the other, the private sector (which can cover NGOs, charitable foundations, corporations or industry groups, educational and research institutions, wealthy individuals, and as donors the general public). Heimans (2008), while recognizing in these funds possibilities of new ideas and initiatives freed from traditional boundaries and bureaucracies, also faces the possibility that they may be more restricted owing to the number of entities that they represent, or at the other extreme that they may not be sufficiently accountable. **International networks on particular objectives** include but go beyond the Global Funds, which could be, like the GFATM, primarily governmental in inspiration. A variety of combinations of private and public participation in organization and funding and knowledge-support are possible. Stansfield, (2003, pp. 94–9) and Sachs (2005, p. 283) give a number of examples in the health field.

A further device, so far implemented only as a pilot, is the **International Finance Facility (IFF)**, a scheme proposed by Gordon Brown, then British finance minister, in 2003. The particular idea here was that aid expenditures could be brought forward through borrowing against future aid commitments. It was intended to involve all the rich donors, but in its original ambitious form received strong support only from France and Britain. An advantage might have been that, as the financial commitments were accepted jointly, there would have had to be co-ordination among the donor countries, though this aspect tended to be played down for presentational purposes. So far the outcome has been a pilot project ('IFF Im.') – one outcome of the 2005 G8 meeting – on a smaller scale than was originally envisaged, to support immunization of children under the GAVI, expected for a period of some years to increase the annual funds available, for that purpose and under those auspices, by $500 million over and above the $600 million a year previously spent. Six donor governments have agreed to participate (OECD, 2007, p. 20). The case for using this device for that particular purpose may depend on the belief that spending at a high enough level now will yield some once-for-all achievements in conquering certain diseases.

A further innovation of 2005–6 is an **Advanced Market Commitment** for new vaccines against certain tropical diseases that otherwise lack enough commercial prospects to attract the research and development needed from pharmaceutical companies. The idea, advocated for some years by Sachs, is that donors would guarantee a market once the appropriate vaccine was discovered. This is a form of aid that would only be paid out when the object was achieved (ibid.).

In order to concentrate donor action more usefully in each particular recipient country and to reduce the bureaucratic burden each of them has to bear, Sachs (2005, pp. 285–7) proposes **something like a 'one-stop shop'** in each recipient country, with a UN representative serving as the channel through which all the donor agencies, including the World Bank and IMF, deal with the recipient. This is a long way from what happens at present, but the possibility of something of the kind, whichever agency is to act as the main contact point, clearly increases as and if more of the aid comes through multilateral channels.

Tapping any large source of funds that is clearly international (such as, for reasons we have pointed out, a general currency-transaction tax) raises the question how such funds are to be administered for global welfare purposes. A suggestion of one way in which this might be done acceptably to all the major players is given by Clunies-Ross and Langmore (2008). The idea is that a new arm of the World Bank should be created for this purpose, with authorization to give aid in grant form and to give it not only through sovereign governments but also through subordinate governments, NGOs, multisectoral networks, and other multilaterals. Its brief might be set by the UN General Assembly under inter-agency advice; and there should be full transparency and independent scrutiny of the new entity's performance. Other equally satisfactory arrangements might well be possible, but it seems that a large new source of funds – of undeniably world provenance or otherwise committed to world disposal – would give the world an opportunity for creating a co-ordinating force with real influence among the donors in each receiving area and overall.

Over and above the humanitarian needs embodied in the Millennium Development Goals, the prospect, from as early perhaps as the second decade of the century, of extraordinary costs for the palliation of the potentially lethal effects of climate change – palliation through, for example, flood control, sea defences, desalination, long-distance transfer of water, and, in the (almost unthinkable) extreme, resettlement of very large numbers of people, possibly several or all of these – makes a large fund genuinely **at world disposal** an urgent necessity.

