

# REAL AID

ENDING AID DEPENDENCY

act:onaid



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**Children laughing and playing in Ratnanagar, Nepal.** The children's neighbourhood surrounds the road which was focused on by ActionAid's pilot ELBAG programme.

PHOTO: KARI COLLINS/ACTIONAID

“Nepal has had its own aid policy since 2002, and many of the concerns it raised were later echoed in the Paris aid effectiveness process.”

## GLOSSARY

**Budget support** - aid which is paid to the recipient government for them to spend alongside their own revenues, on their own national development priorities.

**Country programmable aid** – an OECD measure of aid that can be used directly for development. It excludes items such as emergency aid, debt relief, spending on refugees and education in developed countries, and administrative costs.

**Sector support** – aid which is allocated for spending on a particular area of developing country development, for example education or health, on national priorities of the recipient government rather than particular projects.

**Technical assistance** – donor spending on outside expertise such as consultants, research or training, used to supplement the existing skills of developing country governments.

**Tied aid** – donor funding which has to be spent on goods or services from the donor country.

### We’ll always have Paris – the aid effectiveness process

Global discussions on improving aid effectiveness have over the last decade been organised through a series of international meetings of governments and others.

#### 2002 Monterrey UN Financing for Development Conference

Agreed that co-operation to improve aid effectiveness important.

#### 2003 Rome

The first time the principles for aid effectiveness were outlined in a declaration.

#### 2005 Paris

The first time donors and recipients agreed to commitments and to hold each other accountable for them. This Paris Declaration includes targets which have been monitored on:

- **ownership** – developing countries set their own development strategies for poverty reduction and improve their institutions
- **alignment** – donor countries support these strategies and use local systems
- **harmonisation** – donor countries co-ordinate and simplify to avoid duplication
- **results** – developing countries and donors focus on and measure development results
- **mutual accountability** – developing countries and donors are accountable to each other.

#### 2008 Accra

Designed to deepen implementation of Paris. Civil society participated for the first time. The outcome document Accra Agenda for Action deepened the Paris commitments.

#### 2011 Busan

High-Level Forum on Aid Effectiveness in November 2011.

## ABBREVIATIONS

<b>CSO</b>	Civil Society Organisation
<b>DAC</b>	Development Assistance Committee (An OECD body that deals with aid)
<b>DCF</b>	UN Development Co-operation Forum (A UN body that deals with aid policy)
<b>DFID</b>	Department for International Development (of the UK government)
<b>IFI</b>	International Financial Institution (includes the World Bank and IMF)
<b>LIC</b>	Low Income Country (A classification of the poorest countries)
<b>LDC</b>	Least Developed Country (A classification of the poorest countries)
<b>LLDC</b>	Land Locked Developing Country
<b>IMF</b>	International Monetary Fund
<b>MDGs</b>	Millennium Development Goals
<b>ODA</b>	Official Development Assistance (Aid from governments)
<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>PDE</b>	Paris Declaration Evaluation
<b>SIDS</b>	Small Island Developing State
<b>TA</b>	Technical Assistance
<b>USAID</b>	United States Agency for International Development



## EXECUTIVE SUMMARY

There is good news. Developing countries are getting less dependent on aid.

**Jalena Mohamed and  
Hawa Amiry, Tanzania**

Jalena is a member of the school committee, which ensures the Miyuyu primary school is being run effectively, and Hawa is involved in planning and finance within the community.

PHOTO: ANDREW MCCONNELL/PANOS PICTURES/ACTIONAID

**“We have shown donors that when we are in the driving seat – deciding how to allocate aid money ourselves – we spend donor money more effectively.”**

Ronald Nkusi,  
Finance Ministry  
Rwanda

By aid dependency we mean the proportion of government spending that comes from aid and over the last decade it has fallen on average by a third in the poorest countries. In Ghana aid dependency fell from 47% to 27%, in Mozambique from 74% to 58% and in Vietnam from 22% to 13%. Although aid levels increased, economic growth and the countries' ability to mobilise their own resources increased faster.

The kind of aid that helps support dramatic decreases in aid dependence is what ActionAid calls *real aid* – that's aid which empowers poor women and men to realise their rights, and reduces inequality. It might do this directly, by supporting smallholder farmers, empowering women or building schools. Or it might do it indirectly, by supporting tax systems, better governance or economic development. It is accountable, transparent from beginning to end, and gets the most out of every dollar spent. It supports developing countries to make their own decisions. Substandard aid, however, does not do this – and there's still a lot of it out there.

For Rwanda, real aid has helped transform the country. Aid as a percentage of government spending dropped from 85% in 2000 to 45% in 2010. “We have shown donors that when we are in the driving seat – deciding how to allocate aid money ourselves – we spend donor money more effectively. Donors have responded to the results we have delivered by giving us more and more say over how we use their aid,” Ronald Nkusi, Director of the External Finance Unit in the Finance Ministry, Rwanda.

Real aid is making such a massive difference because it is not tied to overpriced exports from the aid supplying country, or to unwanted or overpriced

technical assistance. Whilst it must be spent, directly or indirectly, on poverty reduction, it does not impose policy conditions or allocation priorities on recipient countries. And it does not carry excessive administration costs itself.

Substandard aid does all of these things. But, if the positive momentum is maintained, we will see more of this aid become “real”.

To ensure aid helps to reduce their dependency on it, developing countries are implementing systems to hold donors accountable. In Rwanda a traffic light system scores donors on factors such as how much they use the country's own finance systems, and use of budget support for procurement and governance.

Developing country governments are also becoming more accountable to their own people, rather than donors. In Ghana ActionAid supports a community in the village of Mampehia to track the school budget, which is financed out of Ghana's national budget, which in turn is substantially boosted by budget support aid.

Another key factor in the improving situation is that many countries have boosted their tax revenue by between 4 and 8% of GNI in recent years.

Donors can support this process by giving more real aid, which allows developing countries to make their own decisions. In Ghana donors have pooled a third of all aid to the country in a flexible programme which reduced the cost of mobilising resources. Donors can also be transparent and accountable themselves, by publishing details of their work in an internationally agreed form, and they can give aid which supports domestic resource

mobilisation. In a very clear example, aid from the UK supported Rwanda to quadruple its own taxes between 1998 and 2006.

### **HOW MUCH AID IS REAL AID?**

Major donors have provided \$24 billion more aid annually than ActionAid found five years ago. The proportion of real aid has also increased – but only by a small amount, from 51% to 55%. There is still a lot of substandard aid, and donors vary enormously in their provision of real aid. As a proportion of their aid, in 2009 Ireland, the UK and Luxembourg provided the most real aid. Greece, France and Austria provided the least.

So to reduce aid dependency even further and faster ActionAid recommends that

#### **1. Aid donors:**

- increase real aid sharply
- ensure aid benefits women
- increase the value for money and results of aid by making aid more predictable and using recipient systems
- focus on true policy coherence for development – e.g. fair non-aid policies such as tax co-operation that will support the good work that aid can do, rather than undermine it.

#### **2. Aid – receiving governments:**

- take clearer leadership on making aid more effective for development results
- be fully accountable to domestic stakeholders
- mobilise domestic resources
- continue to improve their systems for financial management, procurement, monitoring and evaluation and fighting corruption
- incorporate gender responsive budgeting into their country processes

- base national development plans on existing gender equality and women's empowerment commitments.

#### **3. Donors and recipients jointly:**

- design (recipients) and support (donors) strong national development strategies based on democratic ownership
- give preference to local procurement
- accelerate aid delivery.

#### **4. Citizens in developing and developed countries:**

- participate fully in national accountability
- demand greater tax justice globally and nationally.

Finally, to implement these commitments, all stakeholders should agree on strong mutual accountability frameworks, and dramatically improve aid transparency.

**“Fourteen of the 30 most aid dependent countries in 2000 reduced their dependence by more than 20% of expenditure by 2009.”**



**Gita Subedi** is a member of Sunaulo Samuha budget analysis group which audits public programmes in Ratnanagar, Nepal. With ActionAid support the group ensures that the community has a say in planning processes, as well as preventing corruption and misappropriation of project funds.

PHOTO: KARI COLLINS/ACTIONAID

## CHAPTER 1 INTRODUCTION: REAL AID IS TRANSFORMING LIVES

Aid is working – it is helping to bring women and men out of poverty. But more than that, developing countries' dependency on aid is falling, even while the volume of aid increases. As we'll show in Chapter 2, a decline in aid dependency is good reason to cheer - because dependency undercuts countries' ability to chart their own development strategies, which is what's needed if development is to really take root.

One of the many reasons aid dependency is falling relates, paradoxically, to aid itself. When aid is given in such a way that it supports poor countries to lead their own development, be more accountable to their own people, and mobilise more of their own resources, then aid itself contributes to reducing aid dependency. Chapter 3 shows how this can happen.

Allowing space for countries' own development plans to work is one attribute of what ActionAid calls real aid – and major donors have been providing more of it. Indeed, \$24 billion more annually than we found five years ago.

But at the same time there is still a lot of substandard aid out there, and ActionAid will keep urging that it be improved. In Chapter 4 we identify the sources, the problems it creates, and how to change it into real aid so we can further reduce aid dependency.

Finally, we recommend ways that donors and developing country governments can increase real aid, contributing to ending aid dependency.

The rest of this chapter introduces the ActionAid *Real aid* reports, and shows how, in Action Aid's view; aid is doing a great job of reducing poverty and inequality in the poorer countries of the world.

