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Assessing aid: what works, what doesn't, and why

World Bank, Oxford University Press, New York, 1998, xii + 148pp, ISBN 0-19-521123-5

This report summarises the findings of recent World Bank research on aid effectiveness—references to which are provided, along with the web address for access to much of the data used. It gets off to a bad start, however, appearing to claim a degree of success for aid that is not demonstrated by the empirical studies.

Foreign aid has at times been a spectacular success. [Several countries at various times] have gone from crisis to rapid development. Foreign aid played a major role in each transformation (p.1)

It is impossible to determine the extent to which aid has contributed to the development of particular countries during particular periods given that many other factors also played a role, so it is a relief to find that the level of rigour improves after the opening paragraph. Although a certain amount of case study evidence is included, the bulk of the report focuses on the results of econometric analyses of various aspects of performance of some 56 developing countries over six four-year periods from 1970 to 1993.

It is immediately conceded that ...foreign aid has also been, at times, an unmitigated failure. [In Zaire, for example] decades of large-scale foreign assistance left not a trace of progress (p.1).

This sets the scene for the main finding of these analyses—that the quality of economic management is an important determinant not only of economic growth, but also the effectiveness of aid. The 'quality of economic management' enters the analysis as a composite index of

inflation, the budget surplus, trade openness and institutional quality; in turn, institutional quality involves an assessment of the rule of law, the quality of the bureaucracy, and the persuasiveness of corruption (although precise details are not provided).

The regressions suggest that the marginal impact of 1 per cent of GDP in aid on the growth rate of per capita GNP varies from -0.3 per cent for countries with 'poor' policy, to 0 per cent for those with 'mediocre' policy, to 0.5 per cent for those with 'good' policy (p.123). That is, the historical record suggests that aid has had a negligible or even counterproductive impact on growth at the margin in many cases—and perhaps that the worldwide aid portfolio may have been showing negative returns on average, despite success in some countries—although the authors do not put it in these terms. An explanation for the diminishing trend in global aid transfers might be that popular misgivings about the effectiveness of aid have anticipated these econometric findings, although the authors prefer instead to blame troublesome fiscal deficits in donor countries, the end of the Cold War, and the upsurge in private capital flows to developing countries.

The report blames superficial thinking about development during the first few decades after World War II for the patchy impact of aid. Poor countries previously were thought to be held back by market failures and lack of capital, so promoting growth was thought merely to require putting enough funds in the hands of governments to fill the gap between available savings and required investment. There is now a much better appreciation of the positive contribution of markets to development, and a realisation that government failure is a significant problem capable of more than nullifying the potential

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impact of aid. The main recommendation of the report, therefore, is that aid should be 'more about supporting good institutions and policies than providing capital' (p.13).

A problem with the econometrics work on aid and growth is that aid is treated as a single variable. Abstracting from the diverse mix of characteristics of the particular aid package delivered to each country risks lending support to the simplistic interpretation that no aid should go to countries with poor or mediocre management. But aid is not homogeneous, and this allows the authors to avoid making such an unpalatable recommendation. Nevertheless they do argue that less aid should go to less well-managed countries, other things equal, and that donors should be willing to cut back aid to countries with persistently low-quality public sectors. The implication is that this would cut down on wasteful aid, while at the same time providing an incentive to recipient country governments to implement reforms.

At the same time, this smaller flow of aid to such countries should be modified so as to emphasise facilitating the flow of ideas about better economic policies and better institutions. In other words, the authors are of the view that 'ideas aid' can be expected to make a positive contribution in poorly managed countries, even though the typical aid package of the past would not. Perhaps they are right, but that does not seem to be a conclusion that can be drawn from the results presented here. In this respect, the report suffers from the general predisposition of aid optimists to believe that aid will work in the future, despite its failures in the past: all that is required is an appropriate change of emphasis.

The report argues against conditionality as a means of ensuring aid success. Unless there is strong political

leadership and political support for reform, conditions have tended to be ignored.

Worse, loans have often continued to be disbursed regardless of failure to carry out agreed-upon policy measures—reflecting aid agencies' preoccupation with how much money they disburse. Thus, 'policy-based financing should go only to countries with a strong track record or where there is a demonstrable basis for optimism' (p.4). It is noted, however, that even if recipient governments themselves may not be committed to reform, 'there are often champions of local or sectoral reform, and aid at times has been effective in supporting [their] initiatives' (p.4).

