

## The Aid Juggernaut - can it be made to take a different path

### Introduction

Billions of dollars of aid are given to developing countries every year and have been for almost 60 years. Despite this the numbers of people living in poverty exceed 1.5 billion, growing, rather than falling by 25 million a year. Has aid money done any good, or is it harming the poor? Can aid (more of it, and better delivered and utilised) ever hope to eradicate poverty? How important is aid in a world where private capital flows to developing countries outstrip several times over? What is the best way forward?

The answers to these questions are being played out, and debated in a world which is seeing fundamental changes within the engagement between North and South. On issues to do with trade, globalisation, security, migration and public goods, the interests of the donor and recipient countries vary significantly. The aid system, is centrally placed and already plays a key role in influencing outcomes for developing countries in all these areas.

The question for those like Actionaid is how one can find a coherent yet effective positioning through the competing claims, interests and theories on aid that promotes more effective and sustainable poverty alleviation outcomes.

The BIG 5 debates we discuss are:

- **Has the Monterrey consensus changed anything?**
- **Trade for the rich, aid for the poor?** What is the use of aid if other relationships between the North and South ( such as trade) impoverish the poor
- **Foreign policy or aid policy ?** *Is aid an entitlement or about donor interest?*
- **How to get over the debt problem?**
- **How do you make the institutional form of the aid system effective, efficient, and accountable?**

We examine opposing positions on these debates and cite recent evidence to support the propositions of the different players. In practice, opposition, suggestions for change and alternatives to the current aid system come from 3 slightly different groupings. We then try and summarise the positions of the players into these three positions: those of the fundamentalists, the transformative groups and the liberals.

The camp of the fundamentalists believe that the aid system needs to be dismantled, the rationalists who believe that there is a political space for working to transform the aid system in order to make it more pro-choice of the recipients , and a technocratic grouping, who believe the that the system is basically sound but can be improved by better policies and implementation.

At one end of the spectrum is the **fundamentalist** group that believes in revolutionary change. They believe that the foreign aid institutions have a power far out of proportion to the funds that they manage. In Bangladesh for example where aid constitutes only 3% of the national budget they are able to assert conditionalities. It see the business of aid as really being about the spread of ideas and about power. Aid is one way in which powerful institutions encode their doctrines and impose them on the less powerful <sup>1</sup>

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<sup>1</sup> What's wrong with Foreign aid, David Sogge,

The fundamentalist group believes that there are no duty bearers within the aid system and that the real motives of aid are largely political and strategic. They are extremely powerful in that if the IMF withdraws from giving aid to any country then all other bi-lateral and multi-lateral institutions will follow as will most of private banks and investors.

They therefore call for an end to the aid system as it stands, and look for an antagonistic disengagement with the system. They also seek reparations to cover colonial and neo-colonial extraction and net transfers from the south to the north.

The **transformative** grouping do not think that disassociating with the system is a realistic option. They believe that it is worth engaging but in a way that is designed to transform the system. The group views the current aid architecture as being dominated by and subservient to the interests of a few OECD countries, and whose structures and patronage ties shield it from serious scrutiny and accountability. In its present form, the current aid architecture can only deliver marginal benefits if any. It is however politically aware enough to recognise that fundamental transformation is possible if critical mass of opportunities present themselves for change.

In terms of outcomes the transformative group would like to change the international aid architecture with improved governance (transparency, accountability and accountability of aid institutions, to see more coherence of trade, debt, and aid policies (and now security policies), a recognition of the plurality of sovereignty (state, local governance institutions, local collectives) leading to genuine policy ownership by recipient countries.

This in turn would lead to accelerated moves towards increasingly predictable flows of funds for budget support, internationally negotiated agreements on performance standards and selectivity criteria. They would like to see structural adjustment and growth strategies with a 'human-face' and accelerated spending on direct welfare

The **rationalists** do not agree that one needs to change the system. The system as it exists has the potential to alleviate poverty if interventions are better designed and executed. They are evolutionary in approach and recognise and are apologists for many of the past mistakes such as the diversion of funds during the cold war, the debt crisis, the harshness of the structural adjustment process, and commercial interests which have led to tied aid.

While there is recognition of some politics, there is a core belief that the fall of communism, rise of multi-literalism, and the willingness within aid bureaucracies to think rationally about aid, poverty and development, has created an environment where policy changes – re-tooling the aid industry perhaps through some procedural reform of aid institutions – can make aid more effective without necessarily shaping the political environment that drive aid. Equally although there has been too much focus on growth based strategies conditionalities are not all completely wrong, but the manner in which they were implemented caused greater vulnerability to shocks. ( export volatility and food scarcity etc.)

In many ways these are not competitive positions. Work done for example in the sphere of transformative action will have impacts in the practical , technocratic sphere and vice versa.

We begin however with outlining the state of play in the aid system at present.

## **The State of play in the Aid System**

Over the last fifty years, foreign aid has followed a familiar pattern: every bi-lateral agency has set its own course, own rules and conditions, and imposed its own will on the debtors,

and all being moderated by the IMF and World Bank under the rubric of economic growth and market-orientation. The signing of the UN Millennium Declaration in September 2000 signalled a departure from past when the entire donor community set a 'mutual' target in the form of Millennium Development Goals (MDGs), whereby 'aid' began to take a more 'poverty focused' direction. Hopes were raised again that the aid system was gearing itself up to address the challenge of fighting poverty and social exclusion affecting at least 2 billion people, mostly women and children.

The Monterrey conference held in March 2002 built on this because it brought a new momentum and hope to the aid system and resulted in pledges of additional funds. It dealt with many of the weaknesses of the past, and provided a clear link to poverty and good policy .

The Monterrey consensus involved 3 key agreements.

- a) that recipient countries recognize and take up their responsibilities for good governance and the establishment of development priorities in exchange for increased aid volume (0.7% of GNP) and quality and new policies on open trade;
- b) the commitment to achieve the MDGs required recipient countries to prepare plans with set monitoring targets and costs to attain these, against donors countries agreement to fund these.
- c) build a new partnership between donors and recipients where donors would support democratic, consultative processes for development. This was based on a recognition that conditionality did not work and that homegrown policy and adequate institutions directed to pro-poor goals would be a more effective way to deliver results on poverty.