### 1.1 REAL AID REDUCES INEQUALITY AND POVERTY

Aid is far more effective for poor people – and cost effective too – when it is real aid. Real aid empowers poor women and men to realise their rights, and reduces poverty and inequality. It might do this directly – by supporting smallholder farmers, empowering women or building schools. Or it might do it indirectly, by supporting tax systems, better governance or economic development. It needs to be accountable and delivered transparently, so that beneficiaries can track it, and so that it benefits the poorest and most vulnerable people while getting the most out of every dollar spent. It supports developing countries to make their own decisions and implement their own development priorities, rather than dictating their choices.

In 2005 and 2006, ActionAid produced reports *Real aid* and *Real aid 2*, identifying how much aid was real aid. Aid budgets were growing sharply due to booming

economies, and ActionAid insisted that pledges of further increases, made by the G8 and the EU in 2005, must be real aid.

Five years on, the situation is very different. The global economic crisis has brought severe budget restrictions, and some donors have not met their pledges. Aid has been coming under public attack. This report, *Real aid 3*, focuses on how, in fact, aid dependency is going down. It shows how real aid is contributing to that result, and then looks at how much real aid is now being delivered. The key factor in real aid's success is its aim to “work itself out of a job”, as the president of the African Development Bank puts it, by reducing aid dependency. This allows the world's poorest citizens to hold donor governments, and their own, to account for how aid and state budgets are delivered.

As well as assessing aid using official statistics and the vast array of recent literature, for *Real aid 3* ActionAid has carried out a detailed seven-country survey of civil society and government perceptions

of aid quality<sup>1</sup>, and has also interviewed people for case studies in Ghana, Nepal and Rwanda.

### 1.2 THE REAL SUCCESS OF AID

Since the 1950s aid has attracted critics who claim that it is largely wasted, makes recipients more dependent by reducing growth and tax collection, and promotes corruption. Substandard aid can have all of these faults but real aid is working.<sup>2</sup>

In the last 20 years, aid has helped to achieve astonishing progress for human development and poverty reduction. 70% of the world's poor people are women, and aid which supports the social sectors – whether health, education, water supply or social protection – is very likely to support women in particular, as it provides the services that women otherwise have to provide themselves.

Researchers have mapped stories of progress supported by aid, such as rural water and sanitation in Laos, rural roads and irrigation in Thailand, or child health in Rwanda.<sup>6</sup> Aid has contributed to halving the number of people in poverty since 1990 and reducing by 10,000 the number of children who die needlessly every day.<sup>7</sup>

Real aid has helped empower citizens to improve the development process in their own countries by:

- Reducing gender inequality and fulfilling women's rights. There are now 96 girls enrolled in primary school for every 100 boys worldwide. Although not directly aid related, women also now hold 19% of parliamentary seats worldwide.<sup>8</sup>
- Helping them hold their governments to account by supporting national audit

institutions, parliaments, community monitoring organisations and a free and independent media, in countries such as Ghana.<sup>9</sup>

- Improving tax revenue collection, which across Africa has increased by more than 7% of national income since 2000.<sup>10 11</sup>
- Helping the poor to save and invest more in their own businesses through microfinance programmes, which from Bangladesh to Bolivia have created thousands of enterprises and millions of jobs.<sup>12</sup>
- Increasing growth, which studies from the IMF concluded, when aid is specifically intended for this purpose, can increase growth by 0.5-1.5% a year over several decades.<sup>13 14</sup> Growth is, of course, not sufficient to achieve poverty reduction or reduction in inequality, but it is necessary and leads to poverty reduction when focussed on poor people.

The real success of aid can therefore also be measured in genuine sustainable development progress, which empowers the world's citizens to hold their governments to account, and which empower governments to develop their own economies and end their dependence on aid.

Aid is achieving more than ever before. In the 1970s and 1980s, most aid was designed to fight the Cold War. So it went to some countries run by dictators – as long as they were “our dictators” - and provided carte blanche for many to engage in corruption, bribery and wastage. Since the end of the Cold War, research has shown that better quality aid is more targeted towards the poorest countries and people.<sup>15</sup>

“Aid’s results between 2000 and 2010 include: HIV/AIDS treatment to 4 million people,<sup>3</sup> 88 million anti-malaria bed nets,<sup>4</sup> and 40 million more children going to school.”<sup>5</sup>

### 1.3 WHY AID IS IMPORTANT

Back in 2000 world leaders agreed that aid should be targeted to reduce poverty and established the Millennium Development Goals (MDGs) for development. In 2005, they agreed a series of targets for making aid more effective in achieving these results, as well as to sharply increase aid. Though these targets have not all been met, they have increased the volume and the quality of aid.<sup>16</sup> Moreover, the MDG framework with its social sector focus has helped make sure aid benefits poor people.

Aid is only small part of the development picture. It is a small proportion of spending by governments in donor countries, and a fraction of the levels the public assumes. In the UK in 2006, aid represented below 1% of government spending but the public thought that it was close to 20%.<sup>17</sup> Even in Sub-Saharan Africa, the world’s most aid-dependent region, aid per person has averaged only 6 cents a day over the last twenty years.<sup>18</sup> And in many developing countries, aid’s financial contribution to development is dwarfed by other money from overseas such as remittances from migrant workers, foreign investment, bank loans or bonds – and from domestic sources such as tax revenue and domestic savings investment and loans.

But real aid is an important part of the picture precisely because it is money intended to produce development results for poor people. Other foreign money can be positive for growth but is not targeted at the poorest,<sup>19</sup> it can increase inequality, can do its best to avoid tax<sup>20</sup> and can severely damage the environment. Aid does not cause poverty, dependence, and conflict: rather it – and other types of financing – goes to countries ravaged by these factors.<sup>21</sup>

In addition, even though it is a small amount, aid represents two-thirds of the money flowing to the world’s poorest, least developed, countries, which receive little in private flows and have less ability, because of their poverty, to generate domestic revenue. And aid can be, as we will show, powerful in attracting private investments from individuals and businesses, and generating higher tax revenues. When investors are asked what factors are likely to make them invest more, they consistently underline power, water, transport, and healthy and well-educated workforces – all the things for which real aid and government expenditure are the key sources of finance.<sup>22</sup>

So real aid is crucial for long-term equitable and sustainable development, for improving gender equity, and for ensuring that the poorest citizens can enjoy their rights. And vitally, people in developing countries, which receive aid, believe that real aid can transform their lives.<sup>23</sup>





**Theresa Kamara,  
Sierra Leone, Freetown**

Theresa attends the after-school adult literacy class at Al-Qudus primary school, which has received training in Budget Monitoring and Advocacy from the School Management Committee, which is supported by ActionAid.

PHOTO: AUBREY WADE/ACTIONAID

## CHAPTER 2 AID DEPENDENCY

Whilst aid is succeeding in contributing to human development, dependency on foreign aid can be more problematic. This is not, as is sometimes argued, because aid dependency inhibits economic development or mobilisation of domestic resources. But it undercuts countries' ability to chart their own development strategies, which is what is needed if development is to really take root. It does this by reducing developing countries policy autonomy, undermining recipient governments' accountability to their own citizens, and making it harder for them to plan development programmes due to its unpredictability. So it is good news that, over the last decade, even while aid has increased, aid dependency has fallen by a third in the poorest countries.

“Aid is only a means to an end. Indeed, if aid is truly effective, it will progressively do itself out of a job. Effective aid should not foster dependence.”

Donald Kaberuka,  
President of  
the African  
Development Bank

**What is aid dependency? A country is aid dependent when it cannot perform many of the core functions of government, such as delivering basic public services like schools and clinics, without foreign aid. More precisely, this report identifies aid dependency as when aid funds a high percentage of government budget expenditure, on an ongoing basis. Another way to measure dependency is the proportion of the whole economy (Gross National Income) that is made up of aid flows. The two ratios (aid/budget expenditure and aid/GNI) are closely correlated.**

## 2.1 WHY AID DEPENDENCY IS A PROBLEM

Many authors<sup>27</sup> have discussed the potential pernicious effects of aid dependency and why it is desirable to end it. Some of these arguments are overblown. The most extreme have asserted that aid dependency makes countries unlikely to develop or to fund their own development. This includes accusations that the whole population is less inclined to save, to invest, to produce goods for export or domestic consumption, or even to work, or the government is less inclined to implement policies which encourage these trends, and therefore aid reduces growth. This may be true where aid dependency reaches very high levels and continue for a long time (see later in this chapter). However, at lower levels there is little evidence to support this assertion, which also ignores the many positive effects of aid on human development. The more balanced conclusion is that aid has had a positive effect in most countries on accelerating growth, development and poverty reduction, especially when it supports recipient-led policies and processes.<sup>28</sup>

The narrow version of this disincentive argument focuses on reduced pressure to mobilise tax revenue. The argument runs that if governments have reliable flows of aid to support their expenditures, they lose the incentive to mobilise tax revenue, especially from powerful groups such as wealthier citizens or foreign investors.

Then they become trapped in a vicious cycle where low tax revenues force them to depend on high aid, further reducing their ability to tax, and making countries unable to fund their own development over the longer-term. The evidence for this is also rather weak.<sup>29</sup> As will be discussed in the next section, if wisely used, aid can actually encourage higher taxation, savings and investment, including by the poorest citizens of Low Income Countries (LIC), accelerating the growth of their countries.

However, there are other reasons why reducing aid dependency is important. Its strong negative effects include:

### 2.1.1 Loss of policy autonomy

Aid dependent governments can lose the space to design and implement their own home-grown development policies. This can occur as a direct consequence of aid, because donors insist, for instance, on recipient countries implementing the donors' policy priorities. Or, an indirect consequence, because countries are so busy engaging with donors that they fail to develop their own alternative policies, or because aid distorts government spending towards a particular sector.

