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**ECONOMIC DEVELOPMENT IN AFRICA**

**DOUBLING AID: MAKING THE “BIG PUSH” WORK\***

Overview by the UNCTAD secretariat\*\*

**Executive summary**

The current commitments to double the amount of aid to Africa by 2015 and the recent economic performance of the continent (in large measure thanks to increased demand for commodities in emerging economies) have raised hopes that Africa can sustain this growth performance as a basis for meeting the Millennium Development Goals. Yet concerns remain with respect to the effectiveness of aid, the absorptive capacities of recipients, and whether aid can raise growth and help reduce poverty. This year’s report on Economic Development in Africa will address these issues. It argues that while a “big push” designed to instigate a virtuous circle of higher investment, income and savings is necessary for poverty reduction, policies by aid donors and recipients alike are crucial for its success. The impact of aid cannot be separated from national policy autonomy nor from the quality of aid. Based on past successful aid experiences, it argues for a new aid architecture with a much larger multilateral component in order to deal with the present “chaotic” state of aid system, which suffers from high transaction costs, politicization, lack of transparency, incoherence, unpredictability, and too much demand on weak institutions of recipient.

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\* The information in this document should not be quoted by the press before 21 September 2006. It should be read in conjunction with UNCTAD/GDS/AFRICA/2006/1.

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1. After two decades of adjustment without growth, there are, at last, some real signs of improving economic performance in Africa. Not only has growth steadily accelerated since the turn of the century, but new trade and investment opportunities, particularly arising from increasing demand in emerging markets such as China and India, hold out hope that this time around it might be sustained. Ongoing efforts at macroeconomic and political reform have been consolidated in many countries, and the launch of the New Partnership for Africa's Development (NEPAD) signalled a willingness on the part of African leaders to confront past mistakes but also to be held accountable for their side of the development bargain. Real progress has also been recorded at the international level on issues such as debt relief and public health and education, which will have a direct bearing on poverty reduction prospects. Perhaps most encouraging of all, the international community, after retreating in the 1990s, has recovered its faith in official development assistance (ODA), with a promise to double aid to Africa by 2015. With the Cold War a fading memory, hopes are high that this aid will not be distorted by political calculations.

2. However, it would be unwise to lose sight of the magnitude of the challenge. The continent is already behind on meeting the Millennium Development Goals (MDGs) and getting back on track implies, on some estimates, sustained growth of 8 per cent annually for the next decade, well above this year's expected growth of gross domestic product (GDP) of over 5.5 per cent for the continent as a whole. Although high energy and mineral prices have brought large gains to some African countries, increasing average growth rates, so far there has been little impact in terms of reducing poverty and inequality and raising employment. Industrial development remains subdued, at best, while at the same time policy makers in a growing number of countries are having to confront a whole new series of challenges linked to a rapidly expanding urban population.

3. It is also the case that fresh starts for the continent are nothing new. In the late 1970s, when the region was already exhibiting clear signs of economic slowdown, the Organization of African Unity produced the Lagos Plan of Action, a far-reaching reassessment of Africa's links to the global economy. It put the responsibility for the continent's problems, and for finding solutions to them, firmly on the shoulders of African policy makers. The proposed reform agenda, however, was sunk by the combined forces of global economic slowdown and declining commodity prices, leading to a severe debt crisis which engulfed the entire region in the early 1980s. Struggling under severe balance of payments constraints and under considerable pressure from the international financial institutions, aid and loans were extended on condition that countries adopt structural adjustment programmes that would supposedly enable their economies to withstand and benefit from the competitive pressures of a global economy. Instead, the steady worsening of poverty and human development indicators across Africa has forced a rethink by the international community.