The fungibility of aid—that is, the fact that aid directed to one area may have little impact on spending in that area since it permits the recipient government to reallocate its revenues to spending elsewhere—is discussed in some detail. The implication is that the 'effectiveness of finance depends on the quality of all public investments and expenditures, not simply on aid-financed sectors and projects' (p.20). Clearly this is one explanation for the finding that the impact of aid depends on the quality of economic management generally.

One controversial recommendation is that donors should work in partnership rather than in competition. The lack of such cooperation hitherto is explained in terms of the desire of donors to 'plant their flags' on something tangible. But little if any evidence of the supposed harmful effects of competition or lack of coordination is presented, and this reviewer remains sceptical, given the generally beneficial impact of competition in many other fields.

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A Different Kind of Voyage: development and dependence in the Pacific Islands

A.V. Hughes, Asian Development Bank, Manila, 1998, 139pp, ISBN 9715611508

Although this monograph is clothed in a bureaucratic format, with the author's name hidden from the title page, and has the footnotes on p.9 mislabeled, unlike most of its predecessors in the Pacific Studies Series, it is not mere bureaucratisation. In addition to basic information about the evolution of the Pacific islands since their independence, there is also a great deal of interesting and sound analysis. Tony Hughes' love for the Pacific islands is evident, but it has not corroded his judgment. Here, if often between the lines so as not to hurt feelings and upset his Asian Development Bank sponsors, are the reasons why the Pacific islands, in spite of their rich endowment of natural resources and high aid inflows, have miserable economic, social and political growth records.

Policies have often not been at fault. Some prices are distorted (pp.52–57), but though policy-created distortions, such as high labour costs, have been a brake on growth, this has not been the main problem. Government has largely consisted of arbitrary intervention to favour élites and their local and foreign cronies. The ensuing levels of corruption are endemic and epidemic. In some of the Pacific island states it is not surprising that the economies have grown slowly, but miraculous that they have managed to keep up with population growth. The boxes on financial scams (p.65) and offshore financial centres (p.77), together with information in the text about how corruption works in practice, indicate the breadth and depth of tailor-made intervention and the problems it creates.

Tony Hughes, rightly, blames the colonial powers for basic problems in the South Pacific. During the 19th century they

carelessly cut up vast areas of ocean and, in the case of Papua New Guinea, of the largest landmass in the South Pacific, into separate colonies. With independence this resulted in the creation of so-called 'nation states' that do not have the economies of scale to be viable. Their scale problems are not economic. With open trade, capital and labour markets, the Pacific islands could do very well in economic terms. But, with the exception of Papua New Guinea and Fiji, they do not have the critical mass of human resources, even if education was far ahead of present levels, to make 12 or more nation states (that is, the Asian Development Bank members, p.7). Their representation abroad is alone enough to bankrupt them. Had the colonial powers worked toward a Pacific federation as independence approached, the history of the Pacific islands would have been very different. Now federation could take a century to achieve.

The colonial heritage continues to undermine the Pacific islands' ability to grow. Each 'nation state' is a member of all the international and regional organisations that the world's bureaucrats have managed to put together. Tony Hughes has noted that there are well over 200 regional and sub-regional organisations in the South Pacific. They are mostly funded by aid donors, but by providing supra-national salaries and working conditions, they sap the Pacific islands' human resources. To justify their existence, the regional organisations organise constant rounds of meetings that are, inevitably, mostly empty of content. Added to meetings organised by the regional and international organisations, they mean that educated, articulate and literate national staff members are never at their desks to get on with the humdrum tasks that have to be done if governments are to work.

Although his criticism is *sotto voce*, Hughes also points to the numbers of expatriates, generally paid for by aid funds, who are still preventing islanders from

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acquiring the experience that making your own mistakes brings. The International Monetary Fund, for example, initiated the creation of Central Banks and supported them with staff from Washington for years, in countries as small as Tonga. Some island officials work long and hard hours to get things done, but for the most part administrative bottlenecks remain serious impediments to growth. The treatment of private investors, local and foreign, is a particular problem. In the highly regulated Pacific economies they can not just go into business, requiring permit after permit. Hughes quotes a World Bank study that concluded that ‘in many Pacific islands... permitting procedures are generally slow, opaque, circular and unpredictable, open to abuse both by investors and by the system’s administrators’. Attempts to improve the investment climate are constantly being undercut, in spite of protestations to the contrary at regional meetings, by fruitless competition among the islands to attract investment away from each other by ‘deals’.

As another heritage of post-colonialism, instead of focusing on the success of a variety of non-traditional exports and hence on the benefits of removing barriers to trade, the island economies are mired in the ending of the trade-distorting effects of Lomé, PATCRA, SPARTECA and GST preferences. The limited benefits and high long-term costs of those arrangements have been pointed out for years, notably in the *Pacific Economic Bulletin*, but to no avail. Although most of the Pacific islands’ trade is not intra-regional but with the rest of the world, the colonial-minded European Union now insists that the islands form a formal free-trade area. There is no evidence that this will provide benefits, but it will add to the already egregious regional organisation costs. The most important policy for small economies—the unilateral removal of all domestic trade barriers—is not yet accepted in the South Pacific, nor indeed, in the European Union’s high

protection of agriculture that damages the Pacific islands and other developing countries.

The brakes on development created by the freezing of customary rights are discussed in their historical context. The islanders, and particularly the élite groups, want to have their cake and eat it too. Weasel-wording this problem will not enable solutions to be found to the monopolisation of land. The opportunity costs of customary tenure have to be brought out into the open.

The monograph notes that education and health standards, notably in Papua New Guinea (and other Melanesian countries), are below international averages for other countries at similar levels of per capita income. Hughes is also well aware that island women bear the brunt of lagging growth and even greater lags in ‘trickle down’ effects. His central contribution to better prospects for the future makes sense. The islanders themselves have to make the required changes. Declining aid flows are likely to lead to marked improvements in economic performance as they did, for example, in Taiwan and the Republic of Korea, in the early 1960s. It seems extremely doubtful, however, that the tracts about ‘good governance’, ‘accountability’ and ‘transparency’ with which the World Bank and the Asian Development Bank are seeking to improve the performance of the Pacific island economies will have any effect. Those participating in the ‘deals’ that continue to be struck must be genuinely bewildered by these new slogans from the providers of ‘cargoes’. Only if the ‘cargoes’ were to come to an end would the messages be clear.

This is an excellent book. It deserves to be widely read in the Pacific islands and by all those who, like Tony Hughes, have the islanders’ interests at heart.

Helen Hughes

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Trade Policy Review: Solomon Islands 1998

World Trade Organization, Geneva and Lanham USA, WTO and Bernan Associates, 1999, xxvii and 132pp.

The WTO conducts a review of the international payments regimes of its members every two years for its four largest members (the European Union is one), every four years for the 16 next largest, and every six years for the rest.

This is the first review of the Solomon Islands' policies.

Part A is a statement by the chairperson of the Trade Policy Review Body. It is largely a summary, based on the *Report of the Solomon Islands Government* (Part C), of the intentions of the government elected in 1997 to change many of the policies of the previous government so as to achieve reforms consistent with the principles of the WTO, including a reduction in unsustainable logging. This is likely to be more of a 'wish list' designed to demonstrate that the Solomon Islands is observing WTO criteria than a forecast of forthcoming policy changes.

A 102-page completion of a WTO schedule describing the aspects of payments policies that WTO considers relevant plus several 'boxes' outlining WTO-approved principles forms Part B. This is a useful document but it is questionable if resources should be devoted to more than a statement of changes in policy in future reports.

Part D contains the minutes of meetings of the WTO Trade Policy Review Body relating to the Solomon Islands.

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The Role of Commercial Banks in Microfinance, Asia-Pacific Region

Ruth Goodwin-Groen, Foundation for Development Cooperation, Brisbane, 1998, 90pp, ISBN 09586728 4 9

The Australian Agency for International Development (AusAID) commissioned this study, prepared the Foundation for Development Cooperation. Under the Terms of Reference, the purpose of this study was 'to examine the scope for encouraging commercial banks in Australia and in our partner countries to become more engaged in the area of microfinance.' The outcome required of the study was 'a report that will serve as a resource for commercial banks, microfinance institutions, the non-government organisation community, AusAID itself and other interested parties capable of supporting sustainable microfinance activities in the Asia Pacific region'. To this end, the authors of the study undertook, as well as desk study, fieldwork in the form of interviews with representatives of commercial banks and microfinance practitioners in India, the Philippines and Australia. A substantial, though not exhaustive, bibliography on the topic is provided, while a limited amount of statistical information is drawn together from existing work already undertaken by others.