### 2.1.2 Undermining accountability and responsiveness to national citizens, and delivery of services by government

When services are funded in considerable part by aid, this undermines the normal relationship whereby citizens hold their own governments accountable for delivering

services such as education, health or water. This is because governments focus their attention on relations with aid donors rather than with their own people, and citizens focus attention on provision of services by donors or NGOs. As a result, there may be less pressure for budgets to be transparent and accountable.<sup>30</sup>

### 2.1.3 Undermining predictability of government spending and therefore long-term planning

The volatility of aid flows (which is much greater than that of domestically-generated budget revenue,<sup>31</sup> but less volatile than foreign direct investment), persistent large shortfalls compared to pledges, and the lack of transparent reporting on them by donors to government, can make it impossible for LIC governments and their citizens to plan long-term and sustainable spending.

Finally, reducing aid dependency is seen as desirable by populations and governments in donor countries, especially in times of budget cuts.

So whilst real aid is beneficial to poor people in poor countries, aid dependency does have negative impacts – indeed, it sets up a dynamic which makes it harder for aid to be real. So it is worth examining aid dependency more closely.

## 2.2 WHICH COUNTRIES ARE MOST AID DEPENDENT?

The table on page 21 shows the 20 most aid dependent countries in 2000 and 2009. Three issues emerge from this:

- Most of the top 20 are countries affected by conflict or internal political turmoil. Though aid may sometimes have contributed to such conflict by propping

up repressive regimes (eg in DRC/Zaire), one main cause of high aid dependence is political instability or conflict.

- Many of these, and most of the remaining aid dependent countries, have poor education, health and infrastructure. Many are also small islands or landlocked countries with few natural resources. They are faced with a myriad of structural barriers to development – which are causing aid dependency.

- The poorest countries have been constantly hit by shocks – natural and man-made environmental disasters, falling commodity prices, or eruptions of conflict, which undermine their development and make them aid dependent. Shocks tend to deepen aid dependence for a time.

So the most aid dependent countries tend to be countries which have suffered from shocks, or for whom development is particularly difficult for structural reasons.

## 2.3 AID DEPENDENCY HAS FALLEN SHARPLY

Many critics of aid talk as though aid dependency is a permanent state. It is not, as the graph shows. In fact, after rising for the previous 20 years, average aid dependency of low income countries has fallen very sharply over the last decade or so. Since 2000 average low income country aid dependency has fallen by a third (12% of expenditure). The number of LICs relying on aid for 30% of their expenditure has fallen from 42 to 30.

This is because in 1975-85, most LICs were buffeted by oil price rises and commodity export falls and had poor policies, and in 1985-95 they were

“Aid dependency has fallen in Ghana from 46% to 27%; in Mozambique from 74% to 58%; in Rwanda from 86% to 65% and in Nepal from 53% to 34%.”

undergoing deflationary structural adjustment programmes and had high debt burdens. They therefore suffered very low growth and had to cut expenditures in real terms. But since 1995, many have seen rapid growth in income, budget revenue and expenditures. In the 1980s and 1990s aid dependence rose when aid was stagnating and largely ineffective. Since then, aid dependence has fallen sharply even though the absolute quantity of aid has been rising fast. Aid flows have trebled since 2000, to the countries which have reduced their aid dependence fastest, while they have only doubled to other countries.<sup>32</sup> But aid dependency has still gone down – because although aid has been rising, growth has been rising faster, enabling countries to mobilise more resources themselves.

Growth is of course not sufficient to achieve poverty and inequality reduction. But it is necessary, to create the resources for development. The right kind of growth can reduce poverty and inequality directly, by expanding poor people’s opportunities to sell products and services, and by boosting employment. It can also reduce it by creating wealth that can be taxed, and spent on public services which benefit poor women and men. This latter impact means that, where a government is committed to poverty reduction and accountable to its people, the positive impacts of aid on human development can be replicated by domestic resources.

Aid dependency has gone down dramatically in most of the countries featured in this report between 2000 and 2009. In all of these countries human development (measured by the UNDP Human Development Index, which measures income per person and access

to health and education) has at the same time improved, dramatically in some of them.

Finally, it is important to realise that only a small number of countries have a level of aid dependence which might even theoretically have a major negative effect on growth. Those analysts who have looked most closely at the issue (in particular examining the types of aid which go via recipient governments, and those which might be expected to have any effect on growth) find that aid has negative effects only if it goes above 15-20% of GNI (which would limit this potential effect to only 10-20 countries.<sup>33</sup> A similar threshold for aid/budget expenditure, at 40%, would confine the potential impact to 23 countries).

For most other countries, far from aid dependency limiting growth, aid dependency is falling as growth and human development occur. This is why, as the next chapter shows, real aid can contribute to reducing aid dependency, by accelerating development.

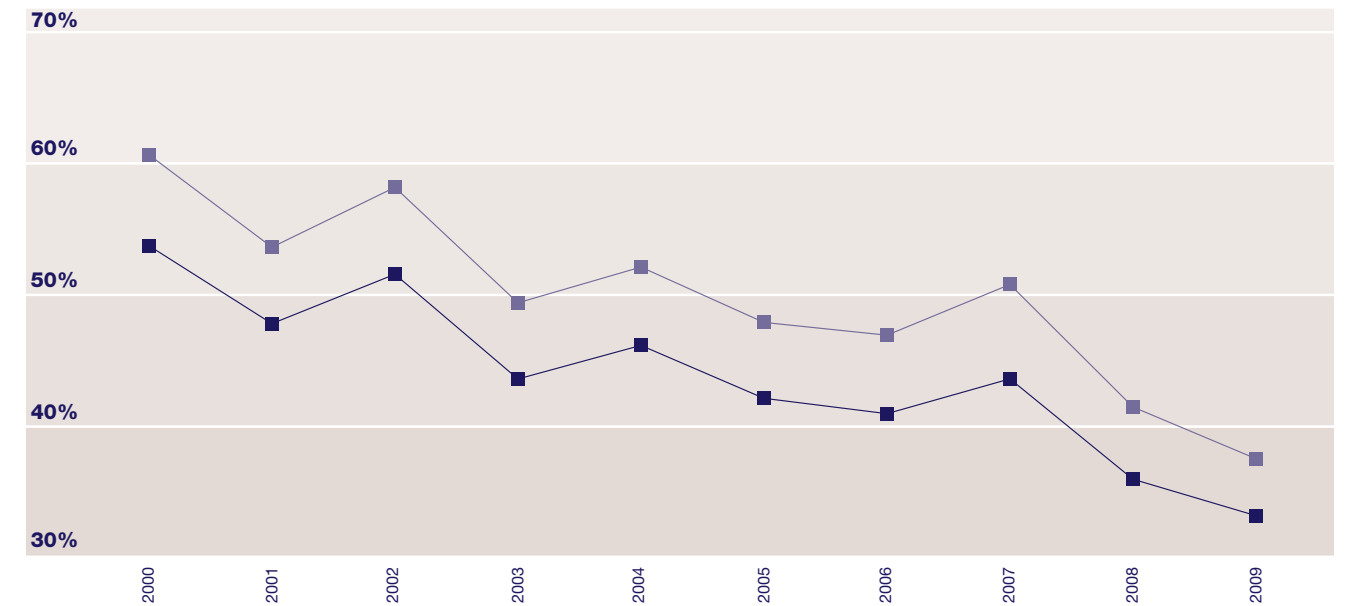
**TABLE OF 20 MOST AID DEPENDENT COUNTRIES IN 2000 AND 2009**

In this table ‘Percentage’ is country programmable aid as a % of total government expenditure.

Definitions: LDC - Least Developed Country; SIDS - Small Island Developing State; LLDC - Land Locked Developing Country

2000 COUNTRY	%	LDC	SIDS	LLDC	FRAGILE STATE	2009 COUNTRY	%	LDC	SIDS	LLDC	FRAGILE STATE
Sao Tome & Principe	389.35	●	●		●	Afghanistan	199.00	●		●	●
Timor - Leste	334.73	●			●	Sierra Leone	92.00	●			●
Sierra Leone	96.86	●			●	Liberia	88.50	●			●
Solomon Islands	88.78	●	●		●	Guinea - Bissau	72.90	●	●		●
Rwanda	85.68	●				Rwanda	65.00	●		●	●
Zambia	83.74	●		●		Solomon Islands	64.40	●	●		●
Guinea - Bissau	78.67	●			●	Vanuatu	63.50	●	●		
Laos	76.21	●		●		Gambia	62.40	●			●
Mozambique	74.01	●				Burundi	61.80	●		●	●
Mali	69.92	●		●		Haiti	59.90	●	●		●
Vanatu	67.24	●	●			Mozambique	58.00	●			
Niger	66.96	●		●	●	Central African Rep.	56.70	●		●	●
Cambodia	65.26	●				Uganda	55.90	●		●	●
Comoros	59.84	●	●		●	Congo, Dem. Rep.	53.10	●			●
Tanzania	57.68	●				Ethiopia	52.50	●		●	●
Burkina Faso	56.51	●		●		Tanzania	51.80	●			
Uganda	56.06	●		●	●	Burkina Faso	49.30	●		●	
Senegal	54.73	●				Kosovo	45.60				
Gambia	54.50	●			●	Zambia	43.90	●		●	
Nepal	52.80	●		●	●	Mali	40.20	●		●	

**AID DEPENDENCY**



This is calculated by the percentage of country programmable aid (CPA) as a percentage of overall government expenditure in each country.

LDCS AVERAGE

LICS AVERAGE



**Issa Omari**, chairperson of Miyuyu village, Tanzania. The village chairperson is elected by the community to give people a voice in political decisions and budget tracking.

PHOTO: ANDREW MCCONNELL/PANOS PICTURES/ACTIONAID

## CHAPTER 3 REDUCING AID DEPENDENCY THROUGH COUNTRY LEADERSHIP

One of the many reasons aid dependency is falling relates, paradoxically, to aid itself. When aid is given in such a way that it supports poor countries to lead their own development, be more accountable to their own people, and mobilise more of their own resources, then aid itself contributes to reducing aid dependency.

This section looks at how this can be achieved. The key to reducing aid dependence is strong leadership by the recipient country rather than by the donors, and for donors to support – not hinder – this.

“Countries with governments that are both capable and committed to national development should be able to handle relatively large amounts of aid well. The strategy for reducing their aid dependence would be for aid to rise for a period as needed and then to taper off.”<sup>35</sup>

It is difficult for poor countries to refuse finance because despite all the problems of aid overriding national autonomy, the problem is still that developing countries cannot make their cash stretch to cover their needs. A country may adopt good policies and resolve only to deal with donors who agree with its aims. But in the real world, when budgets are short and citizens lack services, governments will find it difficult to reject funds with less than ideal conditions. “Will my country refuse aid that doesn’t fit with the policy? It’s hard to refuse. You really need the funding,” says a senior aid official.

### 3.1 THE SUCCESS STORIES

Even the most ardent critics of aid acknowledge the success stories of countries which have ended their aid dependence. Botswana, Korea and Taiwan were all highly aid-dependent in the 1960s and 1970s, as were European countries and Japan after World War II, but they all graduated from aid dependence. Botswana, cut aid/GNI from 30% to 2%, and aid/expenditure from 60% to 6%, between 1975 and 1995.<sup>34</sup>

#### 3.1.1 How did these countries achieve this? Their policies and strategies included:

- Strong leadership and clear policies for national development, combining centralised strategic planning with protection of local industries and market-based growth, which aid donors were expected to support.
- Aid investment in infrastructure such as roads, education, and in supporting increases in tax revenue and domestic savings and investment, as well as improving foreign currency earnings through exports. They did this as well as using aid to support human development for its own sake.
- Aid was used to develop their own national institutional capacity and skills from weak initial levels.
- Botswana had a main export - diamonds - for which prices rose continually from

the 1960s, and for which the country negotiated a good revenue-sharing deal.

- All three countries determined their own strategies with relatively little interference from external sources.
- They reduced dependence gradually over 15-25 years, allowing them to continue to use aid until they had put infrastructure, and higher tax and savings in place.

In other words, one of these countries’ key routes to reducing aid dependence over the longer-term, was using real aid to promote development. High initial aid levels helped them to graduate.<sup>36</sup>

Aid critics treat these as exceptional stories which other countries are unable to repeat because they are stuck in an aid dependence trap, but they are not. Fourteen of the 30 most aid dependent countries in 2000 reduced their dependence by more than 20% of expenditure by 2009, and the average dependence of these 30 countries fell by 36% of expenditure over the same period.

### 3.2 HOW DEVELOPING COUNTRIES ARE REDUCING AID DEPENDENCE:

#### 3.2.1 Country leadership on development and aid<sup>37</sup>

In the long run, sustainable development can only happen when a developing

country leads the process itself.<sup>38</sup> Having a strong national development strategy with clear policies and results-oriented goals and indicators, is an important factor contributing to reduced aid dependence. The 16 countries which were aid dependent in 2000 and are judged in the latest Paris Declaration survey to have developed strong development strategies, have reduced their aid dependence by an average of 13% of budget expenditure since 2000 (even though these countries are also attracting more aid because of the high quality of their strategies). The ActionAid survey conducted for this report finds that this is one of the areas in which the most progress has been made. Six of the seven countries surveyed –Nepal, Rwanda, Tanzania, Sierra Leone, Cambodia and Malawi – have undertaken consultations to prepare development plans, and have multistakeholder bodies overseeing them.<sup>39</sup>

But leadership on aid issues is just as important. The UN Development Cooperation Forum (DCF) and aid recipient countries are promoting, at national level, “mutual accountability” between donors and recipients for the delivery and results of aid and development spending. Eleven of the 22 countries which reduced their dependence by more than 15% of expenditure in the last decade, are among the 18 countries which are the most advanced in developing these processes.

This involves:

- a clear national aid policy including a locally-driven aid quality and results monitoring framework
- annual targets for how each individual donor and the government should comply with the policy
- annual reports and review meetings to assess donor and recipient performance transparently.<sup>40</sup>

Many of these accountability processes are at early stages, but they nevertheless show that an increasing number of governments are prepared to lead the relationship with aid donors. Countries most advanced in this process, Benin, Mozambique and Rwanda, have set targets for individual donors to meet. This leadership has resulted in fundamental changes in the ways donors provide aid, including increased shares of budget support, greater predictability, more transparency, and more use of national financial management and procurement systems. This has applied even to donors whose global performance (for example against Paris Declaration indicators) has been poor, because peer pressure from other donors is applied. For example, Italy’s aid in Mozambique has improved in response to the Performance Assessment Framework there.<sup>41</sup> The recipient countries have also made dramatic improvements in the quality of their development strategies, focussing more aid and spending on producing development results, and improving public financial management and procurement in order to reduce corruption and increase value for money.

Countries such as Afghanistan, Cambodia, Ghana, Liberia, Nepal, Rwanda, Sierra Leone, Uganda and Vietnam have set reducing aid dependence as a key medium-term goal in their national development or aid management policies. Ghana’s new aid policy states: “The Government of Ghana has taken cognizance of the need to reduce dependence on aid in the medium to long term, and therefore intends to redouble its efforts at mobilising non-aid resources to fund its development objectives.”

The Government of Uganda has gone further. To ensure that donors tackle the other causes of aid dependence, it has designed a specific set of goals for its

“Countries like Benin, Mozambique and Rwanda have set targets for individual donors to meet. Their leadership has resulted in fundamental changes in the ways donors provide aid.”

donors to achieve “beyond aid”, on issues including agriculture, trade, tax evasion and incentives, climate change, technology transfer, migration and regional integration. Progress on these issues will also be discussed annually by the government and its partners, with parliament and civil society contributing fully.<sup>42</sup>

### 3.2.2 Accountability to domestic stakeholders

In many of these countries, although not all, increased accountability to domestic stakeholders has played a powerful role in improving the results of aid – and of broader budget expenditure – and thereby reducing long-term dependence. These structures have varied across national audit offices, parliamentary public accounts committees, decentralised agencies, and community accountability initiatives. Accountability has worked best when it has combined strong community-based monitoring with high-level representatives such as parliamentarians, policymakers or officials being prepared to be held to account. Evidence for these successes comes from sources as diverse as the African Development Bank on Ghana and Senegal; Oxfam on Malawi and the World Bank on Uganda.<sup>43</sup> The case study from Ghana provides an example of the impact of such accountability in Ghana, drawn from ActionAid’s work on promoting domestic accountability around the world.

However, a lot more needs to be done. The UN DCF survey for 2010 found that only 6 countries had involved parliaments, local governments and civil society fully in national mutual accountability processes.

The ActionAid *Real aid* survey found that low quality and level of inclusiveness and participation in mutual accountability processes was a major problem for almost all countries’ parliaments, Civil Society

Organisations (CSO) and citizens. This was partly due to government, and sometimes donor, reluctance, but also to organisational and financial constraints, and absence of clear legislation institutionalising participation. This matches repeated concerns expressed by stakeholder groups at the high-level symposia organised by the UN Development Co-operation Forum, and in preparatory statements for the Aid Effectiveness Forum to be held in Busan in November 2011.

Another concern is poor national-level transparency. While a few countries such as Malawi and Mozambique have their aid information systems openly accessible online, many do not, and lack of freedom of information or other legislation guaranteeing transparency is a major problem in asserting their rights. Freedom of Information laws in Kenya, Nepal and Sierra Leone have been helpful in getting specific information released, but less so in providing general access to aid information.

On the positive side, 5 of 7 countries in the ActionAid *Real aid* survey indicated that national development plans had been prepared and are permanently monitored by multi-stakeholder bodies, such as the Cambodia Development Cooperation Forum and the Nepal National Development Council. However, the actual participation of CSOs in these bodies, in most countries is weak and limited to a few organisations, so that their influence on development plans and policies is low.

The constitution or legislation in Kenya, Nepal and Rwanda guarantee women’s participation (women being a key domestic stakeholder group), though this does not necessarily translate into strong gender mainstreaming in planning, budgeting or sector policies, except in

Rwanda where gender issues are fully mainstreamed and monitored.

Similarly, involvement of CSOs and parliament in the formulation and monitoring of aid policies has been relatively low. Cambodia and Uganda have consulted their parliaments about their aid policies, but involvement of parliamentarians in aid oversight remains weak even in multiparty democracies such as Tanzania and Zambia, as well as Cambodia and Vietnam.<sup>55</sup> Civil society has generally not been consulted at all – or only at the last minute – in aid policy design. But civil society and parliament are even worse off when their government has no declared detailed policy – as there is no basis on which to hold government or donors to account for funds or results.

### 3.2.3 Aid to generate other development finance

Many recipient countries have placed a special focus on ensuring that the aid they receive helps them to mobilise other forms of development financing, particularly domestic. These include:

#### 3.2.3.1 Aid for tax systems

Cambodia, Ghana, Guyana, Kyrgyz, Mali, Mozambique, Rwanda, Senegal, Tanzania, Uganda and Zambia are among the many countries which have benefited from donor support to increase their tax revenue collections. The support allows countries to make tax collection more efficient, raise the public profile of taxation and its benefits, and review and improve tax policy. As a result of these programmes, they have increased their revenues by between 4% and 8% of GNI,<sup>63</sup> allowing them in turn to reduce their dependence on aid. 15% of GNI in tax revenue is a commonly accepted minimum figure for countries to aim for.<sup>64</sup>

A good example of progress is Rwanda. In 1998, the Government used part of a grant of £20 million from the UK government, to set up the Rwandan Revenue Authority. Since then the UK and other donors providing support have helped to develop the revenue authority to the point where it now collects the value of that original grant every four weeks.<sup>65</sup>

#### 3.2.3.2 Aid for domestic savings and investment

Multiple initiatives have been introduced to increase domestic savings and investment instead of relying on foreign savings and investment through aid and FDI. These include the development of new financial instruments such as public and private sector bonds into which citizens of low-income countries can put their savings rather than sending them to overseas bank accounts. There has been some remarkable progress: since 2000, domestic savings have risen by 7% of GNI in Africa<sup>66</sup> (mainly reflecting the performance of resource-rich countries).<sup>67</sup>

Aid funding channelled to microfinance, if done well, can increase savings and investment and smooth consumption for the world’s poorest citizens. Global aid flows used for this purpose have surged dramatically in the last decade, reaching more than US\$5 billion in 2010. Rapidly growing programmes in low income countries such as ASA and BRAC in Bangladesh, ACLEDA in Cambodia, Xac Bank in Mongolia or CRDB in Tanzania are successfully promoting self-sustaining rotating savings and loan systems which rapidly become independent of aid flows.<sup>68</sup> And countries are increasingly establishing nationwide microfinance systems – for example through the National Microfinance Bank in Tanzania – rather relying on individual donors or NGOs to fund small groups.

## THE TRAFFIC LIGHTS SYSTEM - HOW RWANDA HOLDS DONORS TO ACCOUNT

“Privately ‘green’ donors do not miss opportunities to compare and contrast their scores with those in the red, an example of the dynamic Rwanda has created.”

With the support of a significant amount of foreign aid, Rwanda has made great strides towards meeting the UN’s Millennium Development Goals (MDGs). Universal primary education has almost been achieved, rising from 62% in 2000 to 94% ten years later. Efforts to tackle child mortality, promote gender equality and combat the spread of HIV/AIDS and malaria means Rwanda is on course to achieve many of the MDG targets by 2015<sup>44</sup>: optimistic Rwandan ministers say all the goals are in reach.

This progress has been made at the same time as Rwanda has reduced its dependency on foreign aid. Aid as a percentage of government expenditure has dropped from 85% in 2000, to 45% in 2010<sup>45</sup>. The case of Rwanda’s transformation over the last decade reveals how strong country ownership over aid spending, coupled with donors increasing their ‘real aid’ contributions and increased domestic resources can combine to reduce a country’s dependency on foreign aid. Ronald Nkusi, Director of the External Finance Unit in the Finance Ministry explains, “We have shown donors that when we are in the driving seat – deciding how to allocate aid money ourselves – we spend donor money more effectively. Donors have responded to the results we have delivered by giving us more and more say over how we use their aid. It is this model of partnership, where we take the lead and oversee how, where and when aid money is spent, that will help us reduce our long term dependence on aid”.

### DONORS USE RWANDA’S SYSTEMS

In 2006, building on the recommendations on aid effectiveness from Paris and Accra, Rwanda’s new National Aid Policy *Vision 2020*<sup>46</sup> created the aid policy architecture to coordinate its economic development and poverty reduction strategy – and crucially, align donors to these ambitions.

The Ministry of Finance and Economic Planning’s *Donor Division of Labour in Rwanda*<sup>47</sup> has gone further and mapped government and donors aid projects and spending – allowing for identification of overcrowded and poorly funded sectors. This has redistributed aid across sectors, reducing duplication and transaction costs. Rwanda’s Single Project Implementation Unit oversees all domestic and external projects – allowing donors to use Rwanda’s own procurement and financial systems, cutting duplicate systems and costs.

### RED LIGHTS SHOW PRESSURE ON DONORS

Rwanda has introduced regular and transparent mutual accountability frameworks to measure progress. Each year it assesses its own and donors’ performance, using a traffic light system to identify progress and problem areas.<sup>48</sup> Green lights indicate that donors are meeting aid effectiveness obligations, such as budget support and using the governments own financial systems, red lights indicate where Rwanda is pressing donors to go further. Privately ‘green’ donors do not miss opportunities to compare and contrast their scores with those in the red, an example of the dynamic Rwanda has created by taking the lead in overseeing aid spending in its own country.

Confidence in the government of Rwanda’s capability in spending aid money effectively, making spending transparent and accountable has led many donors to increase their budget support.<sup>49</sup> Donors also cite Rwanda’s zero tolerance approach to corruption, as recognised by Transparency International,<sup>50</sup> and its clear vision for development, as other good reasons to increase real aid to Rwanda. Between 2007 and 2010, aid as budget support doubled;<sup>51</sup> since 2008 the World Bank has increased budget support from 37% to 83%, the European Commission from 23% to 70%.<sup>52</sup>

Improving the quality of aid and placing more of it in the hands of the government has not been the only factor in Rwanda’s reduced dependency on the aid. As we explain later, Rwanda has benefited from a radical overhaul of the Rwanda Revenue Authority, with support from the UK’s Department for International Development (DFID). Rwanda quadrupled the amount it collects in taxes between 1998 and 2006. The tax base remains low but increasing, while foreign direct investment and a competitive private sector have yet to take off significantly, meaning it may take another decade or so for Rwanda to grow its tax revenue much further. However, from the President downwards, Rwanda’s huge effort to mobilize its own domestic resources looks set to continue reducing dependency on donors.

Despite progress, significant challenges remain, not least because Rwanda’s aid dependency remains high, even by sub-Saharan Africa standards. Rwanda is now placing an emphasis on high tech, transport and energy infrastructure in a bid to spur rapid growth and reduce its dependency on donors.<sup>53</sup> Donors are also placing emphasis on governance, media freedom and accountability. Many, such as the UK’s DFID and the United States Agency for International Development (USAID), are placing resources into strengthening civil society organizations and parliament to improve domestic scrutiny and accountability over government spending.<sup>54</sup>

## NEPAL – AN EARLY AID POLICY ADOPTER<sup>56</sup>

“Nepal has had its own aid policy since 2002, and many of the concerns it raised were later echoed in the Paris aid effectiveness process.”

Nepal is one of the poorest countries in the world but has made impressive progress against poverty, showing the most improvement of any country on the Human Development Index between 1980 and 2010. More than four out of five children are now in school, girls as well as boys – up from one in five in 1970.<sup>57</sup> And starting from a low base, Nepal is on track to meet all the health MDGs.<sup>58</sup> This includes a 50,000-strong force of women volunteer health workers, whose role in expanding access to basic maternal and child health services is vital.

Aid to Nepal has doubled since 2000. Despite this, aid dependency is falling – aid was 53% of government spending in 2000 and 34% in 2009. Meanwhile tax revenue stood at 15% in 2009. “There is no alternative to mobilising domestic resources,” says Keshav Acharya, an advisor in the Ministry of Finance.

### QUALITY OF AID IMPROVES IN NEPAL

Nepal has had its own aid policy since 2002, and many of the concerns it raised were later echoed in the Paris aid effectiveness process. The policy acknowledges that aid is integral to mobilising resources for development, but also sets out a long term aim to enhance self reliance by mobilising domestic resources. It articulates the importance of aligning aid with the national goal of poverty reduction, of moving from projects to budget support, and of transparency in the supply and utilisation of aid.

Despite many continuing problems, aid quality in Nepal is improving. In particular, public spending on health and education has increased as a result of aid to these sectors, and sector wide approaches (SWAPs) are working well. Acharya says, “both donors and government are happy with the way these are working, and they have been extended.” Another official says that the SWAPs have led to more efficient co-ordination between donors.

Use of SWAPs has also reduced the use of tied aid in the health and education sectors<sup>59</sup> and has enhanced division of labour amongst donors. Overall, the Nepal Paris Declaration Evaluation says, “the education sector is demonstrating most of the hallmarks of a successful post Paris sector wide programme.”

In the more complex health sector, there has been progress over the last 5 years towards clear sector level strategies, although issues of governance, excessive technical assistance and lack of skilled staff remain. The contribution of the Paris declaration to progress in the health sector is thought to be substantial.<sup>60</sup>

## COMMUNITIES IN GHANA MONITOR PUBLIC SPENDING<sup>61</sup>

Since the 1990s, multi-donor budget support – aid pooled by donors and spent by government – has increased in Ghana to 33% of its total aid. It has used this flexible and predictable money to fund several new initiatives, including (since 2005) the schools capitation grant. This is a small grant paid per pupil to schools, to abolish fees for exams, with each school choosing how to spend the remaining funds.

ActionAid supports the village community of Mampehia to ensure accountable spending at its primary school. Mampehia is a village overlooked by rolling hills, reached in a couple of hours from Accra, the last few miles via potholed deep red dirt road. The word Mampehia means ‘Women don’t want to live in poverty’, but its residents do live this way. They are mostly smallholder farmers, growing cassava and maize, plantains and yams, keeping a few chickens and goats, and earning about £20 a year after the harvest.

Rebecca Doduo, 86, has seen a few changes, “Things are improving, there has been development. Now there is a school, a road and a church. People don’t get sick as much, and nurses come to immunise the children once a month. We have healthier water. More people work as traders or teachers or in offices.” Rebecca has 14 grandchildren, from two years to 28 and like everyone in the village she helps the school through its parent teacher association (PTA). Many of the teachers are here alone, so she tells her children and grandchildren to fetch water for them, and gives them food from her farm.

Emmanuel Sackey, 60, is chair of the PTA. He has ten children, and the youngest, Mary, is still at school. He explains that children used to have to walk several miles to school but a decade ago the village decided it needed its own school. It formed a school committee, started classes and built a school ‘pavilion’ of sticks with a grass roof. ActionAid helped to fund a permanent building with 3 classrooms, and convinced the local government to manage the school.

### COMMUNITY HOLDS HEADTEACHER ACCOUNTABLE

The school now has 250 pupils, from pre-school to 16, and ten teachers, but since the government took over the school, the community has had to keep a close eye on its management. In 2005, the head refused to disclose how much money he received for the school, but when a teacher showed the PTA a cheque, it was evidence that money was going astray. The PTA got the head sacked.

In 2005, when the ‘capitation grant’ started, the community learned about their rights supported by ActionAid. They now have a say in how the grant is spent and monitor its use against the school’s improvement plan. It has been spent on replacing locks on the school windows and building houses for teachers, but people want to see many other things – improved buildings, water containers, books, extra uniforms for the poorest children, and footballs and seesaws for the new preschool, “so that the tinies will learn to love going to school”.

Emmanuel intends to ensure the PTA asserts its rights, following up in detail exactly how much money there is and how is it spent. As he says, “Education is a big opportunity for our children: even the little writing I can do lets me help hold the government accountable.”

“Education is a big opportunity for our children: even the little writing I can do lets me help hold the government accountable.”



## BUDGETS THAT INTEGRATE WOMEN'S RIGHTS ENSURE AID IS EFFECTIVE

Gender responsive budgeting can play a major part in ensuring that aid is spent effectively. Through analysis of government planning, programming and budgeting, it looks at the impact of these plans for both men and women and identifies how to address gender gaps in sector and local government policies, plans and budgets.

In some cases, it provides a firm evidence base to accurately determine how much needs to be spent to fulfil agreed national and local commitments to gender equality. In other cases Finance Ministries have led the way on gender responsive budgeting which resulted in the national budgeting process becoming more gender responsive, and advocates of women's rights have been able to set goals and monitor them to see how the finance has translated into resources and services for women.

In Nepal since 2007 each ministry has been required to score new programmes for gender responsiveness, looking at the participation of women in planning, building women's skills, share of women in benefits, increase in women's employment, and improvement in the quality of women's time use. Budget allocations which are positive for women have increased from 45% to 54% over 4 years.<sup>62</sup>

## 3.3 HOW CAN DONORS SUPPORT AID DEPENDENCY REDUCTION

Donors can proactively support developing countries to lead their own development and reduce their dependence on aid. How can they best do this?

### 3.3.1 Provide more real aid

First and most important, donors can maximise the proportion of their aid that is real aid (see Chapter 4 for more on this). It seems like a paradox that country programmable aid flows (the nearest OECD measurement to real aid) have trebled since 2000, to the countries which have reduced their aid dependence fastest, while they have only doubled to other countries. In fact, it shows that larger up-front aid flows are helping these countries to implement their development programmes, mobilise other sources of revenue, and thereby reduce their dependence.

### 3.3.2 Be more accountable and transparent

Second, they can live up to the documents they have signed globally, multilaterally and bilaterally which commit them to being held accountable by recipient governments and their citizens. At global level, donor performance is poor in meeting their Paris Declaration commitments, yet the commitments they have made have the potential to transform the quality of aid, and are a vital framework within which national aid policies and mutual accountability have been able to make progress. The Busan High-Level Forum on Aid Effectiveness in November 2011 needs to strengthen that framework by focussing on measures which will most increase the results of aid.

Many recipient countries have been having problems getting all donors to support their aid policies – especially DAC donors

which do not provide budget support, and non-DAC providers (global funds, southern governments and CSOs). But this is changing. Large non-DAC countries such as China are beginning to join accountability processes in several Asian countries such as Cambodia, Nepal and Vietnam. The Global Alliance for Vaccination and Immunisation and the Global Fund to Fight AIDS, Tuberculosis and Malaria are increasing efforts to coordinate their activities with government and in some cases letting governments run their programmes. CSOs are signing up to their own and global accountability standards – with most major UK development NGOs working towards signing the International Aid Transparency Initiative. EU donors and the United States have declared in 2010-11 that they will participate in national-level mutual accountability processes and respect individual donor targets, as well as that they will increase funding for accountability and transparency to parliaments and citizens.<sup>63</sup>

Donor transparency is also vital to successful accountability, with increasing numbers signing the International Aid Transparency Initiative to ensure common international standards. However, to promote genuine accountability it needs to go beyond raw numbers and include documents on project design, conditionality, procurement and other aspects. It also needs to be accompanied by strong support for national accountability structures and citizens, in both donors' own and recipient countries, in order to allow citizens to see and act on the quality of aid.

### 3.3.3 Support tax systems and microfinance

In spite of the success stories described above on tax revenue, domestic

savings and microfinance, less than 0.2% of aid is spent directly on helping developing countries to increase their budget revenues.<sup>70</sup> Similarly, most aid for microfinance is going to middle-income countries and not reaching the poorest countries or people.<sup>71</sup>

However, it is important to be clear that developing countries should set and prioritise their own economic development plans, and donors should ensure aid is able to support these, even if they are not in agreement with the proposed economic pathway. In no way should donors attempt to dictate, with conditions attached, the economic choices made by developing countries.

### 3.4 VALUE FOR MONEY - GET MORE OUT OF EVERY DOLLAR

One key additional way to reduce aid dependence is to get more results for every dollar, euro or yuan of aid spent on poverty eradication. Doing this frees up money to achieve more results for poor people. Many of the best ways to achieve this on a large scale are already reflected in the key issues in the Paris and Accra Declarations. Some of these issues – and some which are increasingly being brought to the table by southern stakeholders – are outlined below.

#### 3.4.1 Untying aid and using country procurement systems

The cost of building a kilometre of road in Ghana or Viet Nam falls by 30-40%<sup>72</sup> when it's built by a local company. In theory 90% of global aid can be used to pay local companies but in reality more than two-thirds of bilateral contracts still go to donor country enterprises. Complex procurement procedures stop contractors from the recipient country from using aid to boost employment and develop their own

skills and capacity.<sup>73</sup> When donors apply 'informal' tying such as non-transparent tendering, tendering in large lots which are too big for small companies from low income countries, LICs, or requesting eligibility criteria that developing country firms cannot fulfill – all of these can increase costs by 15-40%.<sup>74</sup> By untying US\$5 billion of aid between 2005 and 2007, donors may have increased its value by as much as \$2 billion. Even better would be to allow countries to apply sustainable public procurement policies, which take developmental, social and environmental criteria into account. These can help procurement work to achieve the MDGs by promoting the development of the local private sector, and within it those firms which most promote development by driving innovation, creating decent jobs, respecting core labour standards, being environmentally sustainable, and paying their taxes locally.

#### 3.4.2 Making aid more predictable, including cutting policy conditionality

Policy conditionality – making aid conditional on prescribed policy changes – remains one of the major sources of aid "unpredictability" and volatility. Conditionality is of course also inimical to country leadership and to focusing accountability on the relationship between the recipient government and its citizens. Conditions should be limited to following a strong national development strategy with targets approved by the countries and not pushed by the donors, respect for underlying basic principles such as human rights and introducing any financial management, procurement or anti-corruption reforms necessary to ensure that funds are well spent. Policy choices should be left to the government. If countries choose to establish macroeconomic frameworks in conjunction with the IMF, they should also be

sufficiently flexible and open to maximise spending of aid to accelerate progress to the MDGs. To assist governments in forward planning and efficiency donors should also commit their aid for the whole period of each country's national development strategy, which is typically 5 years. Eliminating volatility – where aid flows ebb and flow dramatically – would increase aid's value by 13-17%.<sup>75</sup> The Paris agenda includes a target for increasing aid predictability.

#### 3.4.3 Increasing speed of delivery

This is an issue not raised by the Paris Declaration or Accra Agenda but often raised loudly by southern donor governments, as many of them tend to deliver considerably faster than some DAC and IFI counterparts. If, as suggested by the World Bank,<sup>76</sup> successful aid projects can have a rate of return of 15-20% a year, then each year of delay reduces the value of a project's returns by 15-20%. As some donors take 3-5 years longer than others to complete the same types of project, losses through delays are massive. Some delays are due to cumbersome recipient government procedures, which also need to be streamlined and accelerated.

#### 3.4.4 Using government rather than parallel systems

The Paris Declaration and Accra Agenda have as targets that donors should, wherever possible, use countries' own public financial management and procurement systems rather than establishing their own, and should avoid parallel project implementation units. This is because parallel units fail to create sustainable long term capacity, as well as adding substantially to transaction and overhead costs of aid – recipients indicate by between 10% and 20%<sup>77</sup>. Recipient countries also stated strongly

in Accra that they would prefer donors to use their (the recipient country's) monitoring and evaluation systems, as most do in Vietnam for example, rather than insisting on having separate reviews and evaluations of each project. Recipient countries obviously need to continue improving these systems – though many countries have already done so to the point where donors should be using the systems as a first option.

#### 3.4.5 Combating corruption

The main reason why donors insist on parallel procedures and systems (apart from familiarity with their own systems and jobs for those who run them) is that they are concerned about corruption or misuse of funds. But the results of the Paris Declaration implementation survey show that recipients are making major progress in improving their systems but donors are not following suit in channelling aid via them.

Aid has also been used successfully to combat corruption in many other countries including Azerbaijan, Kenya, Mozambique, Uganda, Zambia and Nepal, by investing in independent auditing, free media, community accountability, and parliamentary structures.<sup>78</sup>

#### 3.4.6 Making sure technical assistance is used effectively

As discussed in Chapter 4, technical assistance (TA) is frequently donor driven and more expensive than it could be. The key issues for recipients here are value for money and sustainability so that TA does not have to be continued or repeated, but instead genuinely contribute to development. The ActionAid survey reports continued pressure from donors on recipients to accept unnecessary TA in 5 of the 7 countries (Nepal, Cambodia, Malawi, Tanzania, and Rwanda) with

**“In Nepal aid dependency is falling – aid was 53% of government spending in 2000 and 34% in 2009.”**

no rigorous assessments of the costs and benefits since the *Real aid 2* report.

Former Ghanaian aid official Hudu Siita, who now works as a private consultant, illustrates his experience of working with donors on TA: “Donors differ. I dealt with Canadian International Development Agency (CIDA) in the early 1990s. CIDA was very flexible. We discussed things, and if I didn’t approve something CIDA didn’t buy it. Others were different and not as transparent.”

### 3.4.7 Providing general and sector budget support

Where countries are committed to poverty reduction and human rights, budget support means real ownership of development aid and therefore a greater chance to escape aid dependency.

There is also growing evidence that budget support provides greater efficiency and value for money, and stronger results, compared to project aid. It has a positive, demonstrable impact on delivery of essential services, by lessening the bureaucracy associated with receipt of aid funds, freeing up time and resources for better investment and improving national planning and budgeting processes. Evaluations from OECD, the EU, think tanks such as the Overseas Development Institute, as well as NGOs like Oxfam, have concluded that budget support increased the quantity of service delivery in almost all countries, especially in basic education and health.<sup>79</sup>

Other studies show that budget support to the health and education sectors led to growth, improved planning, budgeting and financial management, strengthened government accountability and ownership of policies as well as being more predictable. It enabled the introduction of free basic

education and health services in Mali, Rwanda, Uganda and Zambia, and improved Local Government accountability to citizens in Rwanda, Tanzania and Uganda.<sup>80</sup> Health and education sector support in Nepal has also considerably improved service delivery, accountability and dialogue with donors.<sup>81</sup>

One of the main criticisms of budget support is that it is difficult for donors to trace exactly what their money has been spent on and its results. However Hudu Siita points out that project aid carries the same problems from the point of view of the people trying to coordinate development strategically in a whole country. “A couple of months ago I did some work, funded by the Ministry of Finance and The World Bank Office in Accra on the Public Expenditure Review. It was very difficult to get information on donor project aid expenditure. In the end I settled on government of Ghana spending which included only budget support. You are simply unable to know what all the project aid expenditures are.”

Overall, the results and value for money agenda of many donors, which is shared by recipient governments, should be carried out in ways which reinforce real aid and development effectiveness, and help to reduce aid dependency. This also means including in the definition of results and value for money, less tangible, but relatively easily measurable, results such as empowerment, rights and sustainability.

### 3.5 AID DEPENDENCE CAN DROP DRAMATICALLY

Judging by the long-term forecasts of aid which low income countries are agreeing with the IMF, they all want to reduce aid dependence over the medium-

term, in order to have more autonomy over their own development policies.<sup>83</sup> In fact all these countries are planning to reduce their aid dependence much faster than Botswana, Korea or Taiwan – even though many, especially those which are post-conflict or post-disaster, see a need for continuing high aid flows for the next few years to rebuild their economies and societies.

The question is whether these forecasts of reduced aid dependence are realistic. If donors increase the amount and proportion of high quality real aid, and

target it to building countries’ own capacities, infrastructure and domestic sources of development financing, and supporting their own development strategies, then we can realistically expect to reduce aid dependence dramatically for recipient countries.

## TAX JUSTICE

Increasing domestic revenue is a key way that developing countries can increase their development resources as well as reduce their dependency on aid. Furthermore, it binds governments in a social contract with their people, ensuring improved accountability.

But there is also an international perspective in this area. The Organisation for Economic Co-operation and Development estimates that Africa loses more in tax revenue to tax havens than it receives in aid. Some multinational companies dodge taxes, in particular, by shifting their profits around the world through transactions with related group companies, a process known as transfer pricing.

### ACTIONAID IS CAMPAIGNING FOR A RANGE OF ACTIONS TO TACKLE THIS. THESE INCLUDE:

- governments to increase tax transparency, obliging companies to report their financial accounts country by country, and joining a multilateral agreement of tax information exchange
- developing countries to strengthen their transfer pricing legislation, with support from international organisations as requested
- multinational companies to improve their policy on tax planning, ruling out certain practices and negotiating responsibly.

## PEOPLE'S POWER AND THE HIMALAYAN ROAD<sup>82</sup>

“The training opened our eyes and the social audit made us believe in people’s power,”

Gita Subedi, Nepal

### THE COMMUNITY WHO KEEP TRACK OF LOCAL SPENDING

Bharathi Chaudhury is a smallholder farmer, with nine children. She lives in Ratnanagar Municipality, 150km south west of Kathmandu in Nepal. A few years ago she took part in ActionAid-supported training, on budget tracking. She then joined the budget tracking group, Sunaulo Samuha, that was subsequently formed, hosting it in her house. She said, “before the training, I had never gone out of home for a public cause. The training gave me an insight into being aware of our rights, and regular discussion gave me confidence. After joining Sunaulo Samuha, I have been engaging myself in public affairs, supporting others in need and speaking out for our rights.”

In 2007 the group decided to audit spending on the Himalayan road – crucial to the inhabitants of Ratnanagar. Recently constructed, it had already sunk in one place and started deteriorating in others. 40% of the cost of road construction was contributed by users, with the other 60% from local and national budgets. Bharathi was one of the group members with a direct stake in the road, as it runs directly past her house, and she had contributed cash towards its construction.

The group enquired from the local council how much had been spent on the road, how the money had been raised, and what the specifications were. Bharathi said, “Users were not informed how much was collected and where that was deposited until the social audit was organised by our group.” From this process, and a presentation to the group by a local authority planning officer, it emerged that the road had not been made to the thickness it was supposed to be, as well as being narrower than the 4 metres requested by local people and agreed. Despite this substandard work, spending on the project had been considerably above the cost estimate.

The contractor offered to mend the road in the places where it had deteriorated. And as Bishnu Sharma, budget training co-ordinator, says, “The social audit worked as a trigger for reform.” The group continued to lobby and an all-party ‘probe committee’ was formed, which rooted out many further irregularities in local spending.

## SUPPORTING GHANA'S SPENDING ON POVERTY REDUCTION

Ghana is making development progress. The proportion of Ghanaians going hungry has been reduced by three quarters in the past two decades. Almost eight out of every ten children, girls as well as boys, are now in school.<sup>84</sup> The country has had five consecutive free and fair elections. Growth increased from 3.7% in 2000 to 7.3% in 2008.

Development is politically important too. “Government is voted in on the perception of what development will bring. People compare the last government to the current one. There is lots of political discussion on the radio,” says a commentator. There is much still to do, but Ghana seems to be on a positive path.

Over the last 5-10 years, the Ghanaian government has increased spending in a number of areas including education and health, and introduced: the School Feeding Programme, an education capitation grant, a conditional cash transfer scheme for the poor a programme targeting youth unemployment, and a programme to reduce inequities between the north and south of the country. These have been reflected in the budget, with increased expenditures on social services and social protection between 2003 and 2007, although their share subsequently fell.<sup>85</sup>

### HOW MUCH AID IN GHANA?

Aid makes a significant contribution to Ghanaian spending. In absolute terms aid has increased from \$1 billion in 2003 to \$1.9 billion in 2010.<sup>86</sup> But, in common with many other countries, aid dependency has gone down, from 46% of government expenditure in 2000 to 27% in 2009. More than half the aid is delivered through projects, and about a third as budget support – a proportion which has increased modestly over the last decade.<sup>87</sup> Meanwhile, Ghana is a star performer within Africa on tax revenue, collecting 22% of GDP in tax.<sup>88</sup> And oil has recently been discovered there – a new and potentially massive source of revenue which will have far reaching impacts.

### GHANA'S OBJECTIVE IS TO REDUCE AID DEPENDENCE

Ghana's first ever aid policy, *Ghana Aid Policy and Strategy 2011-2015* has just been published. It sets objectives of reducing aid dependence, ensuring aid supports national priorities, and setting a donor performance assessment framework. The aid policy makes it crystal clear that budget support is Ghana's preferred aid modality, and it laments that “much assistance remains off plan and off budget, reflecting a lack of alignment with government priorities and systems”.

Veronica Sackey, Head of Ghana's Multi Donor Budget Support (MDBS) programme, says, ‘We have tried to deepen ownership of the development agenda, setting our own priorities and getting development partners to align. No development agenda with development partners [donors] in the driving seat will be sustainable.’ Sackey explained how MDBS conditions are taken from the national development plan and some are used as ‘triggers’ for further disbursement. In May 2011 Ghana met 11 out of 12 of its triggers. Another aid official said, “There are fewer conditions now. It's more of a discussion.” According to the Ghana Paris Declaration Evaluation, “The MDBS...has improved commitment and predictability of aid inflows...”

“No development agenda with donors in the driving seat will be sustainable”

Veronica Sackey,  
Head of Ghana's  
Multi Donor Budget  
Support programme.

### **THE PROBLEMS OF PROJECT AID**

Veronica Sackey said, "MDBS has played a key role in harmonisation. It's positive because it has reduced the cost of mobilising resources. There's a huge difference compared with project aid.... I used to work in project aid and I wouldn't want to ever again. There's a gamut of conditions dealing with different donors, missions, reporting mechanisms, procurement processes..."

Some of these problems are illustrated in a story from Hudu Siita. He was involved in the early 1990s in the elaborate, cross-cutting, CIDA-funded Northern Region Rural Integrated Programme (NORRIP). Because of the high profile the project enjoyed, the government gave counterpart funding. Clean water provision was the biggest element of NORRIP. The target was to get 350 boreholes; by the time Siita left in 1994 there were 250. But in 1994 CIDA cut NORRIP funding, at a time when many donors were making sweeping aid cuts.

Today lots of the boreholes are still functioning, because the project included training and equipment. But although the project still exists, government interest waned with the withdrawal of donor support. Far more boreholes are needed but there is no money to pay for spare parts for the drills, so new drilling has ground to a halt. The NORRIP has been moved from the Ministry of Finance to the Ministry of Agriculture, where it, "competes with other projects for scarce budgetary investment resources, since it has no donor support now to attract the big counterpart funding."

According to Siita, this kind of thing is less likely to happen if donors buy into the national development strategy rather than picking their own projects – and funding for work started is more likely to be sustainable. This can happen in part through budget support.

### **CIVIL SOCIETY AND GOVERNMENT ACCOUNTABILITY**

Samuel Zan Akologo, until recently chair of the CSO Ghana Aid Effectiveness Forum, is positive about the budget support process in Ghana. "Multi donor budget support acts as a consensus platform of government, civil society and development partners. It has created a structure where civil society organisations engage with the sector working groups and they all feed in to the central consultative group," he explained. This relationship has also been used by Ghanaian civil society to address other issues, for example input to the national development strategy.

This view is supported by the Paris Declaration Evaluation. "It is believed that the Paris Declaration has led to increased dialogue and consultative discussions on aid effectiveness, and inspired the development of the Ghana aid policy document." Furthermore, in the PDE stakeholder questionnaire it was "unanimously recognised that the quality of dialogue on public financial management had improved."

Adwoa Kluitse, Director of ActionAid Ghana, however has a caveat to this. She says that budget support is important for development, as long as funding for CSOs remains – both for programme innovation and for budget monitoring processes to hold government to account. Zan agrees that it is important for donor funding for CSOs to be pooled independently of government, rather than going via government.

Zan is concerned about the possibility that Ghana's new found oil revenue might lead, not only to reductions in quantity of budget support, but to a lessening of the quality of consultation with civil society and other stakeholders in Ghana – because the MDBS process, which has been an effective forum and multiplier, would be reduced.



**Mary Sackey**, a student at Mampehia junior high school, Ghana. The government has increased multidonor budget support to 33% of its total aid. It has used this flexible and predictable money to fund several new initiatives, including the schools capitation grant.

PHOTO: NANA KOFI ACQUAH/ACTIONAID

## CHAPTER 4 WHAT'S NEXT FOR REAL AID?

Allowing space for countries' own development plans to work is one attribute of what ActionAid calls real aid – and major donors have been providing more of it. But at the same time, there is still a lot of substandard aid out there. In this chapter, we look at real and substandard aid, and which donors provide which.

Real aid – the kind of aid that contributes to ending aid dependency – benefits and empowers poor people, either directly or indirectly. It supports developing countries to lead their own development, in their own way. It is accountable, transparent and predictable. Wherever possible it uses developing countries' own spending and monitoring systems, not parallel procedures.

We can also say what real aid is not. It is not spent on debt relief, which should be additional to any aid pledges given the joint responsibility of creditors and debtors for building up country debt burdens. It is not tied to overpriced exports of goods or services from the aid supplying country, or to unwanted or overpriced technical assistance. Whilst it must be spent, directly or indirectly, on poverty reduction, it does not impose policy conditions or allocation priorities on recipient countries. And it does not carry excessive administration costs itself.

#### 4.1 ACTIONAID'S REAL AID REPORTS

ActionAid has assessed real aid three times in *Real Aid* reports – in 2005, 2006 and in this report in 2011. Real aid has the following characteristics:

- it is targeted on the poorest
- it is counted only once as development assistance
- if it is tied to purchases from the donor country, these do not cost more than local purchases
- if it is technical assistance, it is wanted by the recipient and competitively priced
- it supports developing country leadership on development
- it is spent in the developing country not the donor country
- it is administered efficiently.

To assess real aid levels, we looked at aid from OECD DAC bilateral donors, for whom data is available. From the total, we subtracted:

- a proportion of the aid that does not go to the poorest countries
- aid that is doubled counted as debt relief
- a proportion of tied aid, approximating to the extra costs for the recipient country of having to purchase from the donor country
- a proportion of technical assistance, approximating to the amount developing

- countries themselves judge to be unwanted and overpriced
- a proportion of aid that fails to support country leadership, worked out using developing countries' own judgements of donors' effectiveness in this regard
- aid that never leaves the donor country, because it is spent on refugee or student costs there
- aid that is spent on administration, above a certain level.

The rest of this chapter examines real aid on the basis of these definitions. It uses the most up to date OECD data to make its calculations, and makes provisions for double counting. However, as DAC donors do not always supply transparent data even to the OECD, we have also used data from other sources.

#### 4.2 HOW MUCH REAL AID IS THERE?

In 2009, OECD DAC donors provided \$120 billion of aid to developing countries. Overall, we find that \$66 billion of this was real aid. This is a little over half of all aid. In absolute terms, the amount of real aid increased significantly between 2005 and 2009 – by \$24 billion. But the overall amount of aid increased too. The proportion of real aid has increased, but only a little – from around 51% to 55%.<sup>89</sup> Things are improving but not fast enough. As real aid is better value for

money than substandard aid, this finding shows the massive potential for donors to have more impact on reducing poverty and inequality.

#### 4.3 WHICH DONORS GAVE THE MOST REAL AID?

If we look at real aid as a proportion of total aid, in 2009 Ireland gave the highest proportion of real aid, at 86%, with the UK coming second at 85% and Luxembourg third at 83%. On the other hand, the lowest proportions are from Greece at 17%, France at 28% and Austria at 34%. Other large donors which do badly are Germany – providing 42% real aid, and the US at 43%.

It is also necessary to take into account how much aid donors give in the first place. If we look at real aid as a proportion of wealth, the best three performers are amongst those that give high amounts in relation to their overall wealth. Top of total aid here are Sweden and Luxembourg which both give 0.86% of GNI in real aid; third is Norway at 0.77%. The bottom three donors on this measure are Greece at 0.03%, Korea at 0.06% and USA at 0.09%.

#### 4.4 THE COMPONENTS OF SUBSTANDARD AID

So what of the portion of aid that is substandard aid? Overall substandard aid is 45.3% of aid. The largest portion of this – 14.7% of aid – comprises unwanted and overpriced technical assistance. The second largest amount is the aid that fails to support country leadership – the main subject of this report, at 13.6%. The other third breaks down as follows: 7% of aid is not targeted on the poorest, 3.5%

is double counted as debt relief, 2.6% is spent on refugees and 1.9% on students in the donor country; 1.6% is overpriced tied aid and 0.4% is admin costs.

In general, these proportions appear to have changed little in the last five years. The amount of debt relief has fallen significantly, so substandard aid in that category is a lower proportion. Tied aid has also fallen as a proportion.

##### 4.4.1 Poorly targeted aid – 7%

Aid should be spent to benefit the poorest and most vulnerable women and men, whether directly, for example by supporting public services, or indirectly, for example by supporting tax revenue collection which in turn can be spent on public services. However, instead of being focused on them, some aid continues to be allocated for a host of other reasons which benefit the donor country – for example, to buy geopolitical influence, to enhance commercial ties, or to support military objectives.

To measure aid targeting the poorest, we look at how much aid is spent in the poorest countries. This does not mean that all aid should be spent there, as many poor people live in slightly richer countries, but the majority of it should be targeted there. We count the same countries as 'poor countries' as we did in *Real aid 2*, and maintain the same assumption that 70% of poor people live in these poor countries, and 30% in slightly richer ones. Aid to slightly richer countries from any donor above 30% is counted as substandard aid.<sup>90</sup>

Nine of the 23 donors we look at gave more than 30% of their aid to countries not on our 'poor countries' list. Greece, Spain and Austria allocate particularly high proportions of their aid in

this way. The US, France and Germany do next worst, and are larger donors.

**4.4.2 Debt cancellation double counted as aid – 3.5%**

In 2002, in the Monterrey Consensus on Financing for Development, donors committed to cancelling debt without detracting from aid resources. Debt cancellation has been a vital weapon in the fight against poverty, removing a huge burden from the backs of the world’s poor. Much of it cancels payments which countries are making, allowing them to spend much more of their own money on health, education and other key social sectors.

However, considerable sums just cancelled debts which were not being paid, (but still contributed to poor countries’ onerous “debt overhang”), representing an accounting transfer among creditor agencies and reducing sums available for new aid. Debt relief is also billed up front, when the real benefits may take 20 years. Counting debt cancellation as aid is unjust given that debts were often incurred for purposes that had little to do with fighting poverty, and creditors should share the cost of these mistakