



**The Cartel of Good Intentions:
Bureaucracy versus
markets in foreign
aid**

By William Easterly

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The tragedy of foreign aid is not that it didn't work; it was never really tried. A group of well-meaning national and international bureaucracies dispensed foreign aid under conditions in which bureaucracy does not work well. The hostile environment under which such aid agencies functioned induced them to organize a cartel that increased inefficiency and reduced effective supply of development services, frustrating the good intentions and dedication of development professionals. The cartel of good intentions allows rich country politicians to feel that they are doing all in their power to help the world's poor, supports rich nations' foreign policy goals, preserves a panoply of large national and international institutions, and provides resources to poor country politicians with which to buy political support. In short, foreign aid works for everyone except for those whom it was intended to help, with results such as the aid agencies' calculation that it takes \$3521 in aid to raise a poor person's income by \$3.65 a year. The environment that created aid bureaucracies led those organizations to (a) define their output as money disbursed rather than service delivered, (b) produce many low-return observable outputs like glossy reports and "frameworks" and few high-return less observable activities like ex-post evaluation, (c) engage in obfuscation, spin control, and amnesia (like always describing aid efforts as "new and improved") so that there is little learning from the past, (d) put enormous demands on scarce administrative skills in poor countries. Now rich countries have used their past lack of effort at assuring effective aid as an excuse to keep aid at paltry levels. Instead, to change this unhappy equilibrium, policymakers in rich and poor countries should experiment with decentralized markets to match those who want to help the poor with the poor themselves freely expressing their needs and aspirations.

The Cartel of Good Intentions: Bureaucracy Versus Markets in Foreign Aid

May 2002

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Abstract: The tragedy of foreign aid is not that it didn't work; it was never really tried. A group of well-meaning national and international bureaucracies dispensed foreign aid under conditions in which bureaucracy does not work well. The hostile environment under which such aid agencies functioned induced them to organize a cartel that increased inefficiency and reduced effective supply of development services, frustrating the good intentions and dedication of development professionals. The cartel of good intentions allows rich country politicians to feel that they are doing all in their power to help the world's poor, supports rich nations' foreign policy goals, preserves a panoply of large national and international institutions, and provides resources to poor country politicians with which to buy political support. In short, foreign aid works for everyone except for those whom it was intended to help, with results such as the aid agencies' calculation that it takes \$3521 in aid to raise a poor person's income by \$3.65 a year. The environment that created aid bureaucracies led those organizations to (a) define their output as money disbursed rather than service delivered, (b) produce many low-return observable outputs like glossy reports and "frameworks" and few high-return less observable activities like ex-post evaluation, (c) engage in obfuscation, spin control, and amnesia (like always describing aid efforts as "new and improved") so that there is little learning from the past, (d) put enormous demands on scarce administrative skills in poor countries. Now rich countries have used their past lack of effort at assuring effective aid as an excuse to keep aid at paltry levels. Instead, to change this unhappy equilibrium, policymakers in rich and poor countries should experiment with decentralized markets to match those who want to help the poor with the poor themselves freely expressing their needs and aspirations.

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I am grateful to Robert Ayres, Nancy Birdsall, Rebecca Blank, Erik Bloom, William Cline, Susan Collins, Simon Evenett, Roberta Gatti, Amar Hamoudi, Ravi Kanbur, Devesh Kapur, Charles Kenny, Michael Kremer, Craig Neal, John Nellis, William Niskanen, Guy Pfeffermann, Lant Pritchett, S. Ramachandran, Martin Ravallion, David Roodman, Judith Tandler, Nic Van de Walle, and Dennis Whittle for helpful comments, exchanges of ideas, or references, some of which influenced me quite a bit, although none should be held responsible.

Introduction

Though the term “cartel” normally evokes images of greedy oil producers and murderous drug lords, another more benevolent set of institutions also meet the definition of cartel. The members of this cartel are the world’s leading foreign aid organizations, which constitute a near-monopoly relative to the powerless global poor.

This state of affairs helps explain why the global foreign aid bureaucracy has run amok in recent years. Consider a poor person in the countryside of Ethiopia who wants to get a pothole (a hole more the size of a car than a pot actually) repaired in front of his house. The Ethiopian government looks to foreign aid for financing of public services. This poor person somehow communicates his desires to “civil society representatives” and/or non-governmental organizations (NGOs), who allegedly articulate his needs through the government of Ethiopia (itself dominated by one minority ethnic group) to the international donors. The national government solicits a “poverty reduction support credit” (PRSC) from the World Bank (also known as the International Bank for Reconstuction and Development, or IBRD) and a Poverty Reduction and Growth Facility (PRGF) from the International Monetary Fund (IMF). These agencies have many competent staff that can make a difference, but they are often swamped by bureaucracy from above (see organization chart below). To get loans from the IMF and World Bank, the government completes a satisfactory poverty reduction strategy paper (PRSP), in consultation with civil society, NGOs, and other donors and creditors. The government prepares the PRSP in light of the fourteen-point Comprehensive Development Framework (CDF) of the World Bank. The World Bank follows a series of internal steps to approve a PRSC, including the preparation of a Country Assistance Strategy (CAS), a pre-appraisal mission, an appraisal mission, negotiations, and Board approval, all in accordance with OD 8.60, OP 4.01, and Interim PRSC Guidelines. The government also seeks qualification for the Enhanced Heavily Indebted Poor Countries (Enhanced HIPC) Initiative so that the new loan doesn’t simply go to service old loans. The creditors and the government conduct a debt sustainability analysis (DSA). HIPC,

PRSC, and PRGF require numerous reform conditions such as participation of the poor, poverty-reducing government expenditure monitored through annual Public Expenditure Reviews (PERs), fiscal deficit targets, revenue mobilization targets, and structural reforms such as the Civil Service Reform Program (CRSP), implementation of a Financial Information Management System (FIMS) in government, financial sector reform in line with the Basel standards and the eleven areas of International Standards and Codes recommended by the IMF and World Bank, control of money laundering, and privatization, lowering trade barriers in ways governed by the World Trade Organization (WTO), perhaps by applying the “Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries”. The PRSP may or may not include money that could finance road repair for this poor person, depending on the national development program (NDP) that forms part of the government’s Agricultural Development Led Industrialization (ADLI) strategy. The amount of money for road maintenance will depend on a prioritization of various needs for expenditure in a multi-year medium-term expenditure framework (MTEF). The thousand-page *Poverty Reduction Strategy Paper Sourcebook* of the World Bank provides guidance like the following for determining spending on road maintenance:

The sector ministries prepare medium-term strategic plans that set out the sector’s key objectives, together with their associated outcomes, outputs, and expenditure forecasts (within the limits agreed upon by the Cabinet). These plans should consider the costs of both ongoing and new programs. Ideally, spending should be presented by program and spending category with financing needs for salaries, operations and maintenance, and investment clearly distinguished.¹

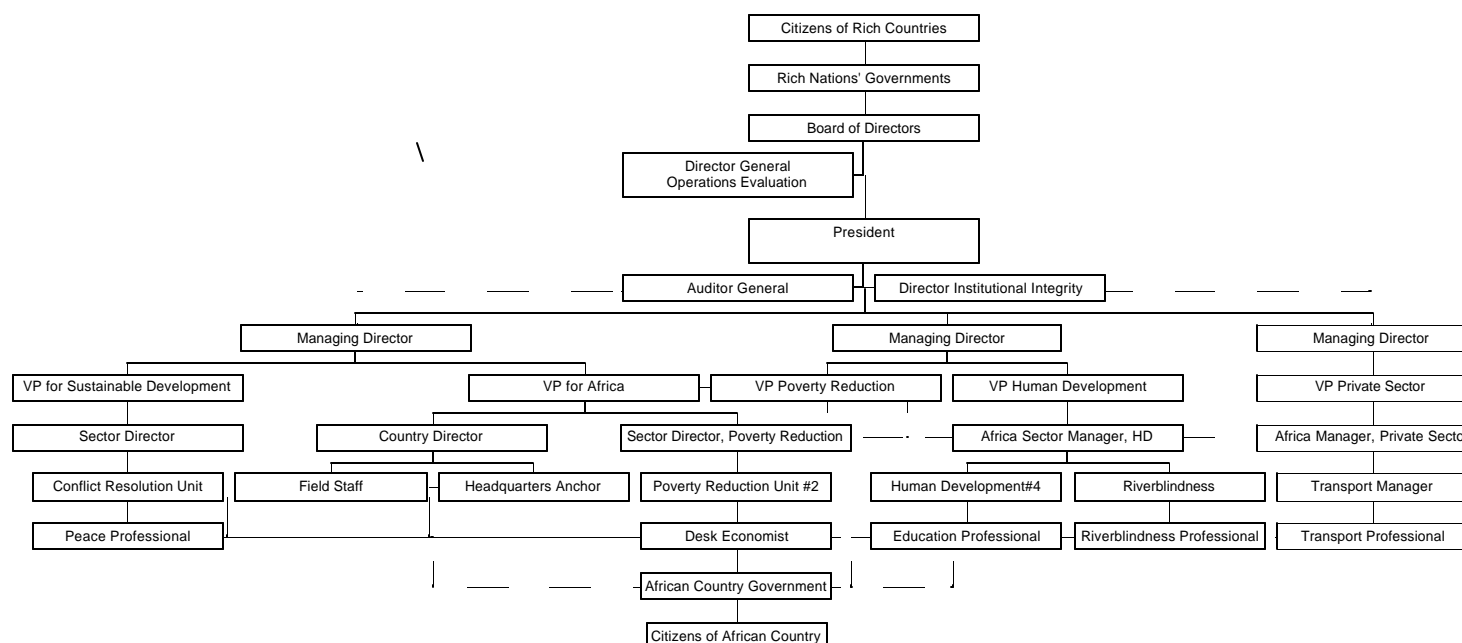
Meanwhile, if beleaguered Ethiopian government officials have any time left, the PRSP Sourcebook also suggests that they cost out all the various ways the government is making progress towards the International Development Goals (IDGs, also known as Millennium Development Goals or MDGs), which include targets for poverty, hunger, infant and maternal mortality, primary education, clean water, contraceptive use, AIDS, gender equality, and the environment. These were all on the agenda of world leaders who assembled for the UN

¹ Poverty Reduction Strategy Paper Sourcebook

International Conference on Financing for Development in March 2002. Meanwhile, other international bodies will review the Ethiopian PRSP, such as the United Nations Development Program (UNDP), the African Development Bank (ADB), the Consultative Group to Help the Poorest, the United Nations Conference on Trade and Development (UNCTAD), the Food and Agriculture Organization (FAO), the World Trade Organization (WTO), the World Health Organization (WHO), the International Labor Organization (ILO), the European Union (EU), the United Nations Children's Education Fund (UNICEF), the United Nations High Commissioner for Refugees (UNHCR), as well as NGOs and the Development Assistance Group (DAG), which includes representatives of national aid agencies such as those from Austria, Belgium, Canada, Finland, France, Germany, Ireland, Italy, Japan, Netherlands, Norway, Spain, Sweden, Switzerland, United Kingdom (DFID), and the United States (USAID). If the international lenders and donors approve the PRSP and release new funds to the national government, then government will allocate the money in accordance with the NDP, ADLI, CRSP, MTEF, CDF, PRGF, PRSC, and PRSP, after which the money will pass through the provincial governments and the district governments, and the district government may or may not repair the pothole in front of the poor person's house. Within the World Bank, the transport economist must try to convince the desk economist that a Road Maintenance Loan that would repair this particular pothole merits higher priority than some other project, like say an Education Reform Loan pushed by the education economist (see diagram for a rendering of the World Bank organization chart applicable to a typical African country).² If the poor person is dissatisfied and wants to complain, he faces so many different organizations and such a complex hierarchy within each organization he is understandably at a loss.

² I had to arbitrarily shift some VPs from one Managing Director to another so they would fit in the chart, and to omit altogether such relevant managers as the Senior Vice President and Chief Economist (no offense intended).

World Bank Organization Chart for a Typical African Country Client



Why does the business of delivering foreign aid services to poor people in poor countries involve so much unproductive bureaucracy? It's not that aid bureaucrats are bad; in fact many smart, hard-working, dedicated professionals toil away in the world's top aid agencies. But the perverse incentives they face explain the organizations' obtuse behavior. Bureaucracy works best where there is high feedback from beneficiaries, high incentives for the bureaucracy to respond to such feedback, easily observable outcomes, high probability that bureaucratic effort will translate into favorable outcomes, and competitive pressure from other bureaucracies and agencies.³ In short, bureaucracy works best when it functions something like a free market.

³ There is a large literature that makes these common sense points. See especially Wilson 1989. The World Bank's 2001 World Development Report on Institutions presented evidence that direct election of individual politicians, more political competition, and a free and independent media reduced bureaucratic corruption and improved public service delivery. Djankov et al. 2001 similarly finds that government domination of the media worsens social service delivery. La Porta et al. 1998 found that more democratic governments were more efficient and delivered more public goods, as were governments bound by common law rather than civil or socialist law (arguing that common law gives more voice to citizens). Kaufmann et al 2001 and Kaufmann et al 2002 show how bureaucracies in Bolivia with more citizen voice and more transparency deliver a higher quality and quantity of public services. Isham, Kaufmann, and Pritchett 1995 found that countries with civil liberties had higher returns on aid projects. Pritchett and Woolcock 2002 describe the failure of the bureaucratic model in public service delivery under unfavorable conditions in poor countries.

All of these conditions are unfavorable in foreign aid. Foreign aid is approved by voters of rich country A, whose national government gives the money through its own aid bureaucracy and international aid bureaucracies to the government of poor country B, who in turn is supposed to make some effort to give the money to poor people in country B. The poor people in country B have little voice in their own government, much less a voice in the distant national aid bureaucracy, international aid bureaucracy, and political campaign in rich country A. The rich country aid bureaucracy and international aid bureaucracy, although well intentioned, have little incentive to hear poor people from country B who do not vote or form pressure groups in country A. The heartbreaking reality of aid isn't so much that it didn't work as that we in rich countries didn't really care whether it did.

Although a poor person in Ethiopia can easily observe a pothole outside his house, it is hard for a foreign aid agency to continuously observe how country B's pothole prevalence. Moreover, it is very hard for aid bureaucracies to get constructive feedback from past mistakes, like financing a road full of potholes, because any admission of past failure is a threat to getting new aid resources to dispense in the future. Additional bureaucratic aid agency effort at fixing potholes in country B will likely miscarry, given the absence of feedback and the dependence of the outcome on government officials and other agents in country B outside of the agency's control. If poor countries are poor because of bad government and other collective action problems, then bureaucratic effort in those countries is less likely to succeed than in rich countries. Finally competitive pressure on aid agencies is very limited, because for self-preservation foreign aid agencies agree to coordinate their actions rather than compete, forming a "cartel of good intentions".

Cartels thrive when customers have little opportunity to complain or find alternative suppliers. For example, the Organization of Petroleum Exporting Countries (OPEC) in its heyday in the 1970s could dictate terms to the customers; it was only when more non-OPEC oil exporters emerged that its power weakened. In the foreign aid business, customers (i.e., the poor

citizens in developing countries) have few chances to express their needs yet cannot exit the system. Nongovernmental organizations (NGOs) can only hold the aid institutions to task on a few high-visibility issues, like conspicuous environmental destruction or taking away the homes of indigenous people (thus the World Bank eventually cancelled its support for the Narmada dam project in India under pressure on both issues). Under these circumstances, even while the foreign aid agencies make good faith efforts to consult the clients, they remain accountable mainly to themselves.