4. With the current proposals to double aid, the credibility of both donors and recipients has been pinned on forming genuine partnerships to "make poverty history" with the MDGs providing a clear reference point and time frame for judging progress. However, there are already signs of slippage. Civil society groups have raised some awkward questions about the inclusion of debt relief as part of the promised increase in aid, about the real volume of aid actually received and about the concentration of flows on a relatively small number of countries. There are also very clear signals that security concerns and energy politics are again shaping the policy debates on aid and development; another scramble for African resources, however, is no more likely to generate a successful development path than in the past. There are, most worryingly of all, growing concerns about the effectiveness of NEPAD

as a reliable development framework, along with persistent worries about whether African elites are willing to forsake short-term rent-seeking behaviour for longer-term commitments to productive investments. It would be a mistake for governments to treat these concerns lightly, lest the seriousness of their commitment be questioned by the public in both the donor and receiving countries. All deserve more careful thought and immediate attention in order to highlight the urgency of fully exploiting the current mood of optimism in order to avoid any resurgence of bearish attitudes towards aid.

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5. Six years ago, UNCTAD called for a doubling of aid to Africa, a call subsequently picked up and amplified by the High-level Panel on Financing for Development, the Monterrey Consensus, the Practical Plan to Achieve the Millennium Development Goals (the “Sachs Report”), the Report of the Commission for Africa, set up by the British Prime Minister Tony Blair, and the World Summit. New life has been breathed into the aid target of 0.7 per cent of developed countries’ gross national income (initially recommended by UNCTAD and subsequently adopted by the United Nations) with some major donors agreeing a timetable for its achievement. Of course, even if aid were to reach these levels, there can be little doubt that a secure economic future for Africa will hinge on the effective mobilization and investment of domestic resources. In the coming years, the debates about development finance will revolve around the search for a successful blend of resources from various sources, strengthening institutional capacity and improving policy coherence.

6. While a “big push” designed to instigate a virtuous circle of higher rates of savings, investment and economic growth is necessary for a permanent reduction in poverty, the quality of both the aid supplied by donors and the policies pursued by recipients are critical factors for success and for eventually ending the need for aid. The impact of ODA, however, as UNCTAD earlier insisted, cannot be separated from the wider issue of choosing an appropriate development strategy to realize the annual growth rates estimated to be necessary for meeting the MDGs in Africa. On any objective assessment of two and a half decades of standardized packages of “stabilization, liberalization and privatization”, the right kind of growth path has simply failed to materialize across most of the continent.

7. This is all the more reason to forge a new consensus on ODA. Moving ahead is certainly not helped by the tendency to polarize the aid debate, in which sceptics continue to return to a series of basic issues, such as promoting market principles in the raising and delivery of funds, questioning the absorptive capacity of recipients, and raising issues of incentive distortion, including those associated with “Dutch Disease” and fungibility problems. Some of these concerns are legitimate, but analysis and empirical evidence provided by academics, non-governmental organizations (NGOs) and the international community, while not conclusive, suggest that they are often exaggerated. A case in point is the risk of Dutch Disease, which is less a matter of insurmountable constraints on absorptive capacity and more a question of effective macroeconomic management of aid and designing development strategies tailored to local conditions. This was the conclusion of the African Ministers of Finance Conference on Financing for Development meeting this year in Abuja, based on discussions that included experts from the multilateral financial institutions.

8. Many useful lessons can be drawn from the history of aid in designing contemporary strategies that aim to advance its developmental impact. Both positive and negative outcomes need to be analyzed in their proper context and taking into account the many variables – economic, social and political – which might help to explain the causes of the

various examples of success and failure. It is certainly in the interests of donors and recipients alike to undertake an unbiased assessment of past policies, identifying their shortcomings and making changes to ensure that the promised increase in aid will have a positive influence on growth, development, and the reduction of poverty.