Summary conclusions

- The humanitarian **purpose** of promoting 'development' and hence of 'development aid' is to reduce world poverty, and to open to an increasing range of the world population an enhancement of freedom that depends in part on realizing ever more widely the material advantages of present world technology and organization.
- **Official development assistance** (grants and concessional loans from governments and multilaterals) is now quantitatively much less important than the sum of **other sources** of external capital-flow to developing countries – direct and portfolio investment, commercial loans, migrant remittances – but it is the part that can be deliberately directed by public policy to promote economic growth and poverty reduction.
- However, official aid is also not the only form of flow that is social, rather than commercial, in its motivation. There has been increasing importance of funds coming from **private fortunes or foundations**, and from or through **NGOs**.
- The **level** of official development assistance given by the high-income countries, except from a small number of (small) countries, has consistently fallen short of the aspirations to which those countries have committed themselves through international resolutions. Its **distribution** among recipient countries has not been at all closely related to their needs as indicated by populations or income levels or degrees of poverty. Even for much of the minor share that comes through the multilaterals, aid has not fitted in any obvious way into a **strategy** of world development. Also, the strategy or strategies broadly promoted by the World Bank and IMF in their own lending decisions have not been, in their entirety, universally approved.
- Whether aid has worked *to promote economic growth* has been questioned. There have been conflicting answers from econometric studies. Yet recently there have been a number of results from which together the conclusion has been drawn that, at least under some conditions, aid contributes to economic growth. But on the question of what those conditions are, how far they can be generated by policies, and if so by which policies, those studies offer no consensus.
- After consideration of the Sachs–Easterly 'debate' and the recent contributions of Collier, we suggested the need for substantially larger amounts of aid *provided it can be used successfully in the interest of the poor, and for eight directions of change mainly in the way aid is managed internationally*. It appeared that change in some of these directions was already occurring.
- As ways of *increasing the volume* of development finance, we mentioned the various forms of international tax cooperation discussed in Chapter 19 and five broad possible sources of additional external aid that would *not* involve donor governments in additional budgetary allocations to bilateral aid or contributions to international institutions (ODA in the usual sense), including as one option 'global taxes'. Among these one possibility at least, a currency-transaction tax, could raise funds of clearly global provenance in sufficient amount to give an international body allowed to administer it an effective co-ordinating role among aid donors.

- Beyond the objectives of the Millennium Development Goals, the prospects of hugely costly expenses for palliating the human effects of climate change makes urgent the need for a large fund fully at global disposal.
- Under '*new directions*' for aid, we considered recent changes that have already moved very tentatively toward 'additional sources'; toward greater 'sectoral' specialization of aid through various forms of 'network' and greater co-ordination among donors, public and private; toward reducing reliance on recipient governments for administering aid receipts; and toward closer orientation to concrete welfare improvements. We also aimed to suggest how changes in those directions might be furthered by realization of a large new source of funds that were indisputably 'global', rather than national, in provenance.

It is hard to doubt the *potential* of foreign aid – in amounts well within the capacity of the donor countries to pay while scarcely noticing it – to generate big welfare improvements, even if not spectacular economic growth. Something – lack of a sense of urgency, itself possibly related to the other obstacles such as internal or international politics, or administrative weaknesses or lack of co-ordination among donors – seems to get in the way. There are promising options for substantially increasing the volume of aid, including, but not only, fulfilment by the donors of the targets that they have accepted – but ingenuity and flexibility, such as are already evident in some new initiatives, are also needed in order to overcome the widely recognized weaknesses in what actually happens.

Questions for discussion

21.1 Suppose that the necessary funds (say $12 billion a year for 15 years) could be obtained. How realistic would it be to make arrangements for replicating the Sauri-type improvements, adjusted to local conditions and needs, over 15 years across say 90 per cent of the rural population of sub-Saharan Africa?

21.2 Would you agree with the assertion that decisively improving living conditions for the poor in informal settlements around Third World cities is mainly a political task – for them and/or for their governments?

21.3 Should the giving of aid be *conditional* on the fulfilment by recipient governments of reforms of policy or of systems of accountability – sometimes at least, or else never? On what conditions, if any, of policy or practice, should donors insist?

21.4 Is there ever validity in the idea (as invoked, for example, by Jeffrey Sachs over the condition of areas such as Sauri) of using foreign aid to break a vicious circle of poverty?

21.5 What do you think of Paul Collier's view that a military peacekeeping force may be the most cost-effective way in which the outside world can contribute to the development of a conflict-prone country?

21.6 Is source-tying of aid ever justified?

Additional reading

Collier, P. (1997) *The Bottom Billion: why the poorest countries are failing and what can be done about it*, Oxford University Press, Oxford.

Easterly, W. (2006) *The White Man's Burden: why the West's efforts to aid the Rest have done so much ill and so little good*, Penguin Press, New York.

McGillivray, M., S. Feeny, N. Hermes and R. Lensink (2006) 'Controversies over the impact of development aid: it works; it doesn't; it can, but that depends . . .', *Journal of International Development*, **18**, pp. 1031–50.