Bureaucracy in foreign aid evolved to face a hostile environment. The resulting edifice of national and international bureaucracies has not provided services effectively to the world's poor. Despite numerous attempts at reform, bureaucratic characteristics of foreign aid stayed remarkably persistent throughout its fifty year history. The tragedy is that bureaucracy captured foreign aid under conditions in which it didn't work well. Rich country donors allowed this bureaucratic capture and then used it as an excuse to decrease aid, rather than enforcing service delivery to the world's poor. This paper suggests that foreign aid move away from monopolistic bureaucracies to decentralized markets. One possibility is giving "aid vouchers" directly to poor people to increase competition, feedback, and accountability.

A story of bureaucracy in foreign aid

I will sketch out a story of bureaucratic behavior and then describe the actual history of foreign aid as a case study of this story. There is a large economics literature on the theory of bureaucracy, principally started by Niskanen (1968, 1971), with good recent surveys by Niskanen (2001), Moe (1997) and Wintrobe (1997). There is also a rich literature on bureaucracy from other social scientists, of which the outstanding example is Wilson (1989).

Niskanen's model, which I give reflecting later amendments to which he agreed, postulated that a bureaucracy behaved like a monopoly firm facing a downward sloping demand curve for the quantity of bureaucratic services as a function of the "price". The bureaucracy maximized the equivalent to firm profits, usually called the discretionary budget (total budget

minus costs of producing the service). A larger net budget was associated with perks for the bureaucrats (or bureaucrats may genuinely care about their field and so maximize the budget it gets.) The bureaucratic monopolist equated marginal revenue to marginal cost, which tended to raise the price and restrict the quantity of services relative to the non-bureaucratic competitive outcome. Hence, Niskanen's model gave a simple explanation for bureaucratic inefficiency (high price relative to marginal cost) and under-provision of services.

Subsequent literature challenged the Niskanen model on several grounds. First, the literature argued the political authorities had the power to design incentives that would give an optimal outcome, using a principal-agent framework. Second, the literature pointed out that bureaucracies don't usually have a monopoly in their area of responsibility – there are usually other competing agencies in the same area.

Moe 1997 is right that the principal agent models are really more about the Congress, Parliament, or President than they are about bureaucracy.⁴ They seem less relevant for bureaucracies with less direct political oversight. For a multinational aid agency, there is a collective action problem among the multiple principals that inhibits designing an optimal principal-agent contract. Principal-agent theory says having multiple principals dramatically weakens the incentives for the agent (the international agency). Each principal will try to get the agent to pursue their objectives and neglect the other principals' objectives; in the aggregate this weakens incentives on all objectives for the agent.⁵ Even for a national aid agency, the unobservable effort and outcomes and virtually nonexistent feedback from the intended beneficiaries makes designing the optimal principal-agent contract a formidable undertaking.

⁴ “Too often, bureaucratic theories are really not pursued for what they can tell us about bureaucracy, but rather for what they can tell us about how much power Congress and other authorities have and what mechanisms they employ to get their way. Bureaucracy is treated as little more than a means to these more important ends and not as an institution worthy of intensive explanation in its own right.”

⁵ For a review, see Dixit 2000

On the competitiveness of bureaucracies, that likely varies across different types of bureaucracy and the environments in which they operate. Suppliers always like to collude, but competitive markets prevent it. Many American municipal bureaucracies face a competitive market because residents can vote with their feet. However, other kinds of bureaucracies may collude if entry is difficult, punishing deviators from collective agreements is easy, and no legal obstacles prohibit collusion. Entry is more difficult in most bureaucracy than in private business, lessening one threat to stability of the collusion agreement. The ethic of bureaucratic behavior stigmatizes excessively competitive deviants (“rogue bureaucracies”), who are singled out for blame if anything goes wrong. Far from outlawing collusion among bureaucracies, governments often encourage it (“coordination” comes up in about every bureaucratic discussion). Bureaucracies may then form a cartel, and behave collectively like the net budget-maximizing monopolistic bureaucracy.

Conditions in foreign aid make it likely that aid bureaucracies will collude even more than other bureaucracies. Aid agencies will operate as a “cartel of good intentions” Why? First, aid agencies maximize gross foreign aid net of operating costs. Maybe aid agency employees want the maximum perks possible, or maybe aid workers genuinely want more resources for the poor countries. Aid agencies garner more aid revenues by acting collectively, because they realize economies of scale in campaigning for aid revenues.

Second, foreign assistance to poor states is a very difficult and risky business, as argued earlier – the causes of national poverty are many and the proven successes are few (not zero, though). The knowledge about how to achieve economic development is itself underdeveloped. The aid agency will have to work with local elites and problematic local government institutions who themselves may not have an incentive to see their society achieve poverty reduction. The feedback from the intended beneficiaries –the poor and voiceless –is not there to give guidance on what is working. The more severe these problems in a society, the more likely that it is a client of a foreign aid agency. Even worse, the aid agency will often be called upon for help just when

an already difficult situation gets even worse – in a social and economic crisis. Probability of failure is high. The aid agency is in the unenviable position of being blamed for a likely bad outcome. Although rational evaluators could control for the difficulty of the environment, conditional evaluation requires inside knowledge that only the aid agencies themselves are likely to have – and of course they are not credible when they protest how hard their job is.

Another element in the market power of aid agencies is that the typical agency forces governments seeking its money to work exclusively with that agency's own bureaucracy--its project appraisal and selection apparatus, its economic and social analysts, its procurement procedures, and its own interests and objectives. Each aid agency constitutes a mini-monopoly, and the collection of all such monopolies forms a cartel.

Agencies handle the high risks in foreign aid by the time-honored bureaucratic strategy of sharing blame. The bureaucracies form a united front so evaluators don't know who to blame for bad outcomes. Monitors don't know whether to blame the international aid community or the national recipient government for bad policies. They don't know whether to blame bad economic design of aid programs, or bad politics that undermines their implementation. The monitors don't know whether to blame the International Monetary Fund for excessive fiscal austerity that restricts funds for worthy programs, or the World Bank for failure to preserve high return areas from public expenditure cuts. Evaluators don't know whether the IMF and World Bank are too tough or too lax in enforcing conditions, or if it is really the regional development banks are being too hard or easy in their conditions for aid. Monitors don't know whether to blame the bilateral aid agencies for being influenced by foreign policy priorities, or the multilaterals for applying a "one size fits all" ideological program to all countries. This sharing of blame is a convenient equilibrium for all aid agencies together. The multiplicity of actors in the aid outcome reduces the probability of blame for any one actor. Hence, there is safety in numbers in the foreign aid business.

Driving competitive foreign aid bureaucracies out of business doesn't make sense since it increases the probability of blame for the remaining bureaucracies. Once a collusive agreement is in place, bureaucracies will not cheat on the agreement by supplying a larger quantity of foreign aid services at a lower price. Such "rogue" bureaucracies are dangerously exposed to bearing solitary blame for their extra activities if they turn out to fail. The higher is the risk of failure, the lower is the incentive to cheat and the higher the incentive to remain in the blame-sharing coalition.

A similar blame-sharing story could explain why foreign aid bureaucracies collude to form a united front relative to a foreign aid recipient, rather than competing to satisfy the recipients' needs. Any agency that "wins the contract" to service recipient X to the exclusion of its rivals becomes dangerously exposed to blame if anything goes wrong in X.

The cartel of good intentions unites donor organizations with different objectives and agendas. This is nonetheless in their mutual interest, because advocates of one objective agree to support other objectives in return for support for their own cause ("log-rolling" in political economy terminology). Conversely, one aid agency will not criticize another agency's interventions; the second will reciprocate such critical restraint.⁶ This collusion destroys information, since one aid agency knows more about bad performance of another agency than outside evaluators. Overall critical evaluation of past aid efforts is suppressed by all agencies because it threatens the overall aid budget. Controlled group experiments, like those that made critical progress possible in medicine, are dangerous because they may generate negative publicity for the whole aid effort. Evaluation of individual interventions (like a particular method of agricultural extension) is forsworn in favor of unconditional support for a myriad of development efforts. The feedback from experimentation and learning by doing that is essential to success in any activity is therefore mostly absent. This robs the aid community of its historical memory.

Thus, donors form a cartel out of the best of intentions. They wind up raising the price and restricting the quantity of foreign aid services. Donors are thus immune from competitive pressure and can implement “supply-driven” aid programs. This may explain the inefficiency of foreign aid and for its disappointing output.

Foreign aid bureaucracies also respond to this problematic environment by skewing the composition of their output in favor of items that are more observable to those outside the aid agencies. If outcomes were perfectly observable at zero monitoring cost, the median voter in a rich country would equate the relative marginal benefit of an aid service to its relative price. With costly monitoring to verify output, the relative marginal benefit of aid is equated to the relative price of aid services plus the marginal cost of monitoring. If monitoring has a higher marginal cost the lower is the ease of observation, then demand is lower for less observable aid services. So aid bureaucracies will define their outputs as much as possible in observable units.⁷ This includes observable outputs that the agencies produce for each other; collusion will suppress any complaints about the quality of such intermediate outputs. The cartel can threaten with public embarrassment any agency tempted to shift from producing visible low return outputs to invisible high return outputs, since the rogue agency will have little to show the public. Thus, even agencies that would like to produce more invisible effective services are kept in the fold. The collective equilibrium is still an emphasis on observable output.

Another response to the difficult environment is obfuscation. Aid agencies are more likely to use bureaucratese, acronyms, and misleading euphemisms than other less risky bureaucracies. However, there is a tradeoff to the bureaucracy -- more obfuscation lowers not only the probability of blame but also the observability of output, which lowers demand for the output as I have just argued. So the obfuscation will hide bad outcomes, while advertising good

⁶ This argument is inspired by Pritchett’s (2001) model of why “it pays to be ignorant.”

⁷ Tirole 1994 has a principal-agent model that also delivers the prediction that government agencies producing multiple outputs will focus their efforts on the observable ones. Dixit also makes this point in a principal-agent framework.

outputs. The aid community over-promises ex ante, then exaggerates the success ex post. The marriage of obfuscation and advertising is “spin control.” Collusion enforces the use of “spin control.” A deviant agency that allocates too many resources to producing development services and too little to spin control will be vulnerable to public relations attacks by the other agencies.

The aid process begins in an aura of emergency. Do something! Do anything! Do it right away!
(Pressman and Wildavsky 1984)

A history of foreign aid

A convenient starting place for the history of foreign aid is with the Point Four program of Harry S. Truman, which he announced in his inaugural address on January 20, 1949: “We must embark on a bold new program for ... the improvement and growth of underdeveloped areas. More than half the people of the world are living in conditions approaching misery... For the first time in history, humanity possesses the knowledge and the skill to relieve the suffering of these people.”

I believe this was the first call for peacetime aid from one state to another in history. At the moment of birth, we have some characteristics of foreign aid that will last through the years – the call for a new program, the rationale in terms of poverty, and the optimism that foreign aid programs can make a big difference.

A statement two years later by a group of UN experts was more precise: “a 2 percent increase in the per capita national incomes cannot be brought about without ... a sum of money ... of about \$3 billion a year” (UN Expert Group 1951). This started a fashion of setting precise targets, calculating aid “requirements” to achieve this target, and then calling for an aid increase. So Walt Rostow in his famous *Stages of Growth* declared that “an increase of \$4 billion in external aid would be required to lift all of Asia, the Middle East, Africa, and Latin America into regular growth, at an increase of per capita income of say, 1.5% per annum.” (Rostow 1960) This recommendation would have approximately doubled current aid spending. Rostow, like others at the time and for many years afterward, also aid was temporary, that only 10-15 years was needed before poor countries attained “self-sustaining” growth in which aid was no longer necessary. The

model for these early efforts to calculate the aid requirement was the Harrod-Domar growth model: growth was proportional to investment, which was in turn financed by aid. Solow's 1957 article on growth had already discredited the Harrod-Domar model in the mainstream profession (as Domar himself acknowledged immediately, saying he had meant to model the business cycle rather than growth), but the model lived on in the development literature (see Easterly 1997).

The statements advocating increased aid continued: "existing foreign aid programs and concepts are largely unsatisfactory ...we intend during this coming decade of development to achieve a decisive turnaround in the fate of the less-developed world, looking toward the ultimate day ...when foreign aid will no longer be needed." (John F. Kennedy 1961) "we recommend a substantial increase in official aid flows" (Pearson Commission 1969), "the current flow of ODA ... is only half the modest target prescribed by the internationally accepted United Nations Strategy for the Second Development Decade" (World Bank President Robert McNamara, 1973), "additional concessionary resources would be required to achieve both higher rates of growth in the poorest countries" (World Bank, IDA-6, 1980), "A cut of just 10 percent in military spending by the countries of the North Atlantic Treaty Organization would pay for a doubling of aid...real growth in aid of only 2 percent a year is an unacceptably weak response to the challenge of global poverty" (World Bank WDR 1990).

The idea of doubling current aid is still a popular rhetorical device in 2001: "If we are serious about ensuring a beneficial globalization and meeting multilateral development goals we have all signed on to, we must double ODA from its current level of about \$50 billion a year." (World Bank President James Wolfensohn, 2001) A World Bank technical study on the cost of meeting the international goals concurred on doubling: "An increase in foreign aid of an amount equal to current foreign aid ... is about the right order of magnitude for achieving the development goals." (World Bank 2002)⁸ It's all a little circular, however, as the World Bank's

⁸ To make this calculation, the World Bank technical study in 2002 was still using the Harrod-Domar growth model 44 years after its demolition by Solow.

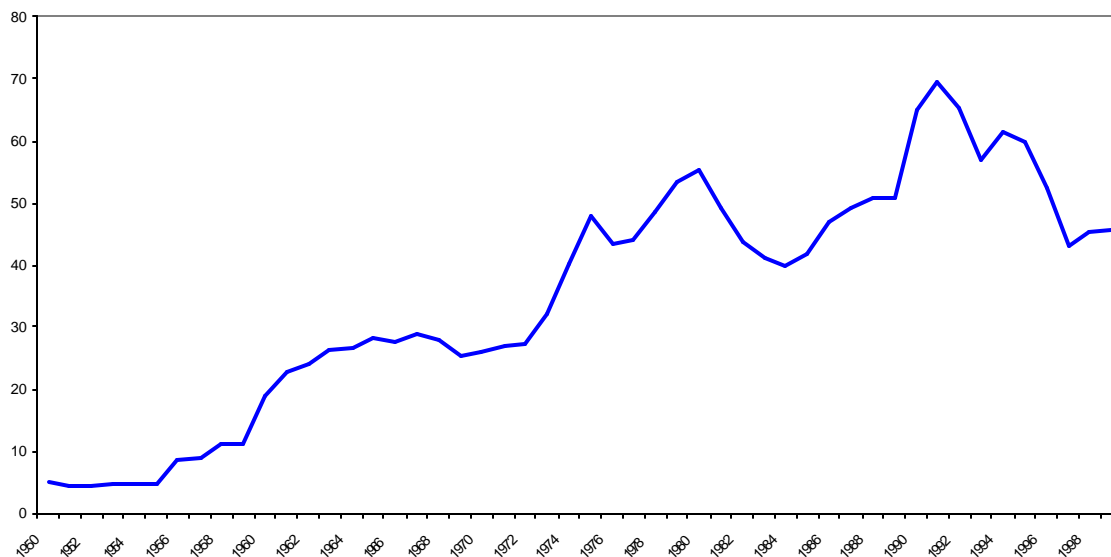
Poverty Reduction Strategies Sourcebook said “Mobilizing resources is without doubt a primary function of targets set by the international donor community such as the International Development Goals.”