9. In 1947, Senator Dirksen famously dubbed the Marshall Plan as “Operation Rat-Hole”, into which the United States taxpayers’ money would disappear with little prospect of returns to the donor. He was proved spectacularly wrong and the Marshall Plan still stands as perhaps the most successful aid exercise in history. This report still sees valuable lessons in this experience. But it is not an isolated case. Ireland and Portugal received massive amounts of aid following their membership of the European Economic Community (EEC): transfers reaching as much as 5 percent of their respective GDPs and continuing for a decade or more were comparable in scale to Marshall Aid. Europe, however, is not the only part of the world where there have been success stories with aid. The East Asian miracle economies, notably the Republic of Korea and Taiwan Province of China, received enormous amounts of aid during the initial and early stages of their development, the assistance lasting well into the 1960s. In Africa, both Botswana and Mauritius received very large amounts of aid at key strategic moments in their development as, earlier, did Tunisia. These examples show that large amounts of well-targeted aid have produced some remarkable success stories in terms of growth and overall development. Aid directed at specific problems has also often proved to be highly effective: health programmes for example, have significantly reduced infant and under-five mortality rates, eliminated river blindness, and put an end to smallpox.

10. Despite all this, however, the sceptics remain prominent, if no longer dominant, in public debates about aid. Africa is often held up as a prime example of wasted aid. This view is usually buttressed by reference to econometric evidence that takes little or no account of structural deficiencies, policy constraints, and the inefficiencies of the aid donors themselves, including the quality of aid, its quantity, unpredictability, political instrumentality and, indeed, its very definition. In short, scepticism about the value of aid rests to a large degree on selective economic reasoning and questionable interpretation of economic history.

11. One reason why aid has not always succeeded in accelerating growth and development is that these have not always been among its objectives. But, as spelt out in past UNCTAD reports on Africa, even when they have, as with adjustment programmes, the links have been poorly thought through, have failed to accommodate local conditions, and all too often have been guided by a search for quick economic fixes.

12. Another major source of the inefficiency and ineffectiveness of much aid is the lack of coherence among donors and their objectives and requirements, and a failure to reconcile these with the needs, priorities and preferences of the countries receiving assistance. The sheer multiplicity of donors, with different outlooks, accounting systems and priorities have created a landscape of aid that, at best, can only be described as chaotic. This has in turn stretched the administrative capacities of the recipient countries to breaking point and undermined any pretence of local ownership of development programmes. The institutional capacities of the receiving countries have been further weakened by the pressures to reduce the size and functions of the state, a prominent feature of the adjustment programmes driven by international finance institutions. The situation is exacerbated by the presence of numerous new bodies such as NGOs through which aid is often disbursed with little or no oversight by the recipient government or other national institutions. Coping with such a

situation would stretch the abilities of the bureaucracies of the Organisation for Economic Cooperation and Development countries, let alone those of poor African states.

13. The sectoral distribution of aid is also greatly influenced by donors' preferences and the different criteria applied by them. With increasing attention by the international community being given to poverty indicators, there has been a major shift in the allocation of aid from infrastructure, agricultural development and energy supply to social expenditure. This is an issue that African Ministers of Finance have raised on several occasions. Their concerns are centered on whether such expenditure can be sustained in the absence of growth-oriented, productive investment. In implementing the proposed increase in aid, both its growth-enhancing and social development goals will need to be carefully balanced in order to ensure that higher rates of economic growth can be sustained in order to reduce aid dependency in the longer-term and ensure that the reductions in poverty are irreversible.

14. Recent initiatives such as the 2005 Paris Declaration on Aid Effectiveness are *ipso facto* recognition of the serious shortcomings in the way that the international aid system has been operating. The recommendations of the Declaration can indeed be helpful in raising the quality and effectiveness of aid. Nevertheless, if donors' recognition of the need for greater local ownership of aid programmes is to be taken at face value, the de-politicization of aid, greater policy space for the recipients of aid and less intrusive policy conditions are all prerequisites for ensuring that aid results in more positive outcomes. In order to attain these objectives, there needs to be a greater multilateralization of aid so that the distorting influence of individual donor preferences is reduced. Such a shift in the balance of bilateral and multilateral aid should also help to simplify delivery by providing greater coherence, transparency and accountability; transaction costs should be lowered, the predictability of disbursement greatly improved and the demands on recipient institutions considerably reduced.

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15. A greater multilateralization of aid can help to reduce unnecessary and costly competition (and associated fragmentation) among donors, and thus greatly reduce administrative costs. It can also provide a buttress against the politicization of aid which has been so damaging in the past. But there also needs to be reform of the existing multilateral institutions that currently provide aid on condition that the recipient country adopts policies acceptable to (and usually formulated by) the international financial institutions. The nature of the current Poverty Reduction Strategy Paper process does not lend itself to the longer-term planning that will be required if a doubling of aid is to be employed to maximum effect. The time is perhaps right to revisit the idea, first broached in the mid-1950s, of a UN funding window for African development.

16. A new international architecture for aid must ensure, first and foremost, that it is used to encourage and supplement national resource mobilization and to fill the gap between national rates of saving and the rates of investment required to meet national development goals, including the MDGs. There is now greater recognition of the need for aid to be increasingly used for budget support, thus implying that it should be seen as part of a comprehensive fiscal and financing package for the implementation of national programmes and priorities and, as such, that it should be subject to parliamentary oversight and scrutiny in the recipient countries. Such a process will reinforce both the ownership of national programmes and the accountability of governments to their national constituencies rather than to foreign donors or multilateral financial institutions. This is one way in which the

organization of aid can help to reinforce democratic processes, strengthen the rule of law and reduce the possibility of aid being captured by corrupt elites, all of which are among the declared aims of donors and recipients alike. A shift to budgetary support does not necessarily imply the abandonment of project support and technical assistance, but they should only be provided in response to express demands from recipients to fill specific institutional lacunae. In particular, post-conflict situations may often require a combination and sequencing of different delivery techniques in order to begin the reconstruction of state and institutional capacities, as will cases where the local elites have a record of capturing the rents arising from aid rather than investing in productive capacity.

17. Recalling one of the most successful aid programmes of the past, both the British Prime Minister and his Chancellor of the Exchequer have called for a Marshall Plan for Africa. Although the problems of reconstruction in post-war Europe were very different from the problems of development facing Africa today, the differences should not be allowed to obscure the fact that many of the features of the Marshall Plan that helped to make it a success point to useful lessons that can inform the creation of a new aid architecture. These include recognition that shock therapy was neither politically or economically feasible in engineering a return to a system of free trade and payments and dismantling the apparatus of state control that had developed over the course of nearly a decade; that piecemeal approaches to aid had not stimulated recovery and that a more coordinated approach was required with each beneficiary state drawing up a four-year plan for recovery; that such plans should be drawn up by the countries themselves without outside interference; that aid would be released in tranches dependent on intermediate targets being met; that conditionality was essential, but it had to be applied in a more flexible manner and over a much longer time-horizon than was possible under International Monetary Fund rules; that trade liberalization would be gradual and asymmetric, with the US providing greater market access more rapidly than the Europeans; that the aid package was generous with a large grant element; and that the European countries were expected to cooperate among themselves and the aid programme was to be coordinated in a regional body.

18. The Marshall Plan recognized that investing in structural change required providing the recipient countries with sufficient breathing space and flexibility to bring often difficult and painful policies to fruition. This report does not pretend that the Marshall Plan can be replicated in detail for Africa, but there is no doubt that the processes and organizing principles that governed the Plan suggest a much better and more coherent model than is currently available for addressing many of the problems and issues surrounding aid delivery and impact. In particular, by requiring the potential recipients of aid to produce coherent development plans, indicating how and where they would use aid to achieve their objectives in a given time-frame would help to eliminate much of the present chaos surrounding aid delivery. Also, by subjecting the coherence and feasibility of such plans to peer review and coordination in a regional forum, donors would become more sensitive to the recipients' objectives rather than the reverse. This, in turn, would give real meaning to the concepts of partnership and ownership.

19. This report discusses these issues in some detail in the light of the commitments to increase substantially the volume of aid to Africa, and on the assumption that these promises will be kept. It presents a perspective that departs from the current modalities governing the supply and uses of aid and insists that major reforms in institutions and current practice are essential if a "big push" for African development is to be really successful, and put an end to aid dependency.