Sachs, J.D. (2005) *The End of Poverty: how we can make it happen in our lifetime*, Penguin, London.

Stiglitz, J. (2006) *Making Globalization Work*, Allen Lane, London.

UN (2005) UN Millennium Project, *Investing in Development*, New York, January ['the Sachs Report']. Found at http://unmp.forumone.com/eng_html_07.html.

The recent works by Collier, Easterly and Sachs, taking three highly distinct positions, are worth reading in full and all read extremely well: Sachs, guardedly and conditionally optimistic; Easterly, anti-establishment and maybe stronger on pulling down than on building up; Collier, persistently using systematic empirical investigation to feel his way through the thickets blocking the path for the poorest countries out of stagnation or worse. McGillivray, Feeny, Hermes and Lensink give an up-to-date account as of 2006 of research on the aid-and-growth question. Stiglitz, in the less famous of his two recent popular books, takes the whole field of world policy toward the developing countries and looks for institutions, consistent with the positive contributions of globalization, that in a number of areas will make the system work better for the poor.

Appendix 21.1 The Millennium Development Goals[1]

Millennium Development Goals (MDGs)

Goals and Targets		Indicators
Goal 1: Eradicate extreme poverty and hunger		
Target 1:	Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day	**1.** Proportion of population below $1 per day **2.** Poverty gap ratio [incidence [*21] depth of poverty] **3.** Share of poorest quintile In national consumption
Target 2:	Halve, between 1990 and 2015, the proportion of people who suffer from hunger	**4.** Prevalence of underweight children (under-five years of age) **5.** Proportion of population below minimum level of dietary energy consumption
Goal 2: Achieve universal primary education		
Target 3:	Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling	**6.** Net enrolment ratio in primary education **7.** Proportion of pupils starting grade 1 who reach grade 5 **8.** Literacy rate of 15-24 year olds
Goat 3: Promote gender equality and empower women		
Target 4:	Eliminate gender disparity In primary and secondary education preferably by 2005 and to all levels of education no later than 2015	**9.** Ratio of girls to boys in primary, secondary and tertiary education **10.** Ratio of literate females to males of 15-24 year olds **11.** Share of women In wage employment In the non-agricultural sector **12.** Proportion of seats held by women in national parliament
Goal 4: Reduce child mortality		
Target 5:	Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate	**13.** Under-five mortality rate **14.** Infant mortality rate **15.** Proportion of 1 year old children immunised against measles
Goal 5: Improve maternal health		
Target 6:	Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio	**16.** Maternal mortality ratio **17.** Proportion of births attended by skilled health personnel
Goal 6: Combat HIV/AIDS, malaria and other diseases		
Target 7:	Have halted by 2015, and begun to reverse, the spread of HIV/AIDS	**18.** HIV prevalence among 15-24 year old pregnant women **19.** Contraceptive prevalence rate **20.** Number of children orphaned by HIV/AIDS
Target 8:	Have halted by 2015, and begun to reverse, the incidence of malaria and ether major diseases	**21.** Prevalence and death rates associated with malaria **22.** Proportion of population in malaria risk areas using effective malaria prevention and treatment measures **23.** Prevalence and death rates associated with tuberculosis **24.** Proportion of TB cases detected and cured under DOTS (Directly Observed Treatment Short Course)
Goal 7: Ensure environmental sustainability*		
Target 9:	Integrate the principles of sustainable development into country policies and programmes and reverse the toss of environmental resources	**25.** Proportion of land area covered by forest **26.** Land area protected to maintain biological diversity **27.** GDP per unit of energy use (as proxy for energy efficiency) **28.** Carbon dioxide emissions (per capita) [Plus two figures of global atmospheric pollution: ozone depletion and the accumulation of global warming gases]
Target 10:	Halve, by 2015, the proportion of people without sustainable access to safe drinking water	**29.** Proportion of population with sustainable access to an Improved water source
Target 11:	By 2020, to have achieved a significant improvement in the lives of at least 100 million slum dwellers	**30.** Proportion of people with access to Improved sanitation **31.** Proportion of people with access to secure tenure [Urban/rural disaggregation of several of the above indicators may be relevant tor monitoring Improvement in the lives of slum dwellers]
Goal 8: Develop a Global Partnership for Development*		
Target 12:	Develop further art open, rule-based, predictable, non-discriminatory trading and financial system Includes a commitment to good governance, development, and poverty reduction – both nationally and internationally	**Some of the indicators listed below will be monitored separately for the Least Developed Countries (LDCs), Africa, landlocked countries and small island developing states.** **Official Development Assistance** **32.** Net ODA as percentage of DAC donors' GNI [targets of 0.7% in total and 0.15% for LDCs] **33.** Proportion of ODA to basic social services (basic education, primary health care, nutrition, safe water and sanitation)
Target 13:	Address the Special Needs of the Least Developed Countries Includes: tariff and quota free access for LDC exports; enhanced programme of debt relief for HIPC and cancellation of official bilateral debt; and more generous ODA for countries committed to poverty reduction	**34.** Proportion of ODA that is untied **35.** Proportion of ODA for environment in small island developing states **36.** Proportion of ODA for transport sector in land-locked countries
Target 14:	Address the Special Needs of landlocked countries and small island developing states (through Barbados Programme and 22nd General Assembly provisions)	**Market Access** **37.** Proportion of experts (by value and excluding arms) admitted free of duties and quotas **38.** Average tariffs and quotas on agricultural products and textiles and clothing **39.** Domestic and export agricultural subsidies in OECD countries
Target 15:	Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term	**40.** Proportion of ODA provided to help build trade capacity *Debt Sustainability* **41.** Proportion of official bilateral HIPC debt cancelled **42.** Debt service as a percentage of exports of goods and services **43.** Proportion of ODA provided as debt relief **44.** Number of countries reaching HIPC decision and completion points
Target 16:	In cooperation with developing countries, develop and implement strategies for decent and productive work for youth	**45.** Unemployment rate of 15-24 year olds
Target 17:	In cooperation with pharmaceutical companies, provide access to affordable, essential drugs in developing countries	**46.** Proportion of population with access to affordable essential drugs on a sustainable basis
Target 18:	In cooperation with the private sector, make available the benefits of new technologies, especially information and communications	**47.** Telephone lines per 1000 people **48.** Personal computers per 1000 people

* *The selection of indicators for Goals 7 and 8 is subject to further refinement*

Source: Reproduced by permission from: S. Devarajan, M. J. Miller and E. V. Swanson 'Goals for Development: History, Prospects and Costs World Bank Policy Research Working Paper, WPS 2819, April 2002

[1] The first ten years of the 25-year period adopted for achieving the Goals.

Appendix 21.2 OECD Development Assistance Committee (DAC)'s aid and capital-flow terminology

ODA (Official Development Assistance) and OA (Official Aid). Both of these categories cover (a) grants and (b) loans of more than a year's term and with a 25 per cent or more grant-element, that come from official sources, and are given primarily for economic development and welfare. They include technical-co-operation grants but not flows for military purposes. The only difference between ODA and OA is in the list of recipients covered. OA has covered payments to 'transitional countries' and some 'advanced' developing countries; ODA, to the rest.

ODF (Official Development Finance) is wider than ODA in that it *also* includes *non-concessional* developmental loans from multilaterals, and also bilateral developmental loans with *less than* a 25 per cent grant element.

OOFs (Other Official Flows) cover flows, to countries on DAC lists of aid-recipients, that are ineligible as ODA or OA because they are not developmental or have too low a grant element. It is not clear whether they overlap with ODF.

Net flows. In the case of loans, net flows are the incoming amounts disbursed, net of outflows for amortization or repatriation of capital (but not outflows of interest) – all net of corresponding movements in the reverse direction. World Bank figures cited in the chapter clearly use the term to include also the corresponding flows for direct investment and portfolio equity investment, and also grants.

Net transfers. For loans, these are net flows *minus* net outward interest payments. (Again they can be extended to include the corresponding figures for investment, with profit remittances and dividends deducted in the same way as interest.)

Private flows. These cover flows on market terms out of private-sector resources: direct and portfolio investment and a variety of forms of loans; together with private grants (grants made by NGOs, and presumably also individual philanthropists, net of any government subsidies). It is not clear in the source whether they include net migrant remittances.

Debt-service ratio. A country's debt-service ratio on its stock of borrowings is taken by the DAC as:

(Interest payments and loan-amortization out) *divided by*
(Exports of goods and services *plus* private inward transfers)

Source: OECD (2007), *Development Assistance: Efforts and Policies, 2006 Report*, OECD, Paris.