The United Nations adopted the Millennium Development Goals (MDGs, also known as the International Development Goals) in a resolution on the turning of the new millennium. They were embraced by all the aid agencies, and set targets for reducing poverty, hunger, infant and maternal mortality, gender inequality, illiteracy, AIDS prevalence, and environmental degradation by the year 2015. The opening sentences of the UN Resolution said “We will spare no effort to make the United Nations a more effective instrument for pursuing all of these priorities. We resolve therefore: To ensure that the Organization is provided ...with the resources it needs to carry out its mandates.”⁹

In the new year, the UN Conference on Financing for Development (the name says it all) in Monterrey, Mexico in March 2002 continues the tradition of focusing on volume rather than effectiveness of aid. UK Chancellor Gordon Brown currently calls for a new “Marshall Plan,” a common precedent invoked for needs from post-Soviet Bloc countries to Bosnia to Africa to Afghanistan.

Aid mounted throughout the period when advocates called for an increase (Figure 1). It did indeed double several times from the early days to the present. If all foreign aid given since 1950 had been invested in US Treasury Bills, the cumulative assets of poor countries by 2001 would have amounted to \$2.3 trillion. The World Bank’s administrative expenses went from \$81 million in 1959-60 to \$1.5 billion in 1993-94 (in constant fy1993 dollars), while its staff went from 657 to 7,106 (Kapur et al. 1997) Meanwhile, the typical poor country has stagnated over the last two decades, and in many aid-intensive African countries for even longer. There have been individual success stories and progress on other indicators like infant mortality and

Figure 1: Overseas Development Assistance in 1999 billions of US\$



school enrollment. But the goal of increased living standards and reduced poverty in the typical poor country was not attained. The decline in the 1990s reflects some aid weariness amidst the feeling that foreign aid created something much less than \$2.3 trillion in productive assets.¹⁰

Meanwhile, rich country politicians consoled themselves they had done all in their power for the world's poor, instead of trying to change the bureaucratic edifice that led to poor results. Rich countries and aid agencies found it convenient to blame the governments of poor countries entirely for aid failures, as opposed to rich country politicking and malfunctioning donor bureaucracies.

Coordination

From the earliest days of aid, the emphasis of all participants has been on coordination rather than competition. After reading the literature one can hardly say “aid” without adding “coordination”. President Truman signaled in 1949 that “this should be a cooperative enterprise in which all nations work together through the United Nations and its specialized agencies wherever

9 55/2. United Nations Millennium Declaration

¹⁰ The report of the Meltzer Commission in March 2000 summarized many of the complaints about aid ineffectiveness.

practicable.” Two decades later, an aid commission repeated “A serious effort is necessary to coordinate the efforts of multilateral and bilateral aid-givers and those of aid-receivers.” (Pearson Commission 1969) The World Bank’s 1981 Berg report on Africa agreed that “Aid coordination, both within recipient countries and among major financing agencies, has been recognized as increasingly important...” (World Bank, 1981) Despite repeated calls for coordination, there was never enough: “donors must act more in concert – with each other and with recipients. This report suggests six ways to improve coordination.” (World Bank Africa report, 1986) “Better coordination among international financial institutions is needed.” (World Bank, IDA-12, 1998) “Deputies encouraged Management ... to maintain close collaboration with other multilateral development banks (MDBs), the OECD-DAC Task Force on Donor Practices, the Strategic Partnership with Africa (SPA), the United Nations and its specialized agencies, and bilateral development assistance agencies. They also noted progress in strengthening partnerships between IDA and other development institutions...and welcomed the recently negotiated Memoranda of Understanding with the African, Asian and Inter-American Development Banks.” (World Bank, IDA-13, 2001)

These continued calls for coordination illustrate first, that cooperation is desired over competition in foreign aid, and second, that cooperation is always a little out of reach. These are consistent with the natural tensions inherent in a cartel – that agencies formally forswear competition but at the same time always feel temptation to encroach on others’ turf.

To give an example from another activity, we have statements like the following “representatives ... meet ... to co-ordinate and unify their ... policies in order to promote stability and harmony”, progress was made through “the increased level of cohesion between Members,” the activity stands to benefit ”from the advances that have been made in the area of co-operation in recent years”, “to realize our increasingly reciprocal ambitions, a lot of hard work, compromises and true goodwill must come into play. Co-operation, not confrontation, is the best

strategy for the betterment of our generations and posterity.” These are all statements from meetings over the last few years of the OPEC oil cartel.

The “coordination” in foreign aid protects the smallest players in the business, even when dealing with them drives the poor countries’ governments to distraction. One wonders if the transactions costs were worth the effort for the Senegalese government to receive 3,344 Euros from the Finnish Ministry for Foreign Affairs Department for International Development Cooperation in 2001,¹¹ or how well Yasser Arafat is monitoring tenders in November 2001 for Consultancy Services for the Palestinian–Finnish Education Programme, Phase I. As the World Bank (1998) said, “It is hard to explain this behavior, except that different donors like to “plant their flags”.”

The multiplicity of donors impelled the aid community to call for centralization of aid and all other revenues by the recipient government:

Negotiating an external assistance strategy in the context of the PRSP process that explicitly identifies the priority sectors and programs for donor financing... More detailed external assistance strategies can then be developed for key areas through sectoral working groups in which representatives of major donors and line agencies participate... **Agreeing on financing priorities for individual donors within the framework of a global external assistance strategy**, rather than through bilateral agreements... (World Bank Poverty Reduction Strategy Sourcebook, 2001)

This asks recipient governments to do central planning, which even rich countries with far more administrative capacity than poor countries have a hard time doing (even without worrying about small grants from the Finnish Ministry for Foreign Affairs Department for International Development Cooperation). This asks the undermanned government of Ethiopia to decide where and whether a given pothole merits repairing, and then “coordinate” which amongst a sea of donors and programs will do the job.

All of the classic criticisms of central planning – the vast information requirements, the oversimplification to quantifiable targets as opposed to the real subjective wants, the meeting of targets without regard to relative costs and benefits, the lack of feedback from local practical

¹¹ http://global.finland.fi/english/publications/annual/2001/annual_02appendices.pdf

knowledge – apply with even more force in a poor country with poor institutions and under-skilled civil service than in a rich country.

Having the government bureaucracy even attempt to “coordinate” donors puts the aid community in a half-way house where they substitute monopoly for competition. First, the “cartel” enables donors to escape pressure for reduction of high costs. Second, the donors present a united front to the well-intentioned people in the rich countries who want to give money to people in poor countries, making it difficult for them to discriminate which among the donors is the most effective channel. Third, the donors impose an unequal relationship on the recipient government, who can only take or leave what the United Donors offer. Finally, the “cartel of good intentions” extends to include the local government bureaucracy, confronting the beneficiaries with a monopoly that is not always customer-friendly. There are many reports like the one in Ukraine of “humiliation that one endures from government bureaucrats, infamous for their ferocious and insulting tone.” In Esmeraldas, Ecuador a group of villagers reported “The mayor even slapped a woman who asked for help...” (Voices of the Poor 2000) Likewise, Filmer and Pritchett 2001 report “a client survey of women who had a birth in the past 2 years at rural health centers in the Mutasa district of Tanzania revealed the most frequently cited disadvantages of giving birth in an institution were: ridiculed by nurses for not having baby clothes (22 percent)...and nurses hit mothers during delivery (13 percent).” We don’t have enough information on how representative such examples are. Still, you could probably improve a system where the bureaucrats beat the beneficiaries.¹²

Coordination also undermines the potential gains from specialization and division of labor among aid agencies. Competition forces firms to find a niche in which their firm has an advantage over others. Firms realize these gains by motivating their own employees to specialize

¹² Bureaucracies in rich countries where clients don’t have much voice could be equally oppressive, like Customs or Immigration in the US. The US government during the Clinton Administration tried to make various agencies more client-friendly. According to an anecdote by John Nellis, the response of Customs officials to this initiative was “we don’t have clients; we have suspects.”

in narrow tasks. Countries, regions, and even city districts specialize in particular products, like Swiss watches, the carpet industry around Dalton, Georgia and the Manhattan diamond district.¹³

In contrast, aid organizations are notorious for trying to do it all. Even small bilateral aid agencies cover the whole spectrum of development topics, rather than focusing on a few. The IMF, World Bank, and regional banks all get involved in short-run financial crises, just as the IMF, World Bank, and regional banks all get involved in reducing long-run poverty. The aid agencies discourage staff from specialization – they prevent them becoming country experts by rotating them frequently among countries and regions. Knowledge of local history, politics, and languages (outside of French, Portuguese, and Spanish, and not even always that) is rare on country desks in aid agencies.

Ferguson 1994 has a devastating critique of a World Bank report on Lesotho. He lays bare the document as a generic product that got wrong the most elementary facts about Lesotho's economy and history (for example, the report portrayed Lesotho as an exotic land untouched by the modern market economy, when in fact it had been integrated into the South African mining industry for more than a century).

The result of all the donors doing everything is an incredible multiplicity of demands on the scarce administrative staff of the poor countries (more on this below). Tanzania had to produce more than 2,400 reports a year for the donors, who sent the poor country 1000 missions a year. (World Bank Africa Development Indicators 2002).

Such an extreme outcome of duplicated services is sometimes taken as a sign that there IS market competition among donors. Multiplicity should not be confused with competition. A competitive market would not lead to such an outcome. Many fast-food joints compete to serve me lunch; I choose one. The joint next door doesn't try to compel me to eat a second lunch. In a competitive market for foreign aid, one agency would "win the contract" to deliver a particular

¹³ I once was looking for a restaurant in downtown Manhattan for several city blocks and saw numerous "restaurant" signs but went away hungry; I had blundered into a district that produced only restaurant

service in a particular country, reducing rather than increasing the multiplicity of donors and projects. What is going on in aid is not competition among donors but many little monopolies operating simultaneously that tie disbursement of *their* money to the use of *their* bureaucracy. The monopolies have control of their own sources of funding (e.g. CIDA has money from the Canadian government, who are not going to give the money to the British DFID) and so don't really compete for funding. Hence CIDA, DFID and other aid agencies have every incentive to coexist, hence the cartel of good intentions.

A donor organization's sense of mission, then, relates not necessarily to economic development but to the commitment of resources, the moving of money. ... The estimates of total capital needs for development assistance in relation to supply seem to have been the implicit standard by which donor organizations have guided their behavior and judged their performance... the quantitative measure has gained its supremacy by default. Other definitions of success and failure of development assistance efforts have been hard to come by (Judith Tendler 1975).

Redefining output

The prediction of the story above is that aid bureaucracies respond to their high risk environment by producing observable outputs. Agencies redefine inputs to development as outputs. The primary output that foreign aid agencies advertise is the volume of money they disburse. This fits in with the campaign to estimate aid requirements of achieving certain goals.

World Bank President McNamara bragged about loan volume: "we proposed to double the Bank's operations in the fiscal period 1969-73 compared to the previous 5-year period 1964-68. That objective has been met...In the five years we achieved a level of operations that exceeded the total of all the operations that the Bank has undertaken in the developing world in the 23 years from 1946 through 1968." (McNamara 1973) Periodic IDA reports continued the stress on volume: "IDA lending to Sub-Saharan Africa rose from a level of \$950 million in ..FY80.. to over \$1.2 billion in FY83, while the share of IDA going to Sub-Saharan Africa rose from 27 percent to 37 percent." (World Bank 1983) As of the World Bank's report on aid in 1998, the stress on volume was said to have continued "Disbursements (of loans and grants) were

equipment.

easily calculated and tended to become a critical output measure for development institutions. Agencies saw themselves as being primarily in the business of dishing out money.” The World Bank’s IDA continued to define itself in terms of volume in 2001: “IDA, as the largest source of concessional assistance to the world’s poorest countries, plays a critical role in their efforts to achieve growth and poverty reduction.” A World Bank publication in 2001 advertised ten accomplishments of the organization – all ten involved volumes of assistance for different purposes.¹⁴ Although voices have been raised throughout the years against “pushing loans” and “moving money,” and change may actually have occurred, the continuity of stressing aid volume is more noticeable than the changes.

This emphasis on moving money had a number of consequences for the aid business. Since the weak institutions of the recipient were often the critical bottleneck in disbursing funds (more on this below), donors often substituted their own institutions for those of the recipient so as to keep the money flowing. As Tendler’s timeless 1975 study puts it: “much of the initiative and work involved in generating public projects in developing countries has been transferred gradually from its usual location – a country’s public sector institutions – to the lending institution.” Twenty-two years later the World Bank’s 1998 aid report echoed this claim: “Faced with low implementation capacity and pressure to ‘move the money,’ aid agencies have a long history of attempting to ‘cocoon’ their projects using free-standing technical assistance, independent project implementation units, and foreign experts—rather than trying to improve the institutional environment for service provision.” A World Bank 2000 report on Africa made an even more dramatic claim, after discussing different groups excluded from the development process, “Africa’s governments are one of the excluded groups: with high aid dependence, in many countries development policy is seen as being the prerogative of donors rather than governments.” In Tanzania in the early 1990s, donors were implementing 15 separate stand-alone projects in the health sector alone (Van de Walle 2001). An aid worker reported to me that

¹⁴ World Bank, *Ten Things You Never Knew About the World Bank*, 2001

Honduras has 57 different projects in the education sector as of this writing, and that the impoverished country was “floating in aid money.” This is an example of what Tendler 1975 called the paradoxical phenomenon of “aid abundance,” where donors want to give money faster than recipients can absorb it.

The emphasis on moving money led to IFIs allocating too little effort to two important activities: (1) insuring that loan conditions were actually observed, and (2) ex-post evaluation of loan effectiveness. Loan conditions were not effectively enforced because the IFIs kept coming back to the same countries with “adjustment loans” with little regard for the performance on previous loans. There was no progress on economic reform indicators from one adjustment loan to the next in the same country (Easterly 2002). The World Bank and IMF gave Argentina 33 adjustment loans over 1980-2001 during repeated macroeconomic crises, yet at the end Argentina went into an even more severe macroeconomic crisis than the previous ones (complicated by the huge debt now owed to multilateral institutions).

Ex-post evaluation receives very low priority in World Bank activities; the Bank reviews only 5 percent of its loans after 3 to 10 years following the last disbursement for development impact (Meltzer Commission 2000). The World Bank has done client surveys since the mid-1990s, but the results have not been made public and there seems to be little mechanism for having managers learn from them (Wade 2001). Aid agencies rarely engage in controlled experiments of particular interventions, despite the small amounts required relative to loan volume. They also show little interest in improving the atrocious statistical systems of the poor countries so that the aid agencies or recipient governments would even be able to know what is happening to growth, poverty, or social indicators. Aid agencies rarely engage in primary data collection and do not even store for future use the (secondary) data contained in their own country reports.

