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The Politics of Bilateral Donor Assistance

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The politics of bilateral donor assistance
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Summary

Motivated by the Millennium Development Goals and international campaigns aiming to 'end poverty', bilateral donors have in recent years made numerous commitments to substantially increase their foreign aid budgets. This paper looks at the role that bilateral aid plays in influencing the policy making processes of developing countries in the context of this surge. The paper uses quantitative and qualitative analysis to explore patterns of aid allocation, both across countries and sectors, and examines the dynamics of aid relationships in three case study countries in order to shed light on the mechanisms used by donors to promote their development agendas.

The paper concludes that bilateral donors do have significant influence in the policy making processes of the recipients of their aid. While recent years have seen an increased focus on national ownership of policies by recipient governments, several studies have shown that in certain circumstances the aid modalities intended to promote this increase in ownership—such as the Poverty Reduction Strategy Papers and General Budget Support—have actually had the opposite effect and increased donor oversight of developing country processes. As such, developing countries are often constrained in their policy options.

Quantitative analysis of the sectoral allocations of bilateral donors and case studies that look at donor-recipient relations in more detail, show that this influence has been used to shift emphasis away from investment in infrastructure and the productive sectors. This reflects the growing focus on social services and governance reform as means of achieving progress towards the MDGs. While these may in themselves be valuable investments, the paper highlights the danger of low investment in infrastructure, industry and agriculture—namely the inability to exploit synergies between social and economic policy, limiting social policy to a residual, protective role.

In this context, allowing recipients greater ownership over their policies can become little more than a façade. Indeed, there is a clear contradiction between the donors' focus on democratic good governance and their influence over sectoral priorities, which takes policy making power away from the government and accountability away from citizens. This highlights the disjuncture between the focus of donors on recipient ownership, and their continued mistrust of developing country administrative and policy making systems.

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1. Introduction

The Millennium Development Goals (MDGs) have come to embody the overriding objectives of development with particular focus on the goal of eradicating poverty. However, there is widespread acceptance that domestic resources alone will not be sufficient to meet the MDGs in many low income countries. This has led to calls from academia, media and international campaigns for western donors to massively increase their aid disbursements to the poorest countries. As a result there have been numerous commitments by donors in recent years to raise aid contributions to unprecedented levels. In the light of this focus on poverty reduction and promises of increases in funding by major donors, this paper looks at the politics of bilateral aid.

In particular, this paper seeks to answer a number of questions: first of all, how important is foreign aid to developing countries and how this been affected by the surge in aid, promised on numerous occasions by donors? Having established the trends in aid levels, the paper asks how have the donors used the considerable influence that their development assistance buys in developing countries? What are the developmental goals of the donors and how are these reflected in their aid priorities? What mechanisms do donors use to influence the policies of their recipients? What are the implications of this outside influence for national sovereignty and the formulation of nationally owned development strategies?

For the sake of brevity, this paper considers the development assistance of the five largest donors, France, Germany, Japan, the UK and the US,[2] as well as three Scandinavian donors, Denmark, Norway and Sweden, often cited as being relatively forward thinking and progressive (e.g. Schraeder, Hook and Taylor 1998). Altogether, these donors constituted 74 percent of the OECD countries' Overseas Development Assistance (ODA) in 2006. The paper utilizes a mixture of quantitative analysis to look at patterns of aid allocation and case study analysis to examine the politics of donor-recipient interactions.

Following this introduction, the next section sets out the framework of the paper, considering the importance of foreign aid to developing countries and the influence that this buys donors in their policy making processes. This analysis reveals an emphasis on poverty reduction and good governance in most donors' policy statements, both in terms of aid selectivity, whereby 'good' performers in the developing world are targeted for an increase in aid receipts, and the sectoral allocation of aid. The paper therefore proceeds by examining how these priorities are reflected in donor practice. Section 3 assesses the implementation of aid selectivity, while section 4 looks at the sectoral allocations of the donors. Finally, section 5 uses three illustrative case studies, Bangladesh, Ethiopia and Mozambique, to examine the donor-recipient relationship in more detail, looking at the mechanisms which donors have used to influence recipients in practice and the goals which they have promoted.