In addition to the agreement, the process for practical implementation was made simpler with the adoption of the PRSP framework<sup>2</sup>. This combined a country's macroeconomic, structural and social policies for growth and poverty with its financing needs. Lending decisions to countries are based on the production of the PRSP, which is then assessed against policy and institutional scores made by a Joint Staff Assessment of the WB and IMF.

The PRSP as a methodology also has the advantage of allowing for participation and ownership of wider civil society in the development of country plans, and also when agreed, enabled donors to provide budgetary support ( a long-time demand of recipient countries) more effectively.

While the consensus has provided a very positive focal point, there has been an under-current of concerns from all sides. For example, while the IMF sees the PRSP process as a way to streamline conditionality<sup>3</sup>, many of the people against what happened in the previous SAP process saw Monterrey as a signal away from conditionality. Other fears have included the fact that Monterrey restricts the options available to aid recipient countries. In a worse case scenario it could choke off all sources off funds to the poorest countries, if they are unable to satisfy the bank/IMF ratings for fund eligibility.

Despite the consensus on process, the aid system has not remained static. In contradiction to the PRSP process and budgetary support potentially irreconcilable Global Funds such as the Global Fund for TB and HIV/ AIDS have been introduced. Other initiatives such as the International Financing Facility ( UK ) and the Millennium Challenge Account (US) are in the process of being finalised.

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<sup>2</sup> See glossary. PRSPs were first introduced in 1999 only for Highly Indebted Poor Countries.

<sup>3</sup> Conditionality in IMF-Supported Programs – Policy Issues. Prepared by the Policy Development and Review Department February 16, 2001

A new framework/architecture of aid for the period 2005-2010 is now being debated. The meeting of the UN special assembly to assess progress on the MDGs in 2005 is giving extra impetus to debates about the overall aid architecture. Much of this depends on the experience of implementation and whether it has matched the expectations of the donors or the recipient countries.

The debates, including the evidence on the implementation of Monterrey, the attainment of MDGs will to a large extent decide the future shape of the aid system. We look at some of the major debates and the perspectives offered on these by the various players.

## The Key Debates

### 1. Has the Monterrey consensus changed anything?

In general, OECD countries (including most OECD INGOs) have taken the view that the Monterrey consensus and the PRSP provide a framework that will make economic growth and poverty reduction go hand in hand in the developing countries. However, there is growing scepticism in the developing countries as to what these can achieve for their economic and social development. While some (an increasing number of 'new' civil society and policy groups) have been participating in the process, a larger group has been questioning the basis, the rationale and the implementation of the process. They argue that poverty reduction is a smokescreen to continue with the BWIs' agenda of structural adjustment and liberalisation.

The OECD position on conditionality: Aid donors are accountable to their national parliaments and publics for the money they provide as aid. They legitimately expect that aid is used effectively and efficiently by recipient countries. There are also ample examples of the use of foreign aid where funds have been squandered. The two conditionalities that donors have chosen traditionally to apply have been to ensure the recipient state enforces:

- a) Macro-economic discipline ( low inflation, fiscal control etc)
- b) Minimal and liberalising state ( privatisation, de-regulation etc.)

These conditions are premised on a neo-liberal model of development, which argues that growth is the key to sustainable development. Barriers and distortions applied to the market inhibit growth and by implication lead to poverty. Proponents of this position argue for privatisation that excessive spending by the state and excessive participation of the state in economic activity lead to inefficiencies and market distortions. Poverty alleviation is best served by allowing market forces to operate.

At Monterrey, donors proposed a third condition be introduced. This was for a policy environment that was positively skewed towards poverty alleviation functioning within a set of institutions that allowed people to participate, and was minimally corrupt. A third conditionality around governance was introduced in its place.

- c) Participation and good governance by a minimally corrupt state

The application of the third 'conditionality' related to governance is perceived by many in the South to be positive. It includes elements of participation, accountability and transparency. The key issue about its effectiveness will be the extent to which it addresses itself to removing the structural barriers of the participation of the poor in the economy - will it prevent their

further exclusion. It could instead as has been seen in some countries become instead a set of measures to protect the interests of the status quo. In whose interests is the 'good' in good governance going to be defined and operationalised.

Originally introduced for Highly indebted Poor Countries in 1999, the PRSP is a framework that describes a country's macroeconomic, structural and social policies and programs to promote growth and reduce poverty, together with its external financing needs. In order to be eligible for loans, countries have to prepare this plan addressing all the conditionalities, in a process that is participative with wider civil society. It is thought that this would give countries 'ownership' over their plans.

### **The experience**

Theoretically, the PPA and PRSP processes could provide the right space and dynamics for genuinely participatory dialogue, diagnosis, strategy development and planning of anti-poverty programmes, involving all key stakeholders. However, evidence is now mounting that this has not been the case.

The major criticisms include:

- a) A UNCTAD notes that fundamentally the poverty reduction strategies are based on continuation of the liberalisation and structural adjustment agenda which the IFIs have been pursuing since the 1980s
- b) The main focus is still on market driven economic growth as key to poverty alleviation, with scant attention paid to both social and environmental impacts.
- c) Export diversification (as opposed to increasing export production) or food security as valuable development goals are mostly neglected<sup>4</sup>. Most PRSPs count on export-oriented agriculture to generate foreign exchange needed to service developing countries' debt burden.
- d) On trade, conditions forcing countries to open up their markets have continued under PRSP, and 'capacity building' provided by the World Bank further promotes the agenda of openness as an end in itself, rather than careful analysis of the kind of trade policy that is best for poverty reduction. In Ghana and Georgia, tariffs agreed by parliament were later removed in response to pressure from the IMF and Bank<sup>5</sup>
- e) Given the limited capacity of national governments in many countries, PRSPs are often 'written up' by WB/IMF staff; no wonder therefore that all the PRSPs effectively reflect official IMF and WB neo-liberal policy recommendations.
- f) Civil society organisations and parliamentarians are still unable to discuss, debate or put forward alternative macroeconomic policies in the context of discussion on PRSPs<sup>6</sup>.
- g) Oxfam, based on its involvement in over 30 countries in PRSP process, notes that despite the rhetoric on PRSPs being country-owned and participatory, the process is managed in a way that is hardly participatory. "Consultation is a more appropriate description than 'participation' in almost all cases", reports Oxfam<sup>7</sup>.

Where does this leave us?