The Bush-Bono summit just before Mr Bush's announcement of more money for development exemplifies the photo-opportunity approach to development aid taken by most US presidents and politicians. (Moises Naim, Financial Times, April 1, 2002)

Observable output

The emphasis on safe observables leads to stress on other kinds of output as well, like international meetings of statesmen, glossy reports for the public, and the proliferation of framework and strategy papers. The standard response to any Third World tragedy is to hold a meeting about it. The World Bank evaluation of IDA activities in 1997 cited “the Interagency Task Force on an Enabling Environment for Social and Economic Development” that “followed up on two key conferences held during IDA10: the Copenhagen Social Summit (March 1994) and the Fourth World Conference on Women (September 1995). During FY94-96 IDA chaired ninety formal meetings and provided substantial input to thirty-eight formal meetings chaired by other donors.” Likewise UNDP in a recent report discussed its success at arranging meetings:

Trust Fund resources have been used to support the preparation and dissemination of social sector expenditure reviews in seven African countries...Five of these reports have already been finalized and a workshop has been or will be held to discuss their findings and recommendations. Preliminary findings of these studies were shared in three regional meetings, co-sponsored by UNDP and UNICEF, which served to sensitize policy-makers about the 20/20 initiative and prepare them for the international meeting which took place in Hanoi in October 1998.¹⁵

IDA’s 2001 draft document discussed the interlocking strategies and frameworks produced by different aid organizations, with an output by one organization often serving as an input to another: “the UN Common Country Assessment, the Bank’s Economic and Sector Work (ESW), and the IMF’s analytical and technical assistance work would contribute to governments’ analytical base for PRSPs {Poverty Reduction Strategy Papers}. {IDA Deputies} also welcomed the European Union’s decision to base its Africa, Caribbean and Pacific (ACP) assistance programs on the PRSPs.” In 2002 alone, the All-World Summit Tour includes the Monterrey Conference on Financing for Development, The Kananaskis¹⁶ G-8 Summit on Africa and the Millennium Development Goals, and the Johannesburg Summit on Sustainable Development. The Johannesburg Summit commemorates ten years of failure to follow through on the previous Sustainable Development Summit, which was held in Rio de Janeiro in 1992. Trying to make up

¹⁵ UNDP

¹⁶ rumored to be somewhere in Canada

for lost time, the UN in its preparatory documents for Johannesburg recommends 185 actions by rich and poor nations.

It is a lot easier for aid agencies to produce observable frameworks rather than actually implement risky programs like “empowering the poor” (risky because local elites would resist, as they do even in industrial countries). The aid agencies thus do not have to face hard choices between a number of competing claims on their scarce implementation resources, potentially alienating single issue lobbies that might influence aid revenues. This allows the frameworks to include a Christmas tree of aims like “an increased focus on issues like good governance at national and international levels and the fight against corruption, respect for all internationally recognized human rights, gender issues, capacity and institutional building, social services supply and environmental concerns” (UN Conference on the Least Developed Countries 2001) Likewise World Bank President James Wolfensohn set out his “Comprehensive Development Framework” in 1999 with a checklist of 14 items, each with multiple sub-items: ¹⁷

1. Good and Clean Government

“capacity building, an open legislative and transparent regulatory system, properly trained and remunerated officials ... corruption which is the single most corrosive aspect of development”

2. An Effective Legal and Justice System:

“the protection of human and property rights... an effective system of property, contract, labor, bankruptcy, commercial codes, personal rights laws ... that is effectively, impartially and cleanly administered by a well-functioning, impartial and honest judicial and legal system.”

3. A Well-Organized and Supervised Financial System

“Information and transparency, adequately trained practitioners and supervisors, and internationally acceptable accounting and auditing standards ... Regulation and supervision must include banking, savings institutions, insurance and pension plans, leasing and investment companies. Capital markets should also be developed and strengthened as resources allow.”

4. A Social Safety Net and Social Programs

“provision must be made for the elderly, the disadvantaged and disabled, for children, for the those men and women unable to find work, and those affected by natural disasters and the aftermath of war. In some transition economies, the social safety net is needed for those put out of work as a result of large-scale privatizations. ... special programs for indigenous people ... Violence and social unrest”

5. Education and Knowledge Institutions

“universal primary education for girls and boys equally, as well as an open and competitive system of secondary and tertiary education. ... Adult education, literacy and lifelong learning ... education of women and girls ... learn lessons of practice and history from indigenous peoples and communities... preschool education ... science, technology, and knowledge transfer.”

6. Health and Population Issues

“mothers are supported and that children get adequate health care before and during school years ... health

¹⁷ <http://www.worldbank.org/cdf/cdf-text.htm>

services for adults and elderly ... services for family health care and family planning. ... growth in population ... tuberculosis and malaria to AIDS”

7. Water and Sewerage

“an effective method of distribution, delivery, finding, and saving ... a strategy for sewerage”

8. Energy

“the use of wood and fossil fuels, resulting in health and breathing problems. Availability of power is not only an issue of convenience but saves the time of women searching for alternative fuels. The environmental impact is also great, it having been evident for centuries with forest destruction altering weather patterns and affecting the quality of air we breath.”

9. Roads, Transportation and Telecommunications

Rural and urban roads Trunk roads ... to link rural, urban and regional areas. Rail and air transportation systems ... telecommunications ... telephone or e-mail, computers or wind-up radios without batteries”

10. Sustainable Development, Environmental and Cultural Issues

“protection of our planetary environment ... biodiversity... the quality of our air and water.. degradation of important natural resources, like forestry, aquifers ... Cultural preservation is also crucial not only historic sites, artifacts and books, but also the spoken word and the arts”

11. Rural Strategy

“ new crops and agricultural extension programs ... {programs} for trading, for microcredit, for storage, for transportation, and for non-monopolistic outlets. ... technical assistance to farmers and converters of agricultural produce. Governments need to think of integrated solutions to rural development.”

12. Urban Strategy

“With 66 megacities of more than ten million people expected to be established in developing countries by the year 2025... governments must have an urban strategy”

13. Private Sector Strategy

“trade policy, tax policies, competition and regulatory policy, and corporate governance. .. a climate of investor confidence — with appropriate laws, transparent regulations, and predictable taxes. ... protection of property rights or fair and equitable labor practices, governments must give certainty to the investor about the "rules of the game". Provision of credit, guarantees, sources of funding for projects ...”

14. Special National Considerations

“ My purpose in suggesting an extra heading (or more, if necessary) ... is to give flexibility for specific country considerations.”

The CDF says these are additional items; governments should also worry about macroeconomic variables like GDP growth, price stability, sustainable government and external debt, a competitive real exchange rate, and adequate level of international reserves. The Comprehensive Development Framework calls simultaneously for “having all the basic prerequisites, say over a 20-year timeframe.”

Similarly the Millennium Development Goals calls for the simultaneous achievement of multiple targets by 2015, without asking if these arbitrary benchmarks are the most effective use of scarce resources to help poor people in every country, i.e. whether the cost-benefit ratios of attaining the various goals are approximately equal. Economics principles dictate that greater effort should go to goals with low costs and high benefits, and less effort to goals where the costs are prohibitive relative to the benefits. But the “do everything” approach of the MDGs suggests

that the aid bureaucracy is above such tradeoffs. Nor do the agencies spell out whether there are enough separate policy instruments to meet all of these separate policy targets simultaneously, or whether an overstrapped bureaucracy can manipulate these instruments in just the right combination to attain the targets.. Aid bureaucracies produce frameworks and goals to satisfy the imperative of visible output, as opposed to rational cost-benefit analysis or target-instrument analysis of what is effective assistance to the poor. Meanwhile, recipient government officials and the aid agency's own frontline workers are gradually driven insane by the proliferating conditions and objectives, each of which is Priority #1.¹⁸

There are more specific consequences of the emphasis on observable outputs. Aid reports for many decades have bewailed the tendency of donors to finance new capital investment projects (easily observable at a point in time) and the neglect of operating supplies and maintenance after the project is completed (which requires more costly ongoing site by site monitoring). Donors consistently refuse to finance maintenance, with the idea that this is the responsibility of recipient governments. The result is a recurrent theme of the World Bank's periodic reports on Africa: "Vehicles and equipment frequently lie idle for lack of spare parts, repairs, gasoline, or other necessities. Schools lack operating funds for salaries and teaching materials, and agricultural research stations have difficulty keeping up field trials. Roads, public buildings, and processing facilities suffer from lack of maintenance." (World Bank 1981) "in country after country, highways are falling into disrepair, if not disuse, from ... inadequate funding of maintenance." (World Bank 1983) "inadequate funds have been allocated to operations and maintenance... there are shortages of schoolbooks, medicines, transport fuel, small tools, and spare parts" (World Bank 1984) "road maintenance crews lack fuel and bitumen ... teachers lack books, chalk ... health workers have no medicines to distribute" (World Bank 1986) "schools are now short of books, clinics lack medicines, and infrastructure maintenance is

¹⁸ Several years ago, I read a World Bank report on Nigeria that listed 300 "main" recommendations at the beginning of the document.

avoided.” (World Bank 1989) “typically, 50 percent of the rural road network requires rehabilitation.” (World Bank 1995) “many countries suffer chronic shortages of current funding, especially for operations, maintenance, and nonwage inputs.” (World Bank 2000) As these quotes show, donors are very aware of the anti-maintenance bias but are seemingly unable to fix the problem. Filmer and Pritchett (1997) estimate that the return on spending on instructional materials in education is up to 14 times higher than the return to spending on physical facilities in a wide-ranging sample of poor countries, but donors continue to favor more observable buildings over less observable textbooks. In another field, Morton 1994 points out how donors were willing to finance hugely expensive but observable satellite early-warning systems for drought in Africa, allowing the inexpensive but unobservable system based on widely scattered rain gauges to fall apart. Aid agencies, themselves an example of top-down bureaucracy, tend to favor highly visible top-down bureaucracies to deliver services in poor countries, even though the conditions for effective bureaucracies are absent (Pritchett and Woolcock 2002).

Since the outputs that really matter are what is observable to the electorate in rich countries, aid agencies often strive to produce side effects for rich countries. Thus, rich country donors often restrict aid to purchases from their own country’s exporters (the infamous “tied aid”). Aid agencies are attentive to the need to reward political allies of the rich countries with aid. Such indicators as the frequency with which a recipient country votes with the donor in the UN and whether the recipient is an ex-colony of the donor can explain aid flows (Alesina and Dollar 2000, World Bank 1998). After September 11, 2001 there was anecdotal evidence of new aid resources for allies in the war against terrorism, like Pakistan and Turkey. The rich countries also contribute to proliferation of conditions by themselves imposing conditions on the multilaterals – Kapur 2002 notes that “IDA-13’s recommendations/actions total no less than 53 (one of which is ‘increasing selectivity’).” Of course, the loading down of aid with all kinds of extraneous rich country objectives makes it less likely to benefit the poor.

The inverse of donors' desire to produce observable positive outputs is their fear of producing observable negative outputs. Donors feel this more than ever in recent years with the increased success of non-governmental organizations (NGOs) in popularizing particular causes in the rich country media. For example, NGOs will blame donors for an aid project that produces visible environmental damage or does politically sensitive resettlement. Thus, for example, the World Bank got tremendous grief for supporting a Chinese project that would resettle poor Han farmers in an area considered to be a Tibetan culture area, eventually causing the Chinese government to withdraw the project (Wade 2001). The blame function is not necessarily related to actual economic costs of negative outputs, since poorly informed monitors will view all of an agency's activities as tarnished after even a small fiasco in one specific area. Prendergast 2001 points out that monitoring by poorly informed outsiders can have the perverse effect of diverting resources away from the objective of the organization towards avoiding visible mistakes (in his example, crime went up in Los Angeles after the department came under external pressure to curb police officers being too obvious about beating up suspects).

Something like this seems to have happened in the aid industry. The aid agencies are choosing increasingly elaborate control procedures to minimize the risk of visible negative outputs. The unfortunate officer on a World Bank country desk is required to produce or commission five separate reports on each client country: a Country Economic Memorandum (CEM)/Development Policy Review (DPR), Country Financial Accountability Assessment (CFAA), Country Procurement Assessment Review (CPAR), Poverty Assessment (PA), and Public Expenditure Review (PER). Four other reports are identified as "important in advancing the Bank's corporate priorities": Country Environmental Analysis, Investment Climate Assessment, Country Gender Assessment, and Financial Sector Assessment Program Report. Twelve other sector reports are mentioned in management guidelines as part of the "menu" but are mercifully optional.

Wade's (2001) insightful study of the World Bank describes the proliferation of NGO and US government pressures that has led the World Bank to adopt "safeguard policies" in the following areas: environmental assessment, natural habitats, forestry, pest management, resettlement, indigenous peoples, dam safety, projects on international waterways, and projects in disputed areas. That is, the beleaguered World Bank project manager has to certify that they are not doing anything wrong in any of these areas. This grab-bag of issues has no particular claim on being the most salient for welfare of the poor, they just happen to be politically visible concerns monitored by NGOs and American political lobbies.

Agencies' urge for increasingly baroque controls is restrained only by their adverse effect on the cost of producing positive output. Bureaucracies will trade off one against the other and wind up at higher cost for producing output than they would if they were just equating additional economic cost to additional revenue.

We constantly underestimate difficulties, overpromise results, and avoid any appearance of incompatibility and conflict, thus repeatedly creating the conditions of failure out of a desperate desire for success. (Daniel Patrick Moynihan, 1969)

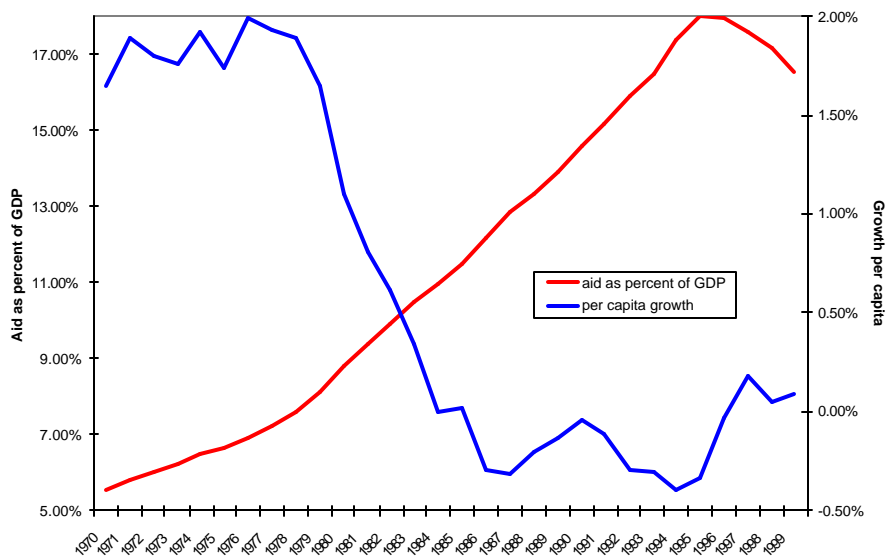
Spin control

The story of foreign aid bureaucracies suggested they will engage in a mixture of obfuscation and advertising. Carefully hedged diplomatic language is an art form in aid agencies: A war is a "conflict-related reallocation of resources" (World Bank Ethiopia report, 2001) Rich country aid efforts to anarchic warlords like in Liberia are "difficult partnerships" (OECD 2001) Countries with homicidal rulers are also known as "low income countries under stress" (World Bank 2002). Countries whose presidents loot the treasury experience "governance issues." Bad performance is "progress {that} has not been as fast and comprehensive as envisioned in the PRSP" (World Bank PRSP Sourcebook 2001). When government officials don't want what the aid agency insists upon, there are "differences in priorities and approaches {that}... need to be reconciled." Soliciting donations is "resource mobilization." Slums are "inadequate human settlements." Being clueless on the destination of debt relief means "continued progress on the

Expenditure Management and Control Program will be needed to maximize the benefits from the HIPC Initiative.”¹⁹ Other aid community jargon (like “good investment climate”) simply lacks any meaning that economic science can discover. You might as well say “the investment climate will be stormy in the morning, gradually clearing by afternoon with scattered expropriations.”²⁰ Aid documents often wander into content-free zones: “We encourage all international organizations to seek to continually improve their operations and interactions” (UN Monterrey Consensus 2002). As Tendler 1975 said, the aid professional has “a tremendous fear of his own writing.”