2. A framework for understanding the influence of bilateral donors

The policy process

The policy process can be envisaged as comprising three main activities: setting the boundaries of the debates and the policy agenda; identifying solutions to existing problems and selecting a policy option; and implementation of the policy selected. While the linear model of policy making, whereby these activities are viewed as discrete stages which take place consecutively, has been disputed (Court and Young 2006), it is still useful to envisage policy making as encompassing these activities albeit that they may overlap with one another.

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[2] In terms of amount of aid, the largest donors by percentage of GNI have consistently been Denmark, Luxembourg, the Netherlands, Norway and Sweden. While not covered here, the increasing importance of China and India as donors to Africa is also recognised. McCormick (2008) provides an insightful and balanced analysis of their likely impact on African development.

Each of these policy making activities can usefully be viewed as interactions between actors with differing viewpoints regarding the goals of development and the best strategies for achieving them, which take place in the context of political, economic, social and cultural institutions, which define the 'rules of the game'. The actors include international actors, such as the bilateral and multilateral donors, the governments and civil society organizations (CSOs) which are the potential and actual recipients of their aid, the populations of these countries and interest groups within them. As such, a recipient government, in making and implementing policies must balance the interests and pressures of a range of national and international actors with its own particular developmental vision. The interests of donors and the extent to which they are able to affect the priorities of recipient governments is the principal focus of this paper. As such, this leads us to consider in the remainder of this section: what the developmental priorities of donors are; what the extent of influence over recipients is; and how this influence is used.

Donor priorities

Economic growth was long considered the basic goal of development. While the emphasis initially was on the state to provide the engine of economic growth, this shifted to a market-led strategy in the 1980s and 1990s following the debt crises and the perceived need to roll back 'bloated' and 'inefficient' states in developing countries. However, the last ten years has seen a significant shift with poverty reduction replacing economic growth as the principal objective of development (Mosley, Hudson and Verschoor 2004). This followed recognition that several decades of development had made a disappointing impact on levels of poverty, partly as a result of the negative social effects of structural adjustment and the failure for the benefits of economic growth to 'trickle down' to the poor. This recognition led to the identification of a set of developmental goals by the OECD's Development Assistance Committee (DAC) in 1996 (OECD 1996), which in turn contributed to the MDGs which were established by the Millennium Declaration, with the headline grabbing goal of halving extreme poverty. Symbolic of the widespread acceptance of poverty as the main objective is the World Bank's focus on poverty in the World Development Report in 2000 (World Bank 2000).

In terms of donor priorities, a focus on ending poverty has led bilateral donors to take considerable interest in the sectoral priorities of the recipients of their aid, with basic social services receiving particular attention. Alongside this focus on poverty, governance has become increasingly prominent in donor discourse. A focus on governance has two main motivations, the first derives from efforts to improve the effectiveness of aid and the need for donors to demonstrate to their own taxpayers that their development funds are being used effectively rather than being corrupted for private gain, and leads to an emphasis on administrative efficiency and financial accountability. The second, more normative conception, which focuses on democratization and respect for human rights makes the assumption that a government accountable to its citizens, as well as being an important goal in itself, will contribute to the design of policies focused on poverty reduction, resulting in better developmental outcomes.

The governments of all but the most inhumane of regimes will share the donor focus on poverty. However, this does not prevent other objectives of developing country governments coming into conflict with that of poverty reduction at times, or indeed disagreements regarding how to achieve these objectives and therefore the policies required. Still more contested is likely to be the donor focus on good governance, which through increased accountability, implies considerable threats to the dominance of powerful elites in developing countries. One of the purposes of this paper is therefore to examine how influential donors are when their recipients disagree with their priorities.

The importance of aid to developing countries

The increased focus on development generated by the MDGs has contributed to a series of commitments by the North to provide aid for the South. In particular, EU countries pledged to increase ODA to 0.51 percent of GNI by 2010 and 0.7 percent by 2015 (EU 2005), while members of the G8 'agreed to double aid for Africa by 2010' at Gleneagles in 2005 (G8 Research Group 2006).

These commitments have undoubtedly resulted in increasing trends in ODA (see figure 1).[3] However, progress towards the targets is disputed based on the inclusion of debt relief in official ODA figures (Mehrotra 2002; Watt and Sharman 2006; Oxfam International 2007). As many of the debts cancelled were not being serviced, and the benefit to recipient countries will be spread over many years, whereas the complete cost of debt cancellation is declared in one year, the actual resources transferred to developing countries does not equal official ODA figures (Oxfam International 2006). This distinction is particularly important as commitments to increase aid have been accompanied by an unprecedented wave of debt cancellations as part of the Highly Indebted Poor Countries (HIPC-2) process and additional commitments made at the G8.

Figure 1: Total bilateral ODA

By including debt relief in their figures for ODA, the OECD (2007a) show that the majority of the targets set by DAC members at Monterrey in 2002 were met in 2006 (see figure 2 below). In particular, Denmark, France, Germany, Norway, Sweden and the UK all exceeded their target of 0.33 percent of GNI and the US exceeded its lower target of 0.12 percent of GNI.[4] However, given that the current round of massive debt cancellations will come to an end in the next few years, if future targets are to be met, a great increase in real transfers of resources will be necessary, first of all to fill the gap left by debt relief and secondly to provide significant further increases on current levels.

Figure 2: ODA as a proportion of GNI and major aid targets

These large flows of aid represent a considerable and growing proportion of resources in developing countries. One way of quantifying the importance of aid is to calculate the aid intensity in a country (ODA as a proportion of GDP). High levels of aid intensity may indicate a situation of aid dependency whereby 'a country cannot perform many of the core functions of government, such as operations and maintenance, or the delivery of basic public services, without foreign aid funding and expertise' (Bräutigam 2000: 9). Bräutigam proposes that levels of ODA greater than 10 percent of GDP indicate possible aid dependence (Bräutigam 2000).

Table 1: Aid intensity of low income and lower middle income countries

The data in table 1 clearly show that aid is of great importance to the poorest countries. The majority, 45 out of 62, of Least Developed and Low Income Countries (from now on the 'poorest countries')[5] and 10 out of 44 Lower Middle Income Countries for which data are available are potentially aid dependent according to the above criteria. In addition, bilateral donors make up the majority of development aid. This reliance of many developing countries on foreign aid means that donors are likely to be extremely influential when faced with recipient governments desperate to ensure continued access to foreign aid. While this is divided between the different bilateral donors, who do not necessarily have identical development priorities, table 2 shows that individual donors also provide

[3] For the purposes of this paper, data from the OECD-DAC is used. Overseas Development Assistance (ODA) is defined as flows 'provided by official agencies … or by their executive agencies' which are 'administered with the promotion of the economic development and welfare of developing countries as [their] main objective' and which are 'concessional in character and convey a grant element of at least 25 percent' (OECD 2007b: 1). Clearly using this definition neglects the considerable variation in the composition of the grant and loan components of aid, as well as the different donors' policies with respect to tied aid. While these issues are of major importance to developing countries, space constraints do not allow them to be thoroughly discussed here.
[4] Japan did not set any targets at the Monterrey Conference (OECD 2007a).
[5] Following the classification used by the OECD (see http://www.oecd.org/dataoecd/23/34/37954893.pdf).

highly significant proportions of individual countries' GDPs. In particular, the US provides an average of 2.7 percent of the GDP of the poorest countries and 3.7 percent of the GDP of Lower Middle Income countries, while France, Japan and the UK each provides an average of more than one percent of the GDP of the poorest countries. In addition, Eritrea, Iraq and Liberia all receive more than 10 percent of their GDP from the US, while the Republic of Congo receives more than 10 percent from France, indicating possible aid dependence on just one donor.

Table 2: Importance and distribution of donor aid

Table 2 also demonstrates that most bilateral donors tend to give at least some aid to virtually every developing country. Only Denmark, and to a lesser extent, Sweden and the UK, seem to be relatively selective in their allocations. It may be that even in countries which are not major priorities for donor assistance, bilateral donors like to be involved to some extent (Alesina and Dollar 2000). One likely explanation is that even a relatively small amount of aid buys a donor a voice in the policy making process.

The mechanisms of exerting influence

With current donor discourse dominated by poverty reduction and good governance, donors use a range of mechanisms of incentives and penalties to promote these goals with recipients of their aid. These different mechanisms are presented below as ideal types, however, it should be noted that in practice these mechanisms are often employed jointly and can be hard to differentiate from one another. In addition, to these mechanisms of direct influence, clearly the very fact that all donors promote the MDGs, poverty reduction and good governance in almost every policy statement and communication that they make will in itself influence the agenda setting of their recipient countries: the governments of developing countries are well aware of the policies favoured by donors.

Policy conditionality

Policy conditionality is the use by external donors of conditions to force recipients to implement certain policies, based on the threat that development assistance could be discontinued if the conditions are not fulfilled. The failings of policy conditionality have been thoroughly documented elsewhere and as such a lengthy discussion is not warranted here. Nonetheless, one important point is to note that although policy conditionality related to structural adjustment reforms may have been very successful in influencing the boundaries of the policy agenda and the policy selection of developing countries, a lack of national ownership of these imposed policies has meant that one of its weaknesses has been in ensuring the implementation of these policies. As a result donors now employ a range of other mechanisms to exert influence over recipient policies, in addition to clearly defined policy conditionality. At least part of the motivation for employing these other mechanisms is to correct for policy conditionality's weakness in ensuring implementation of desired policies.

Process conditionality

One response by donors to the perceived lack of national ownership generated by policy conditionality has been to focus on *process conditionality*, whereby the policy making process rather than a particular policy is the subject of donor specification. The aim of process conditionality is to change the balance of interests in policy making, so that the general population, and especially underrepresented groups such as the poor, have a greater say. In this way, process conditionality focusing on democratization and participation is expected to make governments more accountable to their populations.[6] The

[6] Clearly this assumption is problematic in two main ways. First of all, there remain considerable doubts as to whether democratic institutions can be constructed by external actors or whether democratisation is a process that needs to derive from the bottom-up. Secondly, the contradiction between government accountability upwards to donors and downwards to their electorate is itself incompatible with democracy (Browne 2006).

assumption is that greater government accountability to its citizens will lead to the design of policies focused on poverty reduction and that public participation will improve the likelihood of successful implementation of these policies.

Ex-post conditionality

Another response to the problems associated with conditionality has been to propose a switch from *ex-ante* to *ex-post* evaluation (Dollar and Pritchett 1998). In contrast to policy conditionality where aid distribution is based on ex-ante promises to implement policies in the future, ex-post conditionality is based on prior demonstrations of policy implementation or achievement of development goals.

In this respect the World Bank's *Assessing Aid* report has been extremely influential. It concludes that aid can be effective in reducing poverty but only in strong institutional settings and when governments implement 'good' policies (Dollar and Pritchett 1998). The implications of these findings are that rather than forcing recipient governments to change their policies using policy conditionality, donors should target poor countries that already have relatively good governance records and that are following 'good' policies.[7] It is proposed that this *aid selectivity* could act as a means of influencing the policies and behaviour of recipient countries by introducing competition for aid among developing countries. In this way, developing countries which do not satisfy selectivity criteria would have an incentive to 'improve' their policies and institutions in order to qualify for development assistance. However, for this to be effective donors would need to coordinate their activities to ensure that the poor performance of a recipient punished by one donor does not continue to be rewarded by another.

Rather than an on-off allocation decision implied by strict aid selectivity, a less drastic interpretation of the principle of ex-post evaluation is that aid disbursement is linked to results and outcomes such as the achievement of poverty reduction targets specified by the MDGs. This kind of 'outcome-based conditionality' allows aid recipients greater policy freedom regarding what policies to pursue, as long as they keep meeting development targets (Ortiz forthcoming).

Linking bilateral assistance to multilateral processes

Although the main focus of this paper is on bilateral donors,[8] the International Finance Institutions (IFIs) are massively influential on the bilateral donors and bilateral donors often link the provision of their assistance to the multilateral processes and the conditionality that is inherent in them.

The provision of multilateral aid is conditional on the preparation of a nationally owned PRSP approved by the IFIs. While there is no formal prescription for the required content of PRSPs, several observers point out that recipient countries, based on many years of experience dealing with the IFIs,