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<sup>4</sup> The WDR 2003: A Strenuous Tale of Missed Opportunities; Liane Schalatek and Barbara Unmussig, Heinrich Ball Foundation (2002).

<sup>5</sup> *Ibid.*

<sup>6</sup> Arrested Participation: the failure of PRSP Process; Rick Rowden, ActonAid USA (December 2003)

<sup>7</sup> From 'Donorship' to Ownership? Oxfam Briefing Paper, January 2004.

There is a growing disagreement between Northern-based INGOs and CSOs on what the Monterrey consensus can and are achieving. Many southern NGOs believe that their Northern-based partners (INGOs, donors) have pushed them into participating in the PRSP and post-Monterrey process reflecting the existence of same dependency relationship in the NNGO-SNGO equation that characterises the official aid system. This same tension exists within NGOs (such as Actionaid?), where Northern and Southern perspectives are different.

The view from the donor community is also to some extent shifting. Most donors support the process of PRSP and the streamlining of conditionality that it allows but in the face of the evidence feel that the PRSP process still seems too supply led, too general and there is concern that the quality is variable.<sup>8</sup> Donor countries also differ in the extent to which they trust conditionalities to work - there is a growing set of countries including the UK and the Northern European states which are in favour of dropping conditions for countries where there is a positive policy environment, or where aid forms a small part of a country's GNP. It is unclear whether individual donor countries have used their influence of conditionalities not working within the IMF system but this position is unlikely to change.

Group	Position	Changes
<b>Fundamentalists, revolutionary</b>	<p>Aid as an entitlement transfer with no conditionality and aid recipients fully sovereign in how aid is used</p> <p>End to a system which allows the BWI's to determine the credit rating of all countries.</p> <p>Reparations to cover colonial and neo-colonial extraction and net transfers from south to north</p>	

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<sup>8</sup> Killick 2002, The streamlining of IMF conditionality: aspirations, reality and repercussions

<p><b>Ethical, politically active, transformational</b></p>	<p>Process should have national ownership of PRS (process not be perceived as anti-sovereign or undemocratic) , within framework of democratic plurality - allowing/ encouraging plans using a full menu of demand and supply side policies</p> <p>Conditionalities to be negotiated within a pro-poor framework - disagreements to be referred to independent arbiter. (e.g. anti-poor privatisations of health, education, water)</p> <p>The national development plan should be designed to address issues of institutional (laws and rights) , distributional (resource) and relational (gender, caste) exclusion to change the structural inequalities that cause a persistence of poverty. Should be rights based.</p> <p>Governance conditionality ( and priorities) to be re-oriented towards the perceptions of the poor rather than business and middle classes. (e.g. corrupting influence of the aid system, violence against women and inheritance laws for women labour laws, juvenile justice, reform of police powers, land reform etc)</p> <p>Aid to be seen as an entitlement and therefore additional costs of reaching poor in countries with 'bad' policy environments ( e.g. countries in conflict ) should be accepted by donors.</p> <p>Poverty and national development package should be process oriented ( reform of formal and informal institutions) as well as target led ( MDGs)</p>
<p><b>Rationalists, technocratic evolutionary school</b></p>	<p>Conditionalities can continue but need to be streamlined. Structural adjustment with a human face, increased spending on social services</p> <p>Capacity building of civil society in the South, to enable better and deeper participation in PRSPs and greater accountability through budget analysis. PRSPs should address gender and minority issues</p> <p>Increased pressure on donor governments and multi-laterals on coherence and coordination / harmonisation of policies.</p> <p>Increased pressure on donors for commitment on aid volume (0.7% of GNP)</p> <p>Aid to be untied and procurement policies changed to support local procurement.</p> <p>Selectivity criteria should be improved with a bias towards providing highest level of aid top poorest countries</p>

## 2. Trade for the rich , aid for the poor?

*What is the use of aid if other relationships between the North and South ( such as trade) impoverish the poor*

The stock and flows of funds to a country are not merely governed by aid and debt, but are to a much greater measure by other inward flows such as private capital flows, remittances and trade. The link between aid and trade is now well established. It is now widely accepted that if export earnings are high, sufficient investment goods can be imported and any domestic savings deficit can be alleviated. Trade therefore has a direct bearing on the aid and development strategy of a country.

Another of the conditionalities of aid imposed by the IMF and the World bank has been the removal of trade and investment barriers. The rationale for this derives from neo-liberal economic theory which recognises 'the importance of open trade regimes for sustainable growth, durable macroeconomic stabilization, and balance of payments viability.'<sup>9</sup> The IMF asserts that barriers to trade and investment only protect sectional interests and work against the interest of the consumers and the poor. In addition the IMF collaborates with the World bank and WTO to ensure that they are consistent in their trade policy and related advice.

At the behest of the BWIs, trade liberalisation, the removal of restriction on imports<sup>10</sup> and reduction of discrimination against exports has become a standard policy reform for most developing countries. Whether as part of structural adjustment or independently of it, most countries have embarked on a degree of such liberalisation. There is no doubt that given a choice dependence on trade is preferable to a dependence on aid, but openness of the economy trade and investment has obviously impacted most on fledgling industries and subsistence farmers.

The main question is the degree to which trade policy is coherent with Aid policy – i.e. is the impact of trade likely to compromise poverty alleviation goals. The key issues for debate are therefore centred around the terms of trade and the impact that these will have on the poor. NGOs and Southern governments have called for coherence in the policies on aid and trade on the grounds that there is no point in poverty alleviation measures that are directed towards poverty reduction, while simultaneously trade and investment measures only do the opposite.

As reported by the UN Secretary General to the General Assembly in 2002, *the developing countries transferred almost \$200 billion more to the developed world in debt service payments, profit remittances than they received from sources including aid, private investment and debt relief. Even if the developed countries met their ODA obligations of 0.7% of GNP, this would not be anywhere near the \$200 billion worth of resource transfer from developing to the developed world.*

### **The view from the South**

The potential benefits of trade liberalisation have escaped many countries, particularly in the sub-Saharan Africa which stand to be losers in the trade game, while many countries in Asia and Latin America have made some gains<sup>11</sup>.

Trade has not benefited most of the low income countries or the poor within the trading countries because of a variety of factors namely, unfavourable terms of trade and low relative prices of developing country exports, protectionism within the developed countries which discriminate against developing country exports, the world trade regime under the aegis of WTO being heavily controlled by the western business interests, heavily subsidised farm

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<sup>9</sup> Trade Policy Conditionality in Fund-Supported Programs, Prepared by the Policy Development and Review Department, February 16, 2001

<sup>10</sup> In theory of trade liberalisation, 'imports' mean import of investment goods. However in practice, this also means removal of all restrictions on imports, for example tariffs on imports of Gucci fashion wear and California Wine.

<sup>11</sup> "Foreign aid in the emerging global trade environment", Oliver Morrissey. Foreign Aid and Development, Routledge (2000).



sector exports in the Western Europe and America which goes against the developing countries' prospects for exports, etc.

a) It has been widely documented how the farm subsidies in US, Europe and Japan have devastated the economies of many African countries they assist with rural development programmes. According to the UNDP development report<sup>12</sup>, crop subsidies cost developing countries between \$125 billion and \$ 310 billion in lost sale and lower world prices. The 2003 World Development Report notes that unrestricted access to developed country markets in textiles and clothing alone could yield \$9 billion a year for the developing countries, and access to agricultural markets another \$ 11.6 billion a year.<sup>13</sup>

*The Reality of Aid Report (2002) criticises the global institutions for their double standards which force southern governments to privatise and liberalise, while the OECD restrictive practices, tariff and non-tariff barriers cost the developing countries over \$ 160 billion a year.*

b) Outside the aid arena, decisions that govern trade rules are negotiated multi-laterally within the WTO or in regional or bi-lateral agreements. The concern is that the negotiating strength of aid recipient countries can easily be compromised where donor countries have a position both as a competitor as well as a donor. In most donor countries aid departments still operate within or under foreign ministries.

On the trade agenda, the main grievances for the South were the disadvantageous terms of trade they had to suffer in agriculture, with patents, and as a result of barriers in market access for their products. The straw that broke the camel's back at Cancun was the inclusion of liberalisation of investment in the negotiation process. Although in this instance ( partly as a result of a common stance by India, China and Brazil) the South was able to stand up for their own interests, this is in no measure typical.

Within the wider context of international politics the conditionality on trade is not as benign or as poverty focussed as it is often portrayed. Trade and investment freedom as well as policies that limit national governments freedoms to subsidise or support their business interests are clearly in the interests of multi-national companies. Equally, it is in the interests of multi-nationals to have positive legislation in their favour- such as the legal freedoms investors enjoy within free trade areas. Conditionalities clearly favour the interests not just of the better resourced groups within a country, they also favour the interests of those who want to engage with a country – as a source of labour, knowledge, skills or commodities.

The most worrying part of this scenario is that the same institutions that have a role to play in giving loans and grants as part of aid (for example the IMF/WB and IADB) are heavily influenced by the OECD governments that are trying to negotiate these bi-lateral and regional agreements on trade and investment.

The Reality of Aid Report (2002) argues that broadening the scope and depth of donor conditionalities and tied aid “belie recent rhetoric favouring developing country ‘ownership’ of policies and strategies for reducing poverty”. Based on evidences submitted by 35 NGOs around the world, the report underlines the inseparability of aid volume from the need for institutional reform of the global aid and trade system – who control the systems determine what agenda is pursued and who benefits. *Without democratisation of the global institutional processes which give space to the developing countries' governments and civil society to be equal partners, poverty reduction strategies will continue to be another guise for conditionality and imposition of rich countries' agenda on the poor.*

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<sup>12</sup> “Africa pushes for better Aid Quality”. [www.nepad.org](http://www.nepad.org)

<sup>13</sup> Pathways to Sustainable future, World Development Report 2003, the World Bank.

As the Reality of Aid report asserts, if the entire aid-trade-financial system is not restructured, all the debates about aid and poverty will be “no more than an attempt to retool” the current aid-trade-debt regime based on highly unequal power relationships, under the garb of ownership and effectiveness, to serve the same ends as it has in the past.

**Where does this leave us?**

It has taken several months of ‘reflection’ particularly on the part of the EU to return to the negotiations that fell apart in Cancun. The G22 , which is a grouping of 22 developing countries have been awaiting the resumption of this process. Both the US and the EU have returned making statements that their positions have taken into account the need to address agricultural subsidy issues. The EU says that it is less ambitious about the investment and competition issues that they pursued in Cancun. They both are committed to strong trade liberalization and insist that it should be a two way process of give and take.

It is instructive that the coming together of an alliance has been able to play an important role in trade negotiations. Yet the IMF and World Bank continue to maintain conditionality as a matter of course in agreeing eligibility of loans.

One of the other processes that started immediately after Cancun was the shift towards OECD countries working to develop bi-lateral agreements on trade with countries who picked off one by one have little of the collective strength to be able to put up much resistance.

**Action aid work**

Actionaid has worked on the trade campaign as part of a wide alliance. It has also criticised the use of GM foods being used as food aid to Southern Africa.

Group	Position and approach
<b>Fundamentalists, revolutionary</b>	The relationship between the North and South is fundamentally exploitative. Aid policy is designed to make the terms of trade more favourable to the donor countries. Selection of which countries are given aid is determined more for political/ strategic reasons than any other.

<p><b>Ethical, politically active, transformational</b></p>	<p>Net flows are from the South to the North – rather than the other way around as a result of : Brain drain, capital flight, northern trade barriers, dumping of subsidised northern exports, and the repayment of debt.</p> <p>Policies governing these areas should have coherence with the poverty alleviation agenda. Instead trade negotiations have tied developing countries into unfair terms of trade causing greater harm to the poor.</p> <p>Money from remittances is more substantial than that from aid.</p> <p>No patents on seeds, food crops. Farmers should be free to sell exchange and save food and seeds.</p> <p>On investment: Joint ventures with local firms</p> <p>Rules to ensure that companies buy a certain percentage of their produce from local suppliers</p> <p>Companies made to retain a percentage of their profits in host countries.</p> <p>Protection of assets (e.g. land of the very poor)</p> <p>Multi-national should have a code of practice in which they are not able to distort local markets</p>
<p><b>Rationalists, technocratic evolutionary school</b></p>	<p>Investment decisions based on full consultation with local people. If local people are displaced through industry, proper compensation to be paid.</p>

### Relationship to MDGs

The failure at Cancun over developing country demands for the end of Northern farm subsidies, better market access and reform of inequitable trade policies would have an impact on achievement of MDGs.

### 3. Foreign policy or aid policy ? *Is aid an entitlement or about donor interest?*

It is important to understand a few historical facts about the evolution of aid in the post-war era. The Marshall plan was the first official aid in the modern period and to a large extent it inspired the development aid architecture that evolved in the 1950s. The Marshall plan achieved two things: (a) only a reconstructed/recovered Europe could salvage America's post-war stagnating economy by increasing the demands in Europe, and (b) established America's position in the comity of nations as the leader of the 'free' world.

Another important fact that stands out from the first fifty years of aid is that it has been guided predominantly by four considerations:

- (a) security (bulwark against the rising tide of communism in the cold war period);
- (b) foreign policy considerations based on donors' strategic interests which often propped up political and economic systems that are now some of the failed/failing

states, like Afghanistan, Iraq, DRC, parts of West Africa, Sudan and Somalia etc., for example<sup>14</sup>;

- (c) economic interests, primarily in opening new markets and developing captive suppliers of primary commodities; and
- (d) domestic special interests, e.g., the farmers lobby in the US and Western Europe which has been strong supporter of food aid, private contractor groups doing business<sup>15</sup> with foreign governments, etc.

Aid began the day Harry Truman announced to the world that 'there is a moral obligation to help the 'underdeveloped' parts of the world'. And that's the day when 'development' began, *circa* 1949. The notion of development that came with aid was seen as a linear process, a journey that America (and Western Europe, under the Marshall Plan) had already gone through, and the 'underdeveloped' countries would now follow the same route. And that is the dominant paradigm of 'development' and aid modern economic theories have espoused for, and most countries of the world have accepted, willy-nilly.

Aid and poverty reduction:

In the past, economic growth and macroeconomic stability were considered as overriding in the BWIs<sup>16</sup> approach to developing countries' economy. A clear link to poverty had always been lacking in the approach. In the late 1990s, following several impact studies which pointed out the inadequacy of progress made on poverty and related suffering, serious questions began to be raised as to the effectiveness of aid and the policy interventions by international donors in developing countries. The key for aid to work is a clear link to poverty and good policy environment as was established at Monterrey in March 2002. The PRSP and PPAs are attempts to correct this serious flaw.

All aid generally come as concessional<sup>17</sup> loans. Traditionally aid came in the form of isolated capital-intensive projects which often reflected donors' preferences. The donor allocations were kept outside the government budgets, which affected the recipient government's ability to make rational and strategic choices with regard to development policy or public expenditure.

A most significant progress in recent years worth noting is that some of the major donor agencies are moving towards programme support approach. The programme support approach is not aimed at financing a specific project, but at supporting the implementation of a wide-ranging policy/expenditure programme which incorporate a clear poverty focus, often for a sector or towards the overall budget of the government, laid down by a partner country's government. The funding becomes integral to the country's budget and development framework, and therefore requires new forms of cooperation. Despite this positive development on one side, *some bi-lateral donors are still hesitant in the provision of direct*

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<sup>14</sup> The US aid to a large degree went to prop up client states. In the 1980s, Somalia and Sudan received large amounts of US aid as a product of political alignments.

<sup>15</sup> Donor country contractors and suppliers lobby hard to be rewarded with contracts relating to aid projects. CIDA for example notes that 70% of its aid is spent in Canada (Raymond F Hopkins, "Political Economy of foreign aid" in *Foreign Aid and Development*). No clear figures for the US aid are available, but if one considers the way the contracts are being awarded to US-based companies in Iraq and Afghanistan alone, one wonders what proportion of the \$87 billion the Bush Administration has earmarked for these two countries would actually be spent in the recipient country. More than half of French aid is tied to domestic enterprises.

<sup>16</sup> Bretton Woods Institutions, namely, the World Bank, International Monetary Fund.

<sup>17</sup> Some bilaterals are now moving to more grant-based aid; DfID, the Dutch government and SIDA are some of the leading agencies in this regard.

*budget support preferring instead to promote their own political priorities.* This is notably the case for major donors like France, United States and Japan which account for nearly half of global ODA<sup>18</sup>.

#### Decreasing Aid Volume:

Currently global ODA per annum stands at \$56.9 billion (2001). However this figure (0.22%) is far behind the 0.7% of GNP 'aid' commitment that donors had promised to pledge towards development. Current research shows that ODA or 'aid' will have to double to about \$115 billion<sup>19</sup> per annum in order to realise the MDGs.

This dramatic increase, however, going by current and past trends, looks ambitious. The 1990s saw a decline in net disbursement of ODA as a ratio of donor GNP from 0.38 % in 1982 to 0.22 % in 1997. Since 1992 in particular, net aid disbursements from OECD have declined from \$62 billion to \$ 57 billion in 2001. This was partly due to the then widely held belief that operation of market will take care of everything and partly due to mounting evidence that aid was not making a significant impact on poverty, and is only causing dependency.

At the moment aid flows to LICs are nearly the lowest for over a decade, with aid per capita in 2000 being \$19 compared to \$33 in 1990. *Even now, almost half of the ODA goes to Middle Income Countries<sup>20</sup>, while aid flows to low income countries have only increased at about 1.5 % per annum between 1998 and 2001.*

The quantity of aid intended for disaster relief and emergency aid<sup>21</sup> has more than trebled in the last decade (before the occupation of Afghanistan and Iraq, it was \$6 billion per year). This has led many NGOs to examine their portfolio of development and relief work.

Though aid is also provided through civil society intermediaries (NGOs), bilateral agencies and multilateral institutions are responsible for the bulk of ODA. *In 2001 multilateral institutions<sup>22</sup> were responsible for roughly 33% or \$23 billion approximately of all ODA.* The major bilateral donors together disburse about 64% of the aid. Around 3% of ODA is disbursed through NGOs of which the largest are CARE, OXFAM, Save the Children Fund and the Red Cross/Red Crescent Society.

#### Where does this leave us?

On signing up to the Monterrey consensus donors also signed up to a number of issues to do with increasing the effectiveness and quality of aid. Donor commitments made at the 2000 Millennium summit and the 2002 Monterrey conference include:

- Increasing the amount of ODA available for achieving the MDGs;

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<sup>18</sup> Debt and Millennium Development Goals, Working Paper by CAFOD, Eurodad, Christian Aid, Oxfam and Jubilee Research (September 2003).

<sup>19</sup> This relates to development aid only. Another \$ 9 billion is expected to be required every year for emergency aid.

<sup>20</sup> This is likely to continue and intensify further, with the expansion of the EU to include ten new MIC members who are likely to continue to be recipients of aid for the foreseeable future.

<sup>21</sup> Humanitarian Aid is not included in this discussion as it is governed by a separate process within each donor country, although it may be argued that major allocation to humanitarian aid (like the Bush Administration's allocations for Iraq and Afghanistan) would affect the development aid, although the governments do not usually admit it

<sup>22</sup> The major multilateral institutions are the World Bank, the IMF, the Asian Development Bank, the African Development Bank, the Inter-American Development Bank, the Caribbean Development Bank and the UN.

- Achieving better alignment of donor priorities with national development strategies;
- Reducing duplication and reporting requirements;
- Improving predictability and timeliness and aid disbursements;
- Strengthening ownership and untying of aid. These included the very ambitious goals of taking development spending up to 0.7% of national GNPs, a commitment to untie aid, to a greater degree of coordination and harmonization.

On all these counts there has been some but not much movement. Aid volumes have gone up and there is a promise of this going up even more if the International Financing Facility proposed by the UK is supported by the rest of the donor community. Equally some countries are making progress, as has the UK on untying aid and de-concentration. On the other hand there are a few other issues that have arisen. The first is the use of aid to deal with public goods. Public goods include issues such as security, pollution and diseases for which there is international as opposed to national costs and benefits. Public goods are effectively being funded through aid resource flows. Equally, especially in the EU, aid is increasingly being used as a preventative instrument for migration.

But perhaps the biggest potential change to the aid environment comes not from specific issues to do with the aid architecture, as it stands at the moment, but with the general shift in global concerns. With the September 11<sup>th</sup> bombings, Afghanistan and Iraq, as illustrative examples, a new constellation of concerns are likely to influence the objectives of aid. The 4 key issues that form this are – security, foreign policy, terrorism and aid. It is too early to say how poverty focus will remain as an overall commitment in future aid decisions, or whether a new cold war type, foreign policy led aid will develop, but new initiatives such as the MCA suggest that a selectivity in aid provision is definitely on the cards. Within the South there has been a call for selectivity to be based on independent ratings of a composite of poverty, structural vulnerability, and good policies of recipient governments, but whether this will be accepted is doubtful.

In many ways the crux of the issue is to do with the manner in which aid is viewed. Is aid an entitlement? The idea that humanitarian aid is an entitlement and is neutral is a well accepted principle. Although basic rights are playing an increasing role in development thinking, the idea that aid is an entitlement is not really considered by the donors. It would do much to re-orient the system to buy into long-term aid rather than the current position where countries are expected to sign up to decade long programmes yet have to be content with having aid allocation decided annually.

### **Actionaid work**

ActionAid work particularly in the North has focused on aid effectiveness and there has been some interactive processes with AA country programmes working on the issue in the South.

### **Relevance to MDGs**

It is estimated that another \$50 billion dollars in annual aid will be needed if the MDGs are to be achieved by 2015, although there is a large scepticism on the part of both bi-lateral and multi-lateral donors as to whether there is the capacity to absorb such large amounts of money.

But it is the issue of selectivity will be crucial in influencing the achievement of MDGs. Donors are more disposed to support the countries where there is a positive policy environment and where there is some demonstrable impact, even in the short-term. For countries, such as those in conflict or recovering from conflict, none of these conditions

apply. In these countries the costs of achieving the MDGs will necessarily be higher. It is not clear however if donors are willing to bear these.

#### 4. How to deal with the debt problem

The debt burden of the poorest and heavily indebted countries has a direct bearing on the domestic development policy and public expenditure. The developing countries as a whole have been contributing \$190.000 a minute to debt service, while the poorest of the poor in Sub-Saharan Africa have paid back an average of \$20.000 in interest payments every minute. 'You can build a good many schools and clinics and water-mains and roads for \$20.000 a minute', says the noted activist, Susan George<sup>23</sup>.

The HIPC initiative<sup>24</sup> has not led to any significant change in the debt landscape. In the first four years of the initiative, only 2 (Bolivia and Uganda) of the 41 HIPC countries had reached the last stage of approval, and five others were in the first stage of consideration. By the end of 2001, only 24 countries had reached the decision point with regard to debt relief. In a study on effectiveness of debt relief conducted by the Dutch Government<sup>25</sup>, it was found that even after five years of so-called debt relief, the debt stock has reduced only by 1-4 per cent annually for 6 HIPC countries (Nicaragua, Bolivia, Mozambique, Tanzania, Uganda, Zambia) studied. The study found that instead of any permanent relief, the stocks of debt have remained largely the same or have increased. The study concludes that debt is not sustainable for any country.

Several debates have been raised by the debt question.

- a) Intention - Write off's or restructuring?: Should debt be completely written off, therefore giving seriously indebted nations a clean slate from which to start, rather than continue with the same re-structuring which in effect does not reduce the debt stock.
- b) Accountability and Moral Hazard: The IMF funds are replenished every 3 years by the major OECD donors. This gives IMF the ability to lend to recipient countries, sometimes not very responsibly. Where is the accountability? Is the IMF in a position of moral hazard?
- c) Is debt relief actually having any impact on poverty: Debt relief is generally financed from the aid budget of the donor, which means that for the recipient country it has a negative effect on the overall budget.
- d) Is debt relief distorting the aid giving in favour of countries that are not in debt: Another serious complication of the aid vs. debt debate is that it has the effect of distorting the aid, focussing more on countries that do not manage their aid repayments and against those that have managed to make repayments.

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<sup>23</sup> Cooperation - A third Way with a third force, Susan George, Ottawa, November 1999 (www.tni.org)

<sup>24</sup> Highly Indebted Poor Countries initiative: started in 1996, whereby the rich countries and the IFIs committed themselves to provide partial debt cancellation and debt restructuring to ensure 'lasting exit' from unsustainable debt burdens for 42 countries. In 1999, the HIPC initiative was 'enhanced' to deliver 'permanent exit' from debt rescheduling and to release resources for higher social spending in debtor countries.

<sup>25</sup> Results of International Debt Relief (2003), IOB Evaluation, Netherlands Ministry of Foreign Affairs, NR 292

- e) Should debts be replaced by grants for some countries: should the giving of loans be stopped to countries where debt has been unsustainable – and should it only be paid as grants?
- f) Is HIPC just adding more conditionalities when there is a case to remove them all.

Crucially, recent evidence from a number of studies has shown that for the countries that have satisfied the conditions for debt relief, there has been no additionality in terms of funds. What this means is despite the relief neither the stock of debt nor the flow of funds as repayments has increased. What was sold as debt relief is in fact a re-structuring of debt. This promises to get worse as new loans are being given to countries for whom old loans are being written off.

### Where does this leave us?

The HIPC countries were singled out for special treatment as they were carrying unsustainable debt burdens. Instead of their debts being written off as politically proclaimed these debts were re-structured if they could satisfy several conditions. Even despite writing off debt, if the stock and flow of debt has not decreased, something is wrong.

The fact that this initiative seems to be have hit a dead end is highlighted by the recent move by the US to block the debt cancellation of Ethiopia because "increased debt relief would just be an excuse for more borrowing."

An alternative approach is being suggested by Jubilee 2000 which suggests the introduction of a (need based) international insolvency tribunal that could function as an independent arbiter between the debtors and the creditors. This may be bale to bring some degree of accountability into the situation where IFIs do not need to take responsibility for lending , causing a cycle of bankrupt indebtedness to continue.

Action aid work: NOT SURE

Group	Position and approach
<b>Fundamentalists, revolutionary</b>	Debt is the major outcome of foreign aid and has had the effect of breaking down sovereignty and the emergence of public democratic control over the economy.
<b>Ethical, politically active, transformational</b>	<p>The HIPC initiative which has been a failure should be replaced with cancellation of unsustainable debts from poorest countries . This should be financed by additional resources.</p> <p>An independent system of international insolvency should be introduced to arbitrate between creditors and debtors to see which party was wrong in allowing the debt in HIPC's to occur.</p> <p>There should be an end to the link between conditionality and debt relief.</p> <p>A lower loan component – grants only to the poorest countries.</p> <p>Countries should not take automatically convert export credits to debt. These should be taken off the books.</p>



<b>Rationalists, technocratic evolutionary school</b>	Replacement of debt by grants
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MDGs: This is a crucial question for the attainment of MDGs as the HIPC countries also exhibit some of the worst figures in terms of MDG targets.

### 5. How do you make the institutional form of the aid system effective, efficient, and accountable?

The debates around Monterrey, as well as those around the trade agreements and debt relief point to the importance of the institutional arrangements for both arbitrating between these competing perspectives and in taking the system forward.

The Reality of Aid Report (2002) argues that broadening the scope and depth of donor conditionalities and tied aid “believe recent rhetoric favouring developing country ‘ownership’ of policies and strategies for reducing poverty”. Based on evidences submitted by 35 NGOs around the world, the report underlines the inseparability of aid volume from the need for institutional reform of the global aid and trade system – who control the systems determine what agenda is pursued and who benefits. *Without democratisation of the global institutional processes which give space to the developing countries’ governments and civil society to be equal partners, poverty reduction strategies will continue to be another guise for conditionality and imposition of rich countries’ agenda on the poor.*

As the Reality of Aid report asserts, if the entire aid-trade-financial system is not restructured, all the debates about aid and poverty will be “no more than an attempt to retool” the current aid-trade-debt regime based on highly unequal power relationships, under the garb of ownership and effectiveness, to serve the same ends as it has in the past.

#### Doubts over effectiveness of aid

In the context of Africa, an AFRODAD research<sup>26</sup> notes that aid has benefited only about 10% of the population who are mostly the local elites. In countries such as Tanzania and Zambia, says AFRODAD, the failure of aid to address developmental problems has led to calls for more aid!

*Worldwide 54 countries are poorer now than they were a decade ago<sup>27</sup>. A series of impact assessments by the aid agencies in early 1990s also concluded that aid was only having a limited impact on reducing poverty and suffering – although at times aid was extremely successful, most of the times, there were extreme failures. In 1990/91, on an average, an additional \$1 million worth of aid pulled just over 100 people from poverty. However, the comparable figure for 1999/2000 was 284, signifying a growing ‘relative effectiveness’ of aid.*

Success stories of aid are generally to be found in the realm of humanitarian action or in situations of severe suffering where lack of aid would have made things far worse. The success rate is for developmental programme however is positive only if one absolves aid of

<sup>26</sup> *Ibid*

<sup>27</sup> Shriti Vadera, Council of Advisers, HM Treasury, speaking at The Future of Aid seminar series, ODI, 29 January 2004.

any responsibility for consequences on people and environment. Myriad infrastructure development (roads, power sector, etc) and 'prestige projects' vie for attention and awe in most aid receiving countries, courtesy of the international aid pushers. The cumulative debt burden which the developing countries are now reeling from can be traced to these mega-projects and the investment that went into propping up regimes like those of Marcos, Moi and Mobuto to mention only a few.

Some of the key questions raised as a result of dissatisfactions with the system from both northern and Southern perspectives include:

1. Does the WB/IMF agenda undermine national policy-making?:

A central question being asked in the past few years is whether aid architecture is interfering with the ability of country governments to decide on their priorities? This question is increasingly being asked as despite the importance given to country ownership of the PRSPs, it is clear from several studies that in Africa, Asia and Latin America that this has not happened. In Pakistan for example, elements across civil society formally got together to reject the 'structure, content and process' of the PRSP<sup>28</sup>. It is suggested by many southern NGOs that countries were in fact pressurized into taking on reform agendas which did not derive from domestic political and social factors. As a result there was no commitment or capacity to go through with these reforms. Instead they have in several cases led to tussles between civil society groups, national governments and national parliaments (Global south).

2. Is the aid architecture just overgrown, too expensive and unwieldy ?

Both the World Bank and the IMF have adopted multiple and conflicting roles. The Bank for example has appropriated for itself multiple roles a) as a bank, b) to advance the interests of its shareholders – largely OECD countries, c) trying to change southern countries policies and beliefs, and d) as an agent for the net transfer from OECD to developing countries. Not to be left far behind, the IMF plays multiple roles as arbiter of debt, or trade and investment liberalisation when these are not part of its central mandate or core expertise. In the case of debt, or conditionality there are multiple institutions, the WB, the IMF, and interested donors who need to be consulted to make a decision. Yet there is no overall body that has an overview of the conditions that multiple donors may have made, nor whether there was any consistency between them.

The international aid system suffers from multiplicity of actors – there are some 75 agencies (40 bi-lateral, 20 multi-lateral and about 15 UN agencies) – through which bulk of the ODA aid of \$ 58 billion were disbursed in 2002<sup>29</sup>. Moreover the relationship between various institutions is unclear. Although there is an accepted need for multi-lateralism, there still is a large amount of bilateral aid (in countries) such as Mozambique as high as 80%, where donors continue to follow their own agendas. Within all this the ideas of coherence and coordination are extremely difficult. New forms of tied aid was posing serious problem for the aid system, and the future of multi-lateralism was under threat<sup>30</sup>. Despite Monterrey consensus, not much has changed on the ground in terms of donor practices and procedures. The US government for example have in the past two years come up with new funds like the Millennium Challenge Account, the HIV/AIDS Fund which, though are welcome in terms of the extra funds being committed, are causing obstacles in the way of coming up with a globally coherent architecture.

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<sup>28</sup> Source: Focus on the Global South

<sup>29</sup> Andrew Rogerson, ODI (January 2004): Presentation at The Future of Aid seminar series, ODI, 14 January 2004.

<sup>30</sup> Andrew Rogerson, ODI, The Future of Aid Seminar, 14 January, 2004, ODI, London

There is a general agreement that both in the case of donors, as well as in the case of the multilateral institutions there should be a fundamental remodelling of the system to make it more accountable, transparent democratic and results oriented.

### 3. Lack of Accountability in the aid system:

The call for greater accountability is universal both from the donor countries who have to justify expenditure to their public and from the South because the people bear the brunt of the policies and programmes. At present accountability exists in a narrow instrumental sense - there are budget audits, parliamentary committees and the peer-review process.

Currently there is no mechanism for joint assessment of aid programmes. While the World Bank, IMF and other donors keep themselves busy commenting on how the aid receiving governments are doing, there is no space for reviewing by the governments and civil society how the international aid agencies are performing in relation to their professed commitment to the principles behind MDGs. There is a general agreement that both in the case of donors, as well as in the case of the multilateral institutions there should be a fundamental remodelling of the system to make it more accountable, transparent democratic and results oriented.

This is becoming vitally important now, more than ever before, that donor governments take responsibility for bad policy advice, failed assessments and faulty programmes. Otherwise, it is more likely that continued failure of PRSPs in alleviating poverty will be attributed to weak capacity, poor governance and entrenched structural weaknesses in recipient countries.

### 4. 'Selectivity' in aid allocations:

The criterion of a 'good policy' context is becoming popular with aid agencies for aid allocations as it is argued that good policy environment leads to higher growth rates which in turn lead to alleviating poverty and improving mortality rates<sup>31</sup>. In 2002, President Bush announced the setting up of Millennium Challenge Account which would increase the US development assistance by \$5 billion annually by the year 2006 for countries "ruling justly, investing in their people and encouraging economic freedom". The announcement also emphasised that foreign assistance is governed by security imperatives of the US. Through the MCA, US will focus on strategically important states, and not necessarily the poorest nations or the failed states<sup>32</sup>. While 'good policy' contexts are certainly a pre-requisite for poverty reduction, civil society groups need to challenge the emerging institutional consensus on 'selectivity' if it runs the likely danger of 'forgetting' the poor in the non-good policy contexts.

### **Where does this leave us?**

Partly on the back of the review of the MDGs in 2005, and new leadership mandates for the WB and IMF which are up for renewal in 2005, there is an opportunity for real change within the aid architecture. It is unclear what role INGOs can on their own play in this, but there is a real opportunity to work with Northern and Southern governments to lobby for changes to the system that focus on some of the key issues raised above.

The crux of the problem is that the South doesn't have a sufficient voice in participating and influencing these debates. As a result the structures, the processes and the patronage ties within the system allow the system to be unaccountable. There is a space to change this if

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<sup>31</sup> Collier, P., Dollar, D. (1999). Aid Allocation and Poverty Reduction, Policy Research Working Papers, World Bank.

<sup>32</sup> "Emerging Trends – An InterAction Policy Paper". InterAction (November, 2003).

political backing is built on alternative structures. It is key that a platform that bridges the North-South divide on these issues is developed.

### **What role for Actionaid?**

Action aid has not as yet developed a coherent position on aid. This is partly due to institutional reasons ( such as other priorities, no direct resourcing, no structure or lead etc. ) but also because it is difficult to find coherence across a programme where every country has a slightly different experience of aid.

There is also probably not a natural agreement on the ideological or political position that Actionaid should take on aid. Partly again this is because of the moving nature of the debate. Partly to do with the fact that the aid systems provides for different opportunities and responses.

In the North, it has been perfectly reasonable to concentrate on lobbying for aid effectiveness as AA has close links with DFID and has alliances with others in the same field. It has also proved to be effective, as campaigns on aid untying and aid volumes, have had demonstrable impacts. This will not however be the same starting point for a country like Bangladesh. Historically AA has operated within a rational, technocratic framework in north & within a politically active, transformational framework in south.

Yet, Actionaid is in a sense in a unique position to deal with this challenge, if it can capture the energy of the reversals its organisations are going through at the moment. It has a long and admired tradition in the North, as well as a strong tradition of supporting the poor in the South. It has followed through with its conviction that people in the South know what is good for them by 'handing over the stick'. If it can do it for itself, it can also lead the way in showing that similar reversals can be made in the aid system .

Actionaid needs to build on the traditions and achievements in both spheres. It needs to build on the way it has achieved change in the North as well as ways in which it has achieved change in the South. By doing this it would be able to give people in the South what they don't have - voice. It should be in a position to help people in the South move from the current position recipient position that they have to one in which they can choose the kind of aid that they require. Actionaid can make a real difference if it were to conceive a strategy that is political and transformative. There are variety of reasons why this is the appropriate action in the present situation.

1. The opportunities and threats in the aid system have never been greater and the opportunities to review the system have never been so good.
2. The moral advantage that AA has in making the reversal to be a Southern headquartered and led organisation.
3. The huge number of gaps in strategies and alternatives to deal with the problems that have confounded the aid system, will make it easy to take a lead in this area.

There are also gaps that AA will have to fulfil before it can and during the process of undertaking this kind of work.