Another prominent technique of spin control is to assert that while things may have been bad in the past, things have now changed for the better. This technique is particularly prominent in Africa, the continent where foreign aid has had its most difficult hours. Foreign aid became increasingly important over the decades while growth deteriorated (Figure 2).

Figure 2: Aid and growth in Africa (10-year moving averages)



The World Bank did a steady stream of progress reports on Africa over the last two decades. They first described the poor state of African policy reform: “domestic policy

inadequacies...trade and exchange rate policies have overprotected industry, held back agriculture... “ (World Bank 1981) “unless major changes in African programs and policies are introduced, no amount of external assistance can generate rising levels of income” (World Bank 1984) “Weak public sector management has resulted in loss-making public enterprises, poor investment choices, costly and unreliable infrastructure, price distortions (especially overvalued exchange rates, administered prices, and subsidized credit)” (World Bank 1989) “most African countries still lack policies that are sound ... few besides Ghana come close to having adequate monetary, fiscal, and exchange rate policies...governments continue to intervene heavily in the marketing of export crops... the scarce evidence on public enterprise reform suggests that there has been no significant reduction in financial flows to public enterprises or in the volume of assets held by government...financial reform lags behind as well...nor is there much evidence that public spending within those sectors {health and education} is being reallocated away from costly tertiary programs and toward the basic services most likely to reach the poor.” (World Bank 1994) “While the former Zaire’s Mobutu Sese Seko was reportedly amassing one of the world’s largest personal fortunes (invested, naturally, outside his own country), decades of large-scale foreign assistance left not a trace of progress... Consider Tanzania, where donors poured a colossal \$2 billion into building roads over 20 years. Did the road network improve? No. For lack of maintenance, roads often deteriorated faster than they could be built... Zambia, for example, received 18 adjustment loans between 1966–69 and 1990–93 while its policies got worse” (World Bank, *Assessing Aid*, 1998) “the adjustment decades also saw a substantial deterioration in the quality of public institutions, a demoralization of public servants, and a decline in the effectiveness of service delivery in many countries.” (World Bank 2000) Africa in 2002 is still suffering from “the cruel effects of the HIV/AIDS pandemic, civil wars, and persistent low growth rates” (World Bank African Development Indicators Press Release April 11, 2002).²¹

²⁰ The President of the World Bank, April 2002.

²¹ See the discussion of aid’s failure in Africa in Kanbur 2000 and Van de Walle 2001.

The international community failed to hold aid agencies responsible for this failure. Instead, rich countries were influenced by aid agencies' perpetual promises of a change for the better in Africa: "Policy action and foreign assistance ... will surely work together to build a continent that shows real gains in both development and income in the near future." (World Bank 1981) "There is now evidence that many African governments are more clearly aware of the need to take major steps to improve the efficiency of productive sectors of their economies" (World Bank 1983) "This optimism can be justified by recent experience in Africa ... African leaders increasingly recognize the need to revise their development strategies...some countries are introducing policy and institutional reforms"(World Bank 1984) "progress is clearly under way. Especially in the past two years, more countries have started to act, and the changes they are making go deeper than before" (World Bank 1986) "since the mid-1980s Africa has seen important changes in policies and in economic performance" (World Bank 1989) "African countries have made great strides in improving policies and restoring growth" (World Bank 1994) "Since the mid-1990s, there have been signs that better economic management has started to pay off" (World Bank 2000) "Africa's leaders ... have recognized the need to improve their policies, spelled out in the New Partnership for African Development (NEPAD) ... {they} have pledged to pursue a compact of good governance with their people. " (World Bank African Development Indicators Press Release April 2002).²²

Such optimism (much of which staff knew was misguided according to interviews later conducted by Kapur et al. 1997) facilitated the continuing flow of resources to Africa.

²² The contradiction between "great strides in improving policies" and the continued description of bad policies calls to mind the story about the Japanese homefront during World War II. The long-suffering Japanese people could get their war news only from their government's propaganda. Nevertheless they could follow the war's course by tracking the location of the glorious victories of The Emperor's forces, which seemed to be moving ever closer and closer back to Japan.

Presidents have taken to reorganizations like overweight people take to fad diets -- and with about the same results. (James Q. Wilson 1989)

New and improved

Like laundry detergent, aid is always “new and improved.” One instrument for conveying this spin is the “reorganization” of the aid agency. The World Bank, founded in 1946, had its first reorganization in 1952. Further reorganizations came in 1972, 1981, 1987, 1991, and 1993 (Kapur et al 1997). World Bank President James Wolfensohn has carried out further large-scale reorganization since he took office in 1995. The US foreign aid effort was reorganized in 1948, 1951, 1953, 1955, and 1960, before USAID was finally created in 1961. Further changes in organization of US aid occurred in 1973, 1979, 1985, 1989, 1992, and 1999 (when USAID was moved back into the State Department). President George Bush in 2002 proposed an important new reorganization of the US aid effort with his Millennium Challenge Account.²³

A related spin is increased emphasis on a desirable “new” goal. Following the experience described above with adjustment lending in Africa, a hallmark of donor policy in the new millennium (enshrined in 2002’s so-called “Monterrey Consensus”) has been the new emphasis on “selectivity” of foreign aid, because “aid has a big effect on growth and poverty reduction” only in countries with good policies (World Bank, *Assessing Aid*, 1998). The World Bank in a recent report on aid effectiveness (World Bank 2002) stated that indeed, “during the 1990s, overall aid allocation shifted in favor of countries with good policies.” One’s enthusiasm at the sinner’s religious conversion is tempered only by knowledge of many previous conversions. The table shows that each of the latest donor fads has been around for some time.

²³ <http://www.usaid.gov/about/chronology.html>

Table 1: *Plus ça change, plus c'est la même chose*

<i>Aid idea</i>	Aid Epoch		
	<i>Stone Age</i>	<i>Iron Age</i>	<i>Silicon Age</i>
<i>Donor coordination</i>	"a cooperative enterprise in which all nations work together through the United Nations and its specialized agencies" (Truman 1949)	"Aid coordination... has been recognized as increasingly important..." (World Bank, 1981)	"{The donors need} to ensure better coordination and stronger partnership in ...development cooperation." (World Bank, 2001)
<i>Increasing aid volume</i>	"an increase in the per capita national incomes cannot be brought about without ... a sum of money ...of about \$3 billion a year" (UN Expert Group 1951).	"the current flow of ODA ... is only half the modest target prescribed by the internationally accepted United Nations Strategy " (World Bank President McNamara, 1973)	"If we are serious about...meeting multilateral development goals we have all signed on to, we must double ODA from its current level of about \$50 billion a year." (World Bank President Wolfensohn, 2001)
<i>Aid works in a good policy environment</i>	"objective No. 1: To apply stricter standards of selectivity ... in aiding developing countries" (President John F. Kennedy 1963)	"the relief of poverty depends both on aid and on the policies of the recipient countries" (Development Committee Task Force 1985)	"IDA should increase its selectivity ... by directing more assistance to borrowers with sound policy environments." (World Bank, 2001)
<i>Increase poverty emphasis</i>	"far greater emphasis on policies and projects which will begin to attack the problems of absolute poverty" (McNamara 1973)	"an even stronger emphasis on poverty reduction in IDA's programs" (World Bank 1990)	"increasing the focus ... on the overarching objective of poverty reduction" (World Bank, 2001)
<i>Country ownership</i>	Development policy is "the responsibility of the recipient alone" ("Partners in Development", 1969)	"novel approaches to community involvement in service provision" (World Bank 1981).	"greater national ownership of development programs ..." (World Bank 2001)
<i>Debt relief</i>	"the debt-servicing problem, already severe in the early 1960's, has {become} increasingly difficult" (World Bank 1970)	"more concessional reschedulings for the poorest debtor countries." (G-7 Summit, 1990)	"further national and international measures ... including, as appropriate, debt cancellation." (Monterrey Consensus, UN, 2002)
<i>Africa desperately needs reform</i>	"domestic policy inadequacies...trade and exchange rate policies have overprotected industry, held back agriculture..." (World Bank 1981)	"most African countries still lack ... adequate monetary, fiscal, and exchange rate policies...nor is there much evidence that public spending... is being reallocated ... toward .. basic services ." (World Bank 1994)	"{There was} a substantial deterioration in the quality of public institutions... a decline in the effectiveness of service delivery ... persistent low growth rates" (World Bank 2000, 2002)
<i>Africa is already reforming</i>	"many African governments are more clearly aware of the need to take major steps to improve the efficiency...of their economies" (World Bank 1983)	"African countries have made great strides in improving policies and restoring growth" (World Bank 1994)	"Africa's leaders ... have recognized the need to improve their policies, spelled out in the New Partnership for African Development (NEPAD)" (World Bank 2002)

Indeed, every successive aid document over the decades has called for increased “selectivity.” So the very latest document to solicit funds for the 13th replenishment of the World Bank’s concessional loan facility states “to improve development effectiveness, IDA should increase its selectivity ... by directing more assistance to borrowers with sound policy environments.” (World Bank, 2001) Thirty eight years earlier we have: “objective No. 1: To apply stricter standards of selectivity ... in aiding developing countries” (President John F. Kennedy 1963) “Above all, it is realized that ... that no foreign help will suffice where there is no national will to make the fundamental changes which are needed. It has become very clear that the impact made by contribution of resources from outside depends on ... his overall economic and social policy” (Pearson Commission 1969) “This report stresses that the relief of poverty depends both on aid and on the policies of the recipient countries” (Cassen Development Committee Task Force on Foreign Aid, 1985) “Donors...agreed to place greater emphasis on economic performance.” (Fleming and Smith 1987, IDA-8) “The Deputies underlined the importance of sound macroeconomic and sectoral policies as a basis for effective use of IDA funds in all recipient countries.” (Stern 1990, IDA-9) ““Even very well designed projects cannot succeed in a poor policy...environment.” (Wapenhans Report 1992, quoted in Meltzer Commission Report).

Well after the new emphasis on selectivity, in the summer of 2000, the World Bank and IMF announced new adjustment loans to President Daniel Arap Moi’s government in Kenya, despite 22 years of economic mismanagement during 19 previous adjustment loans to this same government. In a couple of weeks in the fall of 1999, donors made Cameroon among the first eligible for debt relief, and Transparency International declared Cameroon the most corrupt country in the world for the second year in a row (Van de Walle 2001). Indeed, since Van de Walle wrote, Cameroon reached the “decision point” on HIPC debt relief in October 2000 (meaning the World Bank and IMF thought it had a three year track record of good performance). Despite IFI enthusiasm, in 2001 Cameroon was still rated among the most corrupt countries in the

world by TI and was classified as one of the most undemocratic countries in the world (“not free”) by Freedom House. This unsavory combination would qualify the current government of Cameroon for the appellation of “odious” according to Birdsall, Williamson, and Deese 2002 (such an appellation implying no donor funds should go to it). To give a third example, the Bank made a second tranche disbursement of a financial sector adjustment loan to Peru in September 2000, despite well-documented reports of widespread corruption and the failure to keep the IMF agreement in place at the time.

More systematically, there is no relationship between the developing countries’ score on quality of governance (democracy, service delivery, regulation, corruption, etc.) in 2001 and those who received World Bank adjustment loans in fiscal year 2001. Moreover, I am unable to reproduce the World Bank report’s finding of greater selectivity in the 1990s, using the World Bank’s own numbers. There is no evidence of a significant positive association between good policies (using the World Bank’s own subjective rating, which was what was used to make the claims in the 2002 aid effectiveness study) and aid flows in the 1990s or at any other time:

Correlations of foreign aid (ODA) with World Bank country policy and institutional assessments (CPIAs)

Correlation of variable with CPIAs:	ODA/GDP	Log of ODA per capita	observations
1977	0.172	0.131	35
1978	0.167	0.086	37
1979	0.104	0.124	37
1980	0.006	0.111	41
1981	-0.162	-0.011	42
1982	-0.349 **	-0.247 *	42
1983	-0.420 ***	-0.357 **	42
1984	-0.241	-0.269 *	43
1985	-0.159	-0.182	47
1986	-0.060	-0.234	48
1987	-0.110	-0.141	48
1988	0.010	-0.076	49
1989	-0.002	-0.032	50
1990	-0.024	0.012	50
1991	0.026	0.024	49
1992	0.153	0.091	49
1993	0.173	0.113	51
1994	-0.084	0.091	51
1995	-0.040	0.081	55
1996	0.049	0.123	57
1997	0.063	0.141	57
1998	-0.028	0.072	57
1999	-0.079	0.136	50

***Significant at 1% level

**Significant at 5% level

*Significant at 10% level

Correlation performed on sample of low income countries

World Bank (2002) makes strong claims for selectivity of the of the World Bank's own foreign aid (IDA loans). These loans show somewhat more association with policy ratings (again the same CPIA ratings that the World Bank report uses) than does overall ODA, but this association is not robust across years or across definitions of the IDA flow (as percent of the receiving countries GDP or as amount per capita):²⁴

²⁴ On the failure of the World Bank and other donors to enforce "selectivity" and "conditionality", see Kanbur 2000, Van de Walle 2001, Kapur et al 1997 and Lancaster 1999.

Correlations of IDA lending with World Bank country policy and institutional assessments

Correlation of variable with CPIAs:	IDA net disbursements/GDP	Log of IDA net disbursements per capita		observations
1980	-0.028	0.086		54
1981	-0.143	-0.080		53
1982	-0.217	-0.359	***	53
1983	-0.070	-0.112		50
1984	0.147	0.037		50
1985	-0.024	-0.046		55
1986	0.153	-0.151		59
1987	0.027	-0.025		59
1988	0.103	0.207		57
1989	0.103	0.214		54
1990	0.079	0.119		54
1991	0.116	0.354	***	57
1992	0.166	0.304	**	59
1993	0.089	0.154		61
1994	0.063	0.345	***	67
1995	-0.054	0.138		66
1996	-0.023	0.141		68
1997	0.119	0.208	*	71
1998	-0.031	0.043		70
1999	0.185	0.253	**	71

***Significant at 1% level

**Significant at 5% level

*Significant at 10% level

Correlation performed on sample of positive IDA net disbursements

Of course, the “improved” behavior could have happened more recently than is captured by the available data. The aid agencies’ always presenting themselves as “new and improved” makes spin control easier, in that it is impossible to test how “improved” they are at any given moment. One can do research on the past but not on the present.