It is a useful summary, in an easy-to-read form, of the well-known features and issues of microfinance, and includes a set of recommendations for commercial banks and AusAID that unblushingly champion the cause.

That there are very few commercially viable financial organisations involved in microfinance around the world, is readily recognised by the study. Table 2 (p.29), listing fourteen banks in Latin America, Africa and Asia, raises questions as to the authors' definition of 'commercial' banks. The first institution cited, Banco Sol of

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Bolivia, while now a profitable microfinance lending and savings institution, achieved its present status on the basis of many years of non-government organisation, government and international donor support, while continuing to build at least part of its portfolio by accepting groomed clients from its non-government organisation associates.

Within the Asia Pacific region, the study has identified only four such entities, that do not need to rely on subsidies and external financial support—Bank Rakyat Indonesia (BRI) and Bank Dagang Bali in Indonesia, Hatton National Bank in Sri Lanka and Krishna Bhima Samruddhi Bank in India. However, while the study isolates the key factors for commercially viable operations by institutions involved in microfinance, it does not attempt to trace just how these successful institutions got to where they are today. It says little about the long gestation periods involved, the (at least initially) subsidised financial support provided from government and / or international donor sources, and the careful building of lending portfolios associated with stringently imposed savings programs for the poor.

Of greatest interest to readers of the *Pacific Economic Bulletin* would be the study's findings on microfinance in the Pacific region. Annex 2 provides a summary of commercial bank involvement in microfinance in the Pacific island countries. The picture painted is not surprisingly that commercial banks are not at all significantly involved in such activity in the Pacific. The reason given is: 'This is simply because the scale of lending in the Pacific is so small that microfinance is rarely commercially viable' (p.28). No information is provided on non-commercial bank activity in microfinance in the Pacific but that, clearly, would not be—and probably never could be—unsubsidised if only because of questions of economies of scale.

The study ends with series of recommendations for AusAID, banks and microfinancing institutions. These have been carefully drafted and are worth recording below.

Recommendations for AusAID are

- support only the microfinance institutions which are committed to moving towards financial self-sufficiency and ultimately profitability. (Comment: Would this ever be possible in the Pacific?)
- support microfinance institution initiatives in defining national standards of performance which can use to assess the institutions' creditworthiness
- work with other donors to enable interested bankers to learn that microentrepreneurs are a business opportunity, through first-hand experience of success stories
- encourage microfinance institutions to have commercial bankers on their boards
- join with other donors in working to remove policy restrictions to banks in microfinance as interest rate caps and instead to create a supportive policy environment. (Comment: There may be conflict here with government financial policies and policies on the security of the banking system, to say nothing of the obligations of commercial banks to their shareholders and depositors).

Recommendations for banks are

- learn about the different technologies for banks to lend profitably to microfinance institutions or microentrepreneurs
- work with microfinance institutions in establishing national standards of performance and a rating system for the microfinance industry
- support a local microfinance institution by bringing banking expertise to the board

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- work with local microfinance institutions and donors to ensure the policy environment is conducive to microfinance.

Recommendations for microfinance institutions are

- focus on reaching profitability
- work collectively to introduce national standards of performance and a rating system so banks can easily see the best microfinance institutions and lend accordingly
- ensure that the lessons of successful microfinance institutions are known to commercial banks
- invite leading commercial bankers to sit on the board of your microfinance institution. Consider a structure which allows accountability to investors, creditors and clients
- work with local banks and donors on ensuring the policy environment is conducive to microfinance.

These are all very sensible and strongly reflect the high-minded purposes of the non-government organisation movement. Whether civil servants, and more to the point, commercial bankers, are likely to embrace them, remains to be seen.

Alexander Agafonoff

Enhancing the Role of Government in the Pacific Island Economies

World Bank, Washington, DC, 1998, xv and 122 pp, ISBN 0821343513

Enhancing the Role of Government in the Pacific Island Economies was prepared by a team led by Hilarian Codippily from the Poverty Reduction and Economic Management Unit, based on fieldwork carried out in late 1997, in the immediate aftermath of the East Asian financial crisis.

The focus of the report is on the role of government (that is, governance) in the nine Pacific Island Member Countries (PMCs) of the World Bank—Fiji, Kiribati, Federated States of Micronesia, Republic of the Marshall Islands, Palau, Samoa, Solomon Islands, Tonga and Vanuatu.

The issue of governance came to prominence in development studies in the late 1980s, as a result of a realisation that inefficient administration, and poor quality public policy, were major contributing factors in the failure of a significant number of developing countries to achieve long-term sustainable development. The World Bank's definition of 'governance' includes public sector management, accountability, the legal framework and transparency in government decision-making.

The main arguments in this report are that 'state-led growth' has failed and that the countries are characterised by low growth and stagnation, for example 'the PMC governments invested an average of 29 per cent of GDP in their economies, but economic growth remained stubbornly low at 2 per cent a year.' In particular, per capita real GDP growth has been significantly lower in the PMCs than in the Caribbean, African and Indian Ocean islands. The report argues that the public sector in the Pacific island economies commands most of the available resources and makes it difficult for the weak private sector to find, and exploit, new sources of growth.

The report includes chapters on the scope of government in the region, and their spending patterns and priorities. There are profiles of public sector reforms in a number of the Pacific island economies. The structure and size of the public sector, environment and foreign aid are also included as appendices.

The policies advocated by the World Bank for the PMCs in this report include

- diversify their production base and export markets and exercise greater prudential supervision over their respective financial sectors

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- government must invest more efficiently and use its scarce resources more effectively
- an effective development partnership between the state and civil society would form the basis for private initiatives and encourage stakeholders to undertake a wider range of social and economic activities.

The main themes are that, first, government should focus on core functions, match government tasks to its capacity, and improve public sector accountability. Second, government should seek to raise the efficiency of public sector spending through policies designed to quicken the pace of economic growth and reduce poverty, and finally, governments should seek to implement planning and budgetary procedures within the framework for a medium term development horizon and to improve processes of public spending.

Generally, the report ignores the socio-political and cultural context, and the colonial experience of these countries. This is disappointing given that 'a key objective of this report is to underline the importance of fostering an enabling environment for the greater inclusion of their region's population in the development process.' In these countries the structure of government is largely a product of the colonial era, and these institutions have proven to be fundamentally inappropriate. I would argue that western social and economic policies that emphasise 'efficiency' have failed to produce the anticipated benefits and the 'effectiveness' of government in the PMCs is declining. I use these terms to mean that 'efficiency relates to the time and resources required to produce a given outcome' while 'effectiveness' relates to the appropriateness of efforts undertaken to the production of desired outcomes (Grindle 1996).

Policy advisers have often ignored the powerful ways in which culture, and tradition can impact on development in

these countries. The key question to answer is will an 'effective' organisation in a particular sociopolitical and cultural context necessarily produce the same outcomes in a different context? There is evidence of an inherent incompatibility between the World Bank 'model' and the context of the PMCs because

...the traditional economic systems of Pacific island countries are extremely diverse, they are built upon non-market transactions such as redistribution and reciprocal exchange. The social relationships of kinship, rank and community are primary, and the flow of goods and services are merely part of these relationships (Hooper and James 1994).

What is really required is an analysis of the way in which socio-political and cultural factors in Pacific island countries have inhibited 'effective' government, and to provide a framework to encourage 'good governance'.

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The Pacific Islands: environment and society

Moshe Rapaport (ed), The Bess Press, Honolulu, 1999, 480pp ISBN 1-57306-083-6 (hardcover), approx. A\$80, ISBN 1-57306-042-9 (paperback), approx. A\$60

In 1992, prior to the Rio Earth Summit, the South Pacific Regional Environment Programme (SPREP) published *Environment and Development: a Pacific island perspective* (SPREP 1992a) and *The Pacific Way* (SPREP 1992b). These listed and prioritised many environmental issues important and endogenous to the region which have formed the basis of much of SPREP's ongoing Action Plan (SPREP 1996). Both books highlighted and documented the environmental consequences of poor and inappropriate development. Since then it has become even more apparent that neglect of these important environmental issues will, over the long term, limit the opportunities for sustainable development in the South Pacific (Gladman, Mowbray and Duguman 1996, Burt and Clerk 1997, Overton and Scheyvens 1999).

Pacific peoples have long stressed the importance of maintaining strong links with their environments, maintaining traditions and opting for indigenous solutions. Yet what has happened seems to contradict this. Over the last 100 years it seems that development has progressed along western lines. Economic, social and environmental indicators (UNDP 1999) suggest that these countries have a long way to travel or indeed to return to a truly Pacific path to economically and ecologically sustainable, equitable and socially just societies.

The Pacific Islands: environment and society is timely. It presents the reader with a scholarly work on, and an appreciation of, the roots of the Pacific environment and its peoples. This book is an informative source providing a comprehensive survey of the contemporary Pacific. It provides a kaleidoscope to the reader of the past and

the present of the Pacific environments and peoples and is a significant contribution to Pacific island studies.

The book is divided into six sections covering 33 chapters written by prominent resident scholars and commentators from the Pacific, though mainly not indigenous.

Its scope is broad. Chapters are succinct summaries of a wide range of fields. Key themes are environmental processes, social change, population–resource relations, and recognising the region as distinct, environmentally and culturally. The aim of the book is to rethink 'place'. But it is more than this. To me, it is 'to rethink the Pacific'.

The first section deals with the physical environment, with chapters on climate, oceanography, geology, geomorphology, soils and water. Section 2 deals with the living environment and includes chapters on biogeography, terrestrial ecosystems, aquatic ecosystems.

Section 3 focuses on history, with chapters on the precontact period and the postcontact period. In a chapter on changing patterns of power, the author discusses why western institutions and models of development were foisted on the newly independent nations of the Pacific, and their appropriateness and desirability, given their diversity of social organisation. There is a recognition that changes are hindered by the security and strategic interests of colonial powers and western nations.

Section 4 is on culture, covering linguistic and cultural diversity, social relations, and evaluates challenges and changes to kinship and status and other traditional forms of customary Pacific social relationships. A chapter on tenure looks at both land and marine tenure, where customary ownership often conflicts with national laws. The section concludes with chapters on law, religion and art.

Demography, mobility, health and education are covered in Section 5. Chapter 25 is on [Pacific] women, with a discussion on womens' roles in development and

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today's roles of women in the economy, politics and education. Rapid increases in urbanisation have brought changes in lifestyles, environments and customs, while offering opportunities for a higher standard of living. But increasing urbanisation has brought many environmental and social problems.

Reconciling modern individualistic and urbanised lifestyles with traditional culture is likely to be the main challenge for Pacific islanders in the 21st century (p.324).

In the final section on the economy, it is noted that Pacific island economies are constrained by factors of scale, distance, limited resources and vicissitudes of the global political economy. It is suggested that economic development and modernisation theories on microstates need revision when applied to Pacific countries. Pacific economies can be the focus for rethinking theories on economic development and sustainability. An excellent overview of key issues and dilemmas facing mining in Pacific, mainly Melanesia, states that

...the challenge is to include communities in all stages of planning and development; the dilemma is how this objective can be achieved in planning processes that is capital driven and rooted in formal Western-knowledge based ideas of development, which may not be shared by Pacific islanders (Chapter 31:391).

While noting that the Pacific is attractive for its natural and cultural resources, in discussing prospects, including for cultural tourism and ecotourism, the book could have placed more importance on the need to incorporate the wider criteria of environmentally sustainable development. The final chapter on communications notes that communication is critical to development but identifies problems of lack of adequate telecommunications, cultural imperialism, and imbalance in media controls.

My main criticism of the book is that it lacks a final synthesis chapter drawing together its major themes. Despite this it is attractively produced and makes good reading. It contains many useful figures, diagrams and tables, a useful gazetteer, maps and has useful indices. It provides excellent insights into the Pacific and its peoples. It is a most suitable book for the reader who wants to understand more about the Pacific, be they islanders or outsiders. It will be a most useful university-level text in geography, environmental science, anthropology and Pacific island studies.

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