{The program} failed... to wage an effective war on poverty. Many battles were fought, but few were against poverty. (Congressman James Hanley, 1967, quoted in Moynihan 1969)

Why it takes \$3521 in aid to get \$3.65 to a poor person

The “new” emphasis on poverty is also continually reinvented. The creation of the International Development Association (IDA) for the poorest countries in 1960 reflected an early

concern with poverty. World Bank President McNamara came along in 1973 to “to place far greater emphasis on policies and projects which will begin to attack the problems of absolute poverty” (McNamara 1973, IDA-4). Despite his best efforts, each new round of replenishment of the IDA called for more: “...a growing proportion of lending is directed to combating poverty.” (1980, IDA-6) “...The Deputies encouraged an even stronger emphasis on poverty reduction in IDA’s programs” (Stern 1990, IDA-9) “the poverty focus of CASs {Country Assistance Strategies} should be enhanced.” (IDA-12, 1998) “increasing the focus of IDA and IMF concessional assistance on the overarching objective of poverty reduction” (IDA-13, 2001)

The World Bank’s latest aid report (World Bank 2002) combining the new poverty focus and the newly selective aid claims that “an extra \$1 billion in ODA would lift more than 284,000 people out of poverty.” This claim has been prominently featured in the press coverage of the report and has been repeated in other aid agencies reports on “aid effectiveness” (for example, Her Majesty’s Treasury 2002). Parsing out the logic of this statement makes clear that such claims are more about spin than substance. The additional aid spending per person lifted out of poverty is \$3521. Poverty is defined as less than \$365 a year. According to the way the statement says the aid would be distributed, it would increase aid receipts in recipient countries by at best no more than 2 percent of GDP (in most cases, much less). The World Bank’s Assessing Aid report says that 2 percent of GDP in aid raises growth by 1 percent in good policy countries (again an overestimate in this case because the World Bank’s old and new aid reports say not all aid is going to good policy countries). The World Bank’s Globalization policy research report says that 1 percent of overall GDP per capita growth raises the growth of the poor’s income by an equivalent 1 percent. So following the logic of the various World Bank public statements, the effect of the \$3521 in additional aid per person lifted out of poverty is at best to raise the poor’s annual income by \$3.65. Spending \$3521 per poor person to increase their income by \$3.65 does not seem like the world’s biggest bargain. Apparently, the World Bank report authors did not

follow through the logic of their various claims to this absurd conclusion.²⁵ Obviously, aid has other objectives than helping a destitute person stagger across the \$365 finish line out of the poverty headcount. The emphasis on public relations numbers weaves tangled webs for the aid agencies.

Still it is convenient to spin the activities of aid agencies so they are seen to contribute to some socially beneficial goal. Aid agencies can mobilize the current enthusiasm for debt relief to highlight their “new” benevolence towards heavily indebted poor countries (HIPCs): “Deputies reiterated their strong support for the HIPC Debt Relief Initiative and the enhanced framework which is providing broader, deeper and faster debt relief to the world's poorest and most indebted countries.” (World Bank, IDA-13 replenishment, 2001) This is a much better spin than admitting that previous aid loans are uncollectible because of poor results, even in such success stories as Ghana and Uganda (nevertheless the World Bank 2002, with impressive chutzpah, gives IDA’s recollection rate on loans as evidence for aid effectiveness). There is also little mention that debt relief has been needed on many previous occasions. In the 60s and 70s, “the debt-servicing problem, already severe in the early 1960’s, has made it increasingly difficult for such countries to prudently finance their development with loans on conventional or near-conventional terms. To raise or even maintain their rate of economic growth, these poorer countries must obtain an increasing proportion of the external financial assistance they need on concessionary terms.” (International Development Association 1970) Debt problems for poor countries and creeping debt relief continued throughout the 70s, 80s and 90s (Easterly 2001).

The 1996 HIPC debt relief initiative was to provide “exit, once and for all, from the rescheduling process” and to enable the countries to resume “normal relations with the international financial community, characterized by spontaneous financial flows and the full

²⁵ While these reports had some differences in authorship, all of them were supervised by the same managers.

honoring of commitments.”²⁶ Only three years after this “once and for all exit” the IMF and World Bank found it necessary to introduce “Enhanced” HIPC Debt Relief, providing yet further relief. As of this writing in April 2002, the IMF and World Bank have a new report saying that 8 to 10 countries (including such success stories as Bolivia and Uganda) will need additional debt relief even after graduating from “Enhanced” HIPC.²⁷ Calling debt relief “new” at each moment avoids embarrassing questions on what happened to make previous assistance in need of yet further debt relief.

The socially concerned intellectuals...seemed repeatedly to assume that those who had power would let it be taken away a lot easier than could be possibly be the case if what was involved was power. (Daniel Patrick Moynihan 1969)

Power to the poor

A similar story applies to another “new direction” in foreign aid policy, which is home-grown development, known as “country ownership”, “partnership,” “beneficiary participation”, “community-driven development (CDD),” “empowering the poor,” “consultation of stakeholders,” and “bottom up development.” The process of the country preparing a Poverty Reduction Strategy Paper (PRSP) is described as a means to this goal by the World Bank and IMF in 2001: “the PRSP ... was a crucial step towards greater national ownership of development programs which is essential for increased effectiveness of external assistance.” (World Bank 2001, IDA-13) “The broadest and most fundamental changes to the work of the IMF arise from the fact that the targets and policies embodied in {IMF}-supported programs will emerge directly from the country's own poverty reduction strategy.”(IMF 2001) Actually, every foreign aid program since Truman has stressed poor countries’ developing “through their own efforts” (Truman 1949), emphasizing “self-help” (Kennedy 1961), that development policy is “the responsibility of the recipient alone” (“Partners in Development” report—whose title speaks for

²⁶ P. 126, 129 Boote et al. 1997.

²⁷ Nor is the story over even then, as independent analysts like Birdsall, Williamson, and Deese 2002 point out that there remain heavily indebted poor countries outside the program like Indonesia, Nigeria, and Pakistan. Birdsall et al. also project that more of the existing HIPC countries will need relief beyond the 8-10 cited in the new IMF/World Bank report.

itself, 1969), and that agencies should choose “novel approaches to community involvement in service provision” (World Bank 1981). Indeed, the rhetoric of involvement of the recipient is familiar at least since the 1960s War on Poverty in the United States, which called for the “maximum feasible participation” of the communities being helped (immortally satirized by Moynihan 1969 as “maximum feasible misunderstanding.”)

A report from thirteen years ago “sets out a range of proposals aimed at empowering ordinary people, and especially women, to greater responsibility for improving their lives—measures that foster grassroots organization, that ... promote nongovernmental and intermediary organizations. The growing conviction is that development must be more bottom-up less top-down” (World Bank Africa report, 1989). A report eight years ago asked “how can the effectiveness of aid be increased? ...provision of technical assistance designed to so as to enhance, rather than undermine, local capacity ...increased systematic client consultation, and incorporation of the beneficiary viewpoint into program design and implementation.” (World Bank 1995)²⁸

Despite all this rhetoric, we saw earlier that donors often violate national sovereignty with their own rapidly proliferating agendas.²⁹ Moreover, pressures to “move the money” often caused donors to substitute their own institutions for those of the recipient country, despite good intentions on fostering self-reliance. There are some signs that the same is happening with the “new” PRSP process. Since the international financial institutions (IFIs) decided the preparation of a PRSP was necessary to receive debt relief under the HIPC program, pressure on the country to rapidly produce a PRSP was intense – leaving little time for “consultation with civil society” (actually in the event, IFIs agreed to accept an “interim PRSP”). Surveys of the “civil society” that the government was supposed to consult turned up reports of PRSPs being prepared in

²⁸ See Kanbur and Sandler 1999 on the sorry record of “country ownership”

²⁹ To put this in perspective, think of whether the United States would have been willing to have international agencies or foreign governments dictate its policies or institutions at any point in American

English in non-English-speaking countries, and even “in some cases, the rush was such that the IFIs simply took over the task of writing the PRSPs in a way that it would meet the approval of the Boards in Washington.” (Jubilee South 2001). In Honduras, the government presented its PRSP draft to the IFIs before showing it to its own national legislature. (Catholic Relief Services 2001) In Bolivia, the first draft of the PRSP was written in part by an American consultant in Paris.³⁰ Subsequent redrafting was done by a small team of Bolivian officials who bypassed the government’s own pre-existing National Dialogue on poverty relief. In Cambodia, the PRSP paper is being prepared by 10 foreign consultants with guidance from the World Bank; the government has little involvement.³¹ In Tanzania, the government had already devised a National Poverty Eradication Strategy in consultation with Parliament, but the IFIs insisted upon a new process for the PRSP. Because of “the urgency with which they wanted to secure HIPC relief; the Tanzanians initially acquiesced in the World Bank writing the I-PRSP for them.” (Grusky et al. 2001) Even in the cases where governments did prepare the PRSP themselves, the Ministry of Finance took the lead with little participation by line ministries or local governments – possibly motivated by simply fulfilling a requirement to get donor funds (World Bank Social Development Department 2002). Moreover, other aid organizations like the Asian Development Bank and the largest bilateral aid agencies (US and Japan) have not adopted the PRSP, despite it being a “crucial step” for “increased effectiveness of foreign assistance.”

Some of the sources cited have their own biases against the IFIs and it is impossible to say how much such anecdotes are representative of the new PRSP process. There have also been some positive reports of increased participation by civic organizations in determining government policy and donor programs.

history. The most famous case of “foreign aid” to the US happened early in American history with French military support to the American revolution – but remember George Washington was in command.

³⁰ Personal communication between the author and that consultant.

³¹ WIDER 2001 and private correspondence with donor official on Cambodia.

However, even if civil society prepared the document with participation by everyone and their cousin, how a bureaucratic document can redistribute power from those who have it to those who do not is left unexplained. They might as well say “may the force be with you.” For example, the World Bank and IMF awarded a second round of debt relief to Burkina Faso in April 2002 based upon the satisfactory completion of a participatory PRSP.³² It would be interesting to know more about how much the poor were newly empowered in a one-party state that has been in power since 1987, which was in the worst fifth of the world in corruption in 2001, and which supported rebel warlords that perpetrated tragic atrocities in Sierra Leone, Liberia, and Angola.

Similarly, the poor in Tajikistan must have wondered about how President Emomali Rakhmonov managed to satisfy the World Bank and IMF that he had completed an Interim PRSP in the fall of 2000 that laid the groundwork for a “participatory” PRSP. President Rakhmonov, in power since 1992, has presided over an authoritarian government whose rule has featured years of civil war, ethnic conflict and favoritism, political repression, continuing violence, extrajudicial killings, disappearances, torture, arbitrary arrests by the security forces, and trafficking in women and children.³³ The World Bank and IMF praised Tajikistan’s government in 2002 for a “more open dialogue” (IDA and IMF 2002).

In Bureaucracy World, there is no politics. Participation is an apolitical technical process of consulting the poor. The IFIs assume away the political combat between polarized classes, regions, or ethnic groups that is the stuff of everyday life in both rich and poor nations. The IFIs assume that political strongmen like President Rakhmonov will cheerfully give some of their power away to the poor, doing what the poor want instead of what President Rakhmonov wants, all through the magic of writing a Poverty Reduction Strategy Paper.

32

<http://inweb18.worldbank.org/news/pressrelease.nsf/673fa6c5a2d50a67852565e200692a79/6b834179b3fd616b85256b990077a8a7?OpenDocument>

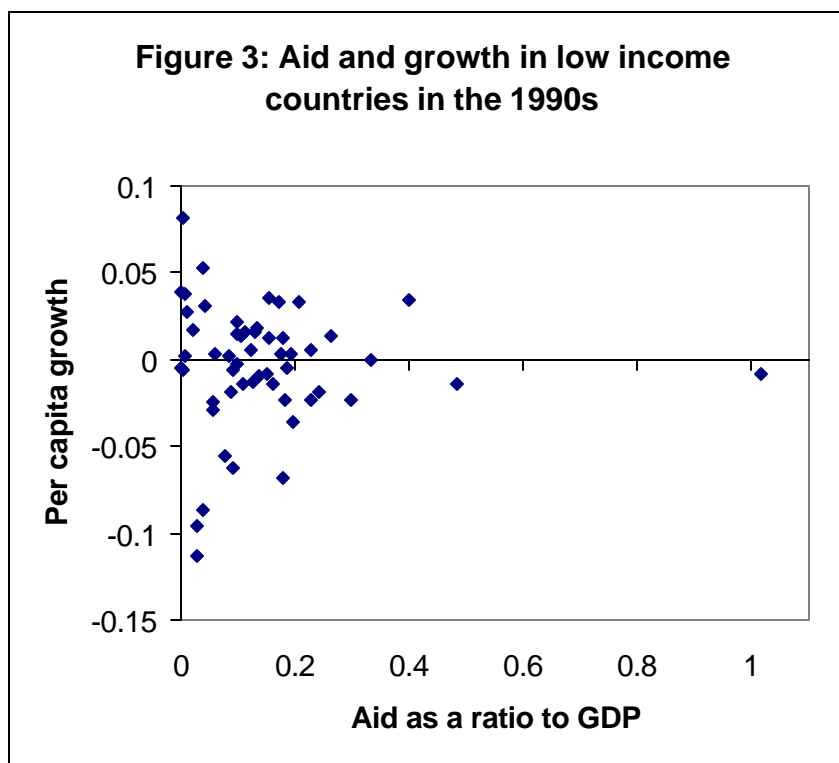
The participation chapter of the World Bank's PRSP Sourcebook provides a useful benchmark. Nowhere does it mention the possibility that the poor might have different interests than the political elite, nor that different groups among the poor might have conflicting interests. The chapter presents the poor "stakeholders" as an abstraction, much like Marxists used to cite "the masses" as the justification for their revolutionary activities. When the chapter mentions diversity among the poor at all, it is merely a complicating factor in gathering information on the poor's circumstances and in the dissemination of the "consensus" somehow achieved. For example, the chapter cites the example of Uganda, whose autocratic government helpfully translated its Poverty Eradication Action Plan into 5 languages. The chapter does not mention the possibility that, as Ferguson's (1994) brilliant case study of an aid project in Lesotho shows, organs for "participation" can often be captured by an authoritarian state. The participation mantra does not address what to do when society and politics are badly polarized along regional or ethnic lines, where it is very difficult for foreign aid to maintain neutrality. For example, Herring's (2001) study of the Mahaweli irrigation project in Sri Lanka shows that aid in this case exacerbated the Tamil-Sinhalese tensions that fueled the ongoing civil war.

Aid success stories

When the aid agencies do report on the past, they report on whoever was successful and claim some credit for the success. For example, the World Bank (2002) offers six aid success stories: China, India, Mozambique, Poland, Uganda, and Vietnam. This is a somewhat surprising list, since China and India receive little aid relative to their GDP (0.4 % and 0.7% of GDP respectively in the 80s and 90s, which is the period the World Bank study mentions). Poland and Vietnam are also below average recipients of foreign aid, even if we ignore the periods before recent reforms when they got no aid. And there is a little irony in highlighting two of the world's few remaining Communist party dictatorships (China and Vietnam) as a triumph of aid from

³³ Freedom House rated Tajikstan as "not free" from 1992 to 2000. The US State Department Human Rights Report 2001 mentions the human rights violations cited here.

Western capitalists!³⁴ Of course, the reason for selecting these countries is not such a mystery: China, India, Mozambique, Uganda, and Vietnam are the fastest growing low income countries in the 1990s (which is the period the World Bank focuses on for all but China and India), except for #3 Sudan that the World Bank apparently didn't want to celebrate. Poland is the fastest growing transition country. It's not convenient to point out that as many aid-receiving low income countries had negative per capita growth as positive, or that most aid-receiving transition countries were a disaster in the 1990s. Among all low income countries, there is not a clear relationship between aid and growth (Figure 3).



Longer term success stories are not that easy to come by. The aid agencies had often mentioned Ghana as an African success story since reforms started in 1983, but recent struggles have apparently dropped it from the list. World Bank 2002 mentions South Korea and Botswana as long term success stories (again apparently selected by virtue of their near world-record growth rates over the past four decades). Although many other African countries received more,

³⁴ Milanovic points this out.

Botswana did receive significant amounts of aid during its period of rapid growth. Unfortunately, a study for the World Bank's Operations Evaluation Department found that Korea's growth accelerated only after the decline in US aid, and did so following policies contrary to the advice of US aid officials; hence, the consensus of most studies of Korea is that aid contributed little to Korea's takeoff (Fox 2000).

Spin control can also gloss over the contradictions in the different efforts of the aid agencies. So the contradiction between "country ownership" and greater "selectivity" (as the IFIs decide which "country-owned" policies to select) goes unremarked. The contradiction between "participation" and the imposition of the PRSP process by the IFIs (who determine when the recipient has "participated" enough to satisfy them) goes unremarked. The tradeoffs between targets set out in the Comprehensive Development Framework and the Millennium Development Goals – say between faster poverty reduction and greater environmental protection -- also escape mention. The answer is "do everything." In aid agencies, there are no second priorities and there are no conflicts between competing goals, much to the chagrin of the unfortunate frontline workers who have to implement "everything."

You can't learn how to do it from a slogan that tells you the way to get you want is to already have it. (Pressman and Wildavsky 1984)

The New Amnesia

The examples above of a "new" initiative that repeats many previous initiatives reflects the lack of historical memory in the aid community. As described above, the aid community does not want to critically examine the past because doing so might lead to negative publicity of past failures, threatening the ability to raise new aid revenue. Ironically, the unwillingness to shine light on past failures makes new failures more likely. The reluctance to report on the past short-circuits the process of cumulative learning by doing that is essential to the success of any activity. As Isaac Newton said, "if I have been able to see so far, it is because I have stood on the shoulders of giants." The aid bureaucracy does not want to stand on their predecessors' shoulders and so does not see far. The eminent authors of a well-received two-volume history of the World

Bank in 1997 (commissioned by the World Bank at considerable expense for its 50th anniversary, Kapur et al 1997) were never invited to give a lecture on their findings within the World Bank.

A comparison with the academic community is apt. Academic papers are only published if they generate new findings. Papers subject to this competitive process cite previous studies and make clear their incremental contribution. In contrast, studies produced in the cartel of good intentions often duplicate one another and repeat the themes of previous studies without citation (sometimes because they are unaware of the previous studies). Klitgaard 1990 gives the example of a World Bank agriculturalist recommending a cut in cocoa taxes, despite not having had the time to read four previous World Bank reports on cocoa production in Equatorial Guinea. A USAID consultant recently gave me the example of a large mission that had produced a report on corruption in Uganda in 2001, unaware that a British team had produced a report on the same topic six months earlier. World Bank reports often repeat the same recommendation for many years, without analyzing what had gone wrong with previous recommendations. For example, an independent consultant had pointed out financial problems in Kenya Railways as long ago as 1972. World Bank reports repeated the recommendation to restructure or privatize Kenya Railways numerous times, such as in 1983, 1989, 1995, 1996, and 2000, each time failing to point out the previous history of failed recommendations. Similarly, World Bank reports on Kenya repeated a recommendation for increased funding for road maintenance in 1979, 1983, 1989, 1994, 1996, and 2000. The World Bank 1998 noted that in Kenya “the World Bank provided aid to support identical agricultural policy reforms five separate times.” The sheer repetition of adjustment loans to countries with poor track records, like Kenya’s 21 World Bank and IMF adjustment loans as of the year 2000, reflects the same historical amnesia.

There is little effort in aid agencies to collect case studies of adjustment programs, projects, and sectoral programs, and to use these case studies to inform current management and staff what mistakes to avoid and what more successful methods to repeat. For example, the chapter on macroeconomic adjustment in the World Bank’s PRSP Sourcebook does not mention

the conclusions of many observers that structural adjustment lending was a failure.³⁵ Similarly, the chapter on rural poverty does not mention the record of general failure of integrated rural development projects, or even the lessons of their occasional successes (as set out in for example in Tendler 1993). The World Bank had an expensive program of sending managers for six-week intensive training at the Harvard Business School. They would have done better just to send the managers to the World Bank's own library and document archives, where they could read case studies of projects failing and (sometimes) succeeding.

They might have benefited from reading a case study like Ferguson 1994, which describes a CIDA project to help farmers in the mountains of Lesotho to gain access to markets and develop modern methods of livestock management and cash crop production. The only problem was that the beneficiaries did not consider themselves "farmers" since they mainly depended on migration to jobs in South Africa, and they already had access to markets, where they had long since learnt that cash crop production was not competitive given the region's poor agricultural conditions. Ferguson 1994 describes how the main long run effect of the project seemed to be the creation of a new administrative center and army garrison that strengthened government control over what had been an opposition stronghold.

Similarly, the Bank might have learnt from the failure of its \$25.6 million Institutional Development II project in Malawi, which ended in June 2001. Despite training 1584 officials and providing computers and manuals, an internal review concluded that the project did not improve the efficiency or effectiveness of civil servants. It also failed to prevent such incidents as the disappearance of the government's grain reserve, apparently sold for the benefit of government parties unknown, which according to latest reports is threatening some Malawians with famine in 2002. Similar insights might be gained from the study of the Bank's \$28 million health project in Haiti, which ended in March 2001. An internal review concluded the project

³⁵ see Kanbur 2000, Van de Walle 2001, Kapur et al 1997 and Lancaster 1999. For a poignant description of the structural adjustment fiasco in Zambia, see Ferguson 1999.

failed to attain most of its objectives, including control of AIDS and TB. Health conditions did not improve in Haiti over the life of the project, perhaps compromised by political instability and the lack of interest in the Ministries of Finance and Health in the project. Even in a more politically stable states like India and Mexico, a Bank shrimp-farming project that ended in 2000 failed to improve the well-being of its intended 14,000 very poor Indian beneficiaries, while a 1994-2000 Bank project on solid waste management in Mexican municipalities failed to make any progress on expanding modern sanitary landfills..

Perhaps the Bank managers could also learn from even more surrealistic projects as the \$45 million Roads Rehabilitation and Maintenance Project in Sierra Leone, disbursed in the middle of brutal civil war during 1998-2001. About 33 percent of the credit went to compensate contractors for lost time and destruction of their civil works. The rationality of financing infrastructure that is simultaneously being destroyed by rampaging armies is not immediately apparent.

Of course, there are more successful projects in the Bank's portfolio, like the \$70 million loan to Ceara state government in the Brazilian Northeast concluded in June 2001, where high commitment by the government led to innovative initiatives in land reform, rural electrification, and water supply. In fact, most projects in the Bank's portfolio are rated as "satisfactory" by the (somewhat-less-than-independent) Operations Evaluation Department. What is sad is that there seems to be little effort to draw lessons from successes and failures to inform future efforts, either in the World Bank or in other aid agencies.

It is far easier for would-be reformers to change the formal structure of an institution than to change its practices. Redesigning the lines and boxes in an organizational chart is simpler than changing how that organization in fact operates. Changing the rules and regulations is simpler than eliciting behavior that conforms to them. (James Scott, 1998, p. 255)

The funnel

It is a paradox of foreign aid that it demands the most from bureaucracy under the conditions in which bureaucracy functions worst. Aid bureaucracy has to operate with little

effective feedback, as mentioned earlier, and must contend with severe skill shortages in the recipient countries. Yet aid bureaucracy tries to manage aid through a hierarchical top-down process.³⁶ Even though top managers are overwhelmed, individual agents in aid agencies continue to refer back to the same center of power for authorization of their actions.³⁷ The center is sometimes within the larger assistance agencies like the World Bank or IMF, where the recipient government is weak and other donors are small (as in most African countries). Sometimes a bilateral aid agency will take the lead when it has an especially large program in a country, like USAID in Egypt. In large countries with strong governments, like India, the recipient government becomes the center. Even where the center of power is de facto in aid agencies, agencies try hard to get formal approval from the recipient government of all programs and projects.

Given the multiple goals and procedures described earlier, consistent with the urge to produce visible outputs and avoid visible fiascos, the center is the chokepoint for aid. Frontline staff in aid agencies can barely keep up with the flood of mandates, political pressures, procedural requirements, and authorizations required to keep the aid money flowing. In the recipient government, the relative burden on the management is even greater, given the scarcity of skills, the extreme political pressures in factionalized societies, and the prevalence of red tape and corruption.³⁸ Aid agencies fluctuate between taking over administration themselves and trying to nurture “country ownership,” as discussed above. In any case, the implementation of aid projects through the frontline bureaucracy becomes the choke point of the whole process. The mighty river of aid must pass through a very small administrative funnel.

It is not surprising that in a country like Ethiopia one major donor noted a “slow pace of disbursement,” which is due to “capacity constraints” at both the government and donor level.

³⁶ See the excellent description by Morton 1994.

³⁷ There is of course a huge literature on the shortcomings of central planning. F.A. Hayek was an early critic, although long dismissed as an ideologue. James Scott’s important book (1998) is wonderfully insightful about many real-world planning fiascos (interestingly, Scott appears to come from almost the opposite ideology of Hayek).

³⁸ Tandler 1975 has a very good description of this process, which remains timely today.

This in turn led this donor to emphasize “capacity building” as the “major cross-cutting theme” of its development assistance (European Union 2001). Capacity building has been a theme of donor recommendations since forever, although it continues to exert its fascination in the latest reports (it is point #5 in the World Bank President’s 2002 seven point Agenda for Action After Monterrey). There is a certain irony in donors increasing the pressure on the government’s managerial capacity through donor red tape and then turning around and trying to satisfy their own demands through “capacity building.” No amount of “capacity-building” seems likely to relieve the severe managerial bottlenecks to the foreign aid process.

It does not really address the problem to call for increased “results-based” evaluation of aid agencies. Centralized monitoring and evaluation (M&E) just becomes one more activity imposed on the frontline staff, adding to the pressure on the funnel. M&E is central planning with output targets. M&E has already been a part of many World Bank projects, without much effect. Morton 1994 pointed out that “vast sums of money and unbelievable levels of technical complexity have been expended to make Monitoring and Evaluation ... into a functional tool... World Bank representatives did not quite admit that they had spent \$40 million, of money lent to the Nigerian government for Monitoring and Evaluation, to very little effect.”³⁹ Moreover, bureaucracies can manipulate quantitative indicators of performance to achieve “success” without real quality improvements.⁴⁰ (This is different from evaluation for the sake of learning lessons for future practice, like control group methodology for particular interventions.)

³⁹ A more recent example is the World Bank-supported Social Action Program in the 1990s in Pakistan, where numerous “results-based” targets were set for the health, education, and rural water supply sectors. Performance was so unsatisfactory that the program had to be redesigned halfway through (SAP II replaced SAP I), and then performance of the redesigned program was in turn unsatisfactory.

⁴⁰ The World Bank’s Poverty Reduction Strategy Sourcebook (2001) gave the example of the target to reduce the backlog of cases waiting to be treated in Britain’s nationalized health service. Administrators put pressure on doctors to treat less serious cases first, because those could be treated more rapidly and thus bring down the backlog more quickly. Another famous anecdote is the condition that the Australian government gave for disbursing aid to parks in aboriginal communities, that the communities keep the lavatories clean. The communities easily met the condition by cleaning the lavatories once, and then padlocking them.

Aid agencies do not face incentives to economize on the very scarce administrative resources in the recipient governments or even in their own front line staff. They instead have the incentive to keep producing the visible frameworks and strategies and procedures (all above the funnel). The river of aid keeps flowing, but effective benefits dribble slowly out of the bottom of the funnel.

Is it too strong to suggest that the way to show true respect for ... the people of developing countries as a whole is not to involve them in some condescending and patronizing “partnership” but merely to leave them alone, in the confidence that they do have the necessary strengths and abilities to make their own choices? Would the more appropriate outsider role not be to spread the wares of outsider knowledge and allow rural people to choose for themselves what they think would be useful? (Morton 1994)

Brainstorming about markets instead of bureaucracy

Given all the perverse incentives faced by bureaucracy in delivering foreign aid, is there a better way? It is time for some brainstorming about market mechanisms for foreign aid. Consider how a goods market succeeds in matching those who need something with those who want to supply it. There is no center coordinating such matches, there is no monopoly power of suppliers to restrict supply and to raise the price, there is no administrative funnel through which all matches must pass, there is no pressure for the supplier to produce visible results, there is no pretense about simultaneously satisfying contradictory goals, there is no obscurity about what the demander really wants – no matter how unobservable those wants. The market has no central administration or planning; it achieves its results by the decentralized actions of a myriad of participants. The market clears by adjusting the price of the goods to match the quantity of goods offered with the quantity of goods demanded. The demander of the goods trades off her various needs against each other at the relative market price, which reflects the opportunity cost to the supplier of producing the good.

Some markets work through intermediaries. Retailers and wholesalers match producers of consumer goods with demanders of those goods. Financial markets have banks matching suppliers of savings with loan demanders who want to invest those savings, or brokers matching

suppliers and demanders of bonds and equities. Insurance companies match those who want to hedge against risk with those who want to take risks for a profit. Intermediaries lower search costs for suppliers and demanders. The risk that an intermediary will take the money and run is controlled by the need for intermediaries to maintain their reputation for repeated transactions and by supporting institutions that collect information on the historical behavior of each intermediary and punish intermediaries who misbehave.⁴¹

How would markets work in foreign aid? We can imagine intermediaries that arrange decentralized matches between those who want to help the poor and the poor who want help to improve their future. But how would a “price” clear the market? Think of stock certificates, which facilitate impersonal matches between investors and firms, with the price reflecting the confidence of the investor in the firm. An analogy is an “aid voucher” given to the poorest parts of the population in poor countries. The vouchers could be given either to individuals, households, or communities, depending on social structure in the recipient society. Part of new or existing aid money would back the vouchers with an amount of funds equal to their face value. The poor could turn in the vouchers at any national, international, nongovernmental, or even private development agency to receive development services. The agency could then turn in the vouchers at the central voucher fund, who would give the agency a corresponding increase in its budget. The poor would then choose how much of their vouchers to spend on any given development service, and each development agency would decide whether they can supply the service at that “price.” The intermediaries would scout out opportunities to assemble blocks of vouchers for a given development service, like roads, health clinic, drugs, school, textbooks, water supply, sanitation, irrigation, and fixing potholes. The intermediaries would then shop around development agencies to find one willing to supply the service in return for the blocks of vouchers. The vouchers would have to have some term structure appropriate to the capital and recurrent costs of development services.

⁴¹ See the World Bank’s 2002 WDR, *Institutions for Markets*.

The vouchers would inevitably develop a secondary market, where the price of the voucher reflects the success of the aid effort in that area. Alternatively, aid agencies could issue their own vouchers that could be redeemed only at that agency. The secondary market price then would give information on the effectiveness of that agency.

The intermediaries could be anyone – from private individuals or firms to NGOs to international financial institutions. Intermediaries could also verify that the customers receive the development service requested and are satisfied, which is enforced by the desire of all participants to maintain their reputation for future transactions. For communities that are fortunate enough to have electric power, phones, and web access, participants could use the Internet to facilitate communication and posting of information on projects searching for funding, donors searching for projects, and intermediaries' reputation. (This last is an idea being pioneered by a private company in Washington called Development Space.⁴² Even if some of the recipient communities lack even elementary electric power or phone lines to connect to the Internet, some of the other players could communicate via the web.)

Aid vouchers would address some of the bureaucratic hindrances in foreign aid. They would induce competition between aid agencies, creating incentives for them to cut costs and reward production, shift away from observable trophies to meeting the needs of the ultimate beneficiaries. Competition, as compared to the cartel of good intentions, would expand the quantity and lower the price of aid services. Competitive pressure would induce aid agencies to specialize in their various comparative advantages and reduce the proliferation of donors and projects in small, poor countries.

Vouchers would give valuable feedback from the previously voiceless poor on what the poor really want and what and who is effective at meeting those wants. The flow of vouchers to different aid agencies would indicate their relative efficiency, with even a small amount of such

⁴² <http://www.developmentspace.com> I do not have any personal financial stake in Development Space, I just think it is a promising idea!

transactions at the margin sufficient to give feedback on agency performance (or the vouchers could be agency-specific and then the price would reflect agency efficiency, as suggested above). Likewise, the flow of vouchers through different intermediaries would indicate *their* relative efficiency and probity.

The decentralized matching of donors and recipients bypasses the centralized administrative funnel that chokes the current delivery of aid. The vouchers create competitive pressure on government agencies in poor countries to really deliver services or see their budgets stagnate. If aid agencies are really serious about participation by the poor, then they should like a mechanism that allows the poor to make choices. Vouchers are a way to make international bureaucracies behave more like firms in private markets.

Are vouchers superior to just giving cash grants to poor individuals? Given the incentives facing individuals and the closeness to subsistence of the poor, cash grants would likely be used for consumption rather than productivity-enhancing investment. Foreign aid is too small to make much of a difference in consumption of the world's poor. A voucher for development services is a subsidy to those productivity-enhancing services for the poor, which conceptually would seem to improve well-being of the poor more than a cash subsidy for consumption.

Still the minimum standard with ANY foreign aid program (including all those discussed above) should be that it do no worse than simply giving aid money as a financial asset to the poor. A control group of the extreme poor could have aid funds deposited in an account that purchases OECD treasury bills and pays out the interest as an income supplement to the poor every year. We should be open to the possibility that this alternative would out-compete both existing aid delivery mechanisms and other fancier schemes for reinventing aid.

Even with the voucher recipients, one could imagine a savings alternative. To strengthen bargaining power of the voucher recipients, for example, the vouchers could be saved for future years if individuals are not satisfied with the services being offered. And the hypothesis that

vouchers are superior to cash grants could be tested by doing both experiments and comparing the behavior of the two groups of recipients to each other and to a control group that did not receive either.

Of course, one can think of tons of logistical difficulties with implementing such a scheme. It is a largely untried idea, and should be subjected to all the skepticism appropriate to untried ideas. It should be tried only experimentally and gradually (and humbly given the history of failure of bright ideas in foreign aid), with a lot of learning and modification along the way. And another “of course”, there are some services for which a voucher scheme might work, and others for which it clearly would not. Vouchers might work for some local environmental issues but not for more global ones. It’s hard to see how vouchers could solve problems of law and order, national defense, enforcing property rights, social conflict, or defending human rights.⁴³ Some societies may have a predatory government or elite that would steal any vouchers given to the poor. The voucher proposal does not directly address the international financial institutions and aid community’s difficult problem of fomenting social change from bad governments to good governments in poor societies. By increasing voice of beneficiaries, market competition, and feedback on government performance, vouchers might increase pressure on governments to deliver effective services. However, there are difficult questions about how provision of development services by international aid agencies, if they turn out to be the winners in the competition for vouchers, would increase or lessen the pressure on national governments to work better.

There are also potential problems of judging aid intermediaries on absolute performance because there would likely be sorting of the best aid projects into the best aid intermediaries, who engage in “cream-skimming”. Hsieh and Urquiola 2002 point out this problem with the

⁴³ Pritchett and Woolcock 2002 point out that “demand-driven” approaches cannot solve the problem in sectors where the agency’s “customer” is someone who would prefer the agency NOT to provide the service (e.g. the criminal, external or domestic aggressor, or human rights violator and enforcement or defence agencies).

implementation of school vouchers in Chile, where the increased incentives for school performance were offset by stratification between students. The best private schools attracted the best students from the public schools, leaving the remaining students in the public schools worse off since there are strong peer effects in schooling. Analogously, one would be concerned that rewarding aid intermediaries for absolute performance would cause them to select projects that from better off areas that have greater likelihood of success, neglecting poorer areas that need the help more. One can think of ways to compensate for these perverse effects, perhaps by giving more vouchers to poorer areas or by designing the reward scheme for intermediaries so that they are judged by net performance rather than absolute performance.

There are also worries about the multiple objectives that aid agencies face. Competitive pressure might lead aid agencies to compete on some dimensions that satisfy the customers, but neglect other goals that serve some larger public purpose (Dixit 2000). They might figure out ways to game the system to attract vouchers in ways that don't improve public welfare.

Also there are difficult information problems in making sure that poor people with low human capital have enough knowledge to make good choices. Well-informed insiders might buy up vouchers at a steep discount from poorly informed peasants. Nevertheless, it is better to address information problems directly rather than not have a market at all. Letting poor people make their own choices seems like a powerful force to try harnessing for economic development.

Other market mechanisms can also be envisioned.⁴⁴ Direct subsidies to income creation, savings, or human capital accumulation would have some of the same advantages of minimizing bureaucracy and getting resources directly to the beneficiaries. Each would use money to create

⁴⁴ George Soros has recently made a proposal to use a marketplace to allocate aid (Soros 2002), with financing coming from a new issue of Special Drawing Rights by the IMF. Soros recommends a jury of eminent persons to vet the decentralized submission of project proposals, which would then be presented for financing to donors. The World Bank's Private Sector Development Strategy (2001) has some interesting ideas about contracting out aid initiatives to private providers with performance-based contracts. The Meltzer Commission (2000) suggested the World Bank should with grants solicit competitive bids for delivering social services, including from NGOs and private companies, with ex-post performance checked by independent auditors. Social Funds are a mechanism that has been tried in some countries to bypass

incentives for individuals to invest in future income creation. One reason that the returns to such investment are low without a subsidy might be collective action failures. For example, human capital investment might only pay off only if you have skilled people to work with. Your human capital investment payoff depends on everyone else investing in human capital. If everyone starts off with low human capital, people remain trapped in poverty because each individual faces low return to human capital accumulation. Subsidies to poor communities cause all individuals to increase their investment together, theoretically solving a collective action problem, if any.⁴⁵

Low returns to investment by the poor may also stem from poor institutions and poor infrastructure. The top down approach to development tries to bureaucratically improve the institutions and infrastructure. It may be just as effective to create increased demand for infrastructure and institutions by increasing the productive capacity of individuals, who will then have more voice to petition for reforms and can demonstrate high payoffs to reforms. Market-based subsidies may turn vicious circles of low human capital, poor institutions, and poor infrastructure into virtuous ones through bottom-up change.

One could also foment change from the bottom up by giving some vouchers directly to municipal or regional governments that establish a track record of good service delivery. There *are* some examples of “good governments in the tropics,” to use the phrase of Tandler’s (1997) study of Ceará state, Brazil.

One can still try on a separate track to make money available to good national governments, still using market forces of competition. One could adopt some variant of Kanbur, Sandler, and Morrison’s (1999) “common pool” approach, in which donors would put their money into a fund that would finance unrestricted block grants to “good governments.” Of course, the critical issue is to decide what is a good government. To resolve the problems of poor

bureaucratic obstacles, but these do not really use market mechanisms and are typically centralized at the national level (see Tandler 2001, Ellerman 2001).

selectivity in the past, the managers of the fund (whoever they are) could announce that only the best X governments will receive funding. Governments could then of their own free will decide to apply to this fund, submitting a proposal documenting their own program and their previous track record at fostering economic development and poverty alleviation. This would be a welcome change from the micro-management and the insulting intrusiveness of donors in poor country affairs. The fund itself does not violate sovereignty anymore than a venture capital fund violates the autonomy of a firm soliciting financing by deciding yes or no on the firm's application. Results of the aid fund would be monitored over time and the management of the fund held accountable for bad decisions or poor results.⁴⁶

Another advantage of a central aid fund is that it breaks the link between aid money and the obligatory use of a particular agency's bureaucracy. Foreign-assistance agencies would devote part of their resources to the common pool. The recipient countries could take the funds and work with any agency they choose. This scenario would increase the bargaining power of the poor recipients, minimize duplication, and foster competition among aid agencies.

Maybe we can change existing aid bureaucracies to function more like firms accountable to consumers and less like unaccountable central planners. Decentralized autonomous units within aid agencies could be encouraged to specialize in delivering particular services in particular regions, with control group evaluation of all interventions, systematic accumulation of data and previous historical and country experience, and intensive interaction with beneficiaries. Beneficiaries and their representatives should "know who to call" to get something done. Such units could compete with each other and with units from other aid agencies for the "aid contract" to supply a particular service in a particular area, with winners determined by previous track

⁴⁵ This is one possible *raison d'être* for aid. The aid community has shown surprisingly little interest in what exactly is the conceptual rationale for aid to the poor. Showing that the poor are needy is not enough unless you have some concept about how aid would meet those needs.

⁴⁶ The "Millennium Challenge Account" proposed of President Bush is a step in this direction, although it did not foresee unrestricted block grants. Svensson 2002 discusses the virtues of competition among aid recipients to receive funds in an "aid tournament."

record and reputation for efficiency and specialized expertise. These units could eventually be split off from the parent agency altogether. Just as dissatisfied consumers can penalize the firm by taking away their business, donors, beneficiaries, and their representatives could exit to another supplier if the first one proves unsatisfactory. To give another analogy, a private firm chooses a particular input supplier based on the reputation of the supplier for specialized knowledge of the business and the previous experience with that supplier. If a firm is unhappy with a supplier, it changes to another supplier. To break up the cartel of good intentions, the donors and beneficiaries should be free to choose suppliers who deliver satisfaction.

And what of donor “coordination”? The problem with aid has not been too much competition among donors, as conventional wisdom has it, but too little. The decentralized market that matches donors and beneficiaries should be the mechanism that coordinates donors. The market does not have two different suppliers producing the same output for the same customer, unlike the frequent duplication in foreign aid, because once that customer’s demand is satisfied there is no incentive for another supplier to satisfy it again.

Experience with vouchers and other market mechanisms

There has been some experience with market mechanisms to aid the poor, both in rich and poor countries. The most famous are school vouchers. These are issued to parents, who can turn them in at any school of their choice who is willing to take them. Although intensely controversial, the consensus of the literature seems to be that school vouchers have improved schooling opportunities and outcomes for the poor. The studies range from those in US cities like Milwaukee (Rouse 1998) to those that find improved earnings of poor workers in Colombia (Angrist et al. 2000). Hoxby 2001 found positive effects of school choice on school productivity in Milwaukee, Michigan, and Arizona, arguing that regular public schools boosted their productivity in response to competition. Peterson et al. 2001 found positive effects of school voucher programs on test scores of African-Americans in New York, Dayton, and Washington D.C. Hanushek and Rivkin 2001 found that competition increased teacher quality in metropolitan

areas across Texas. . As mentioned earlier, however, Hsieh and Urquiola 2002 challenge these positive findings with a study of Chile that fails to find overall positive nationwide effects of vouchers, arguing that negative general equilibrium effects of increased segregation by skill offset positive effects on individual students or schools.

Another voucher experiment in the US was with vouchers for housing for the poor, giving the poor choices on where to live, which some studies find improved well-being (Blank 1997). Contracting out of public services, performance-based reviews, or outright privatization in the US, UK, and New Zealand have garnered mixed reviews (see survey in Dixit 2000).

There are alternative market mechanisms to vouchers that have also been tried. There are many programs in poor countries to provide cash or food to families in return for keeping their kids in school (PROGRESA in Mexico, Bono Escolar in Argentina, Bolsa Escola in Brazil, the SUF or Subsidio Unitario Familiar in Chile, PRAF in Honduras, a subsidy to female students in China, and Food for Education in Bangladesh; see Morley and Coady 2002). Studies of the Bangladesh and Mexico programs have found a positive effect on schooling and income (Morley and Coady 2002, Ravallion and Wodon 1999, Skoufias et al 2000, IFPRI 2000). Subsidies to income creation by the poor, such as the Earned Income Tax Credit in the US, seem to have increased work effort and income (Blank 1997, Blank and Ellwood 2001, Neumark and Wascher 2000, Hotz and Scholz 2001) The welfare state seems to succeed at ameliorating poverty in rich societies where there is a strong consensus about helping the poor; racial antagonisms seem to be the main reason why the government does not try harder to reduce poverty in the US (Alesina et al. 2001).

*The reasonable man adapts himself to the world.
The unreasonable one persists in trying to adapt the world to himself.
Therefore, all progress depends on the unreasonable man.*
George Bernard Shaw (quoted in Power 2002)

Conclusions

Aid foundered in a sea of bureaucracy, despite the good intentions, altruism, and genuine professional dedication of the individuals involved. The aid community responded to its difficult environment by organizing itself as a cartel of good intentions, suppressing critical feedback and learning from the past, suppressing competitive pressure to deliver results, and suppressing identification of the best channel of resources for different objectives. The bureaucracy controlled foreign aid, with the result that foreign aid lost support in the rich countries and liberal political and economic ideals lost support in the poor countries.

Foreign aid should try harder to harness the decentralized genius of the market in order for aid to really reach its intended beneficiaries. Rather than trying to fix a pothole for one poor person in Ethiopia through an arsenal of international goals, frameworks, and bureaucracies, let aid marketplaces and aid vouchers work to match a donor with that recipient. Rather than imposing processes, strategies, and wish-lists on the poor, let the poor make their own choices. If aid vouchers and other market mechanisms were more effective at getting donor funds to the poor, support in rich countries for foreign aid would likely increase (maybe even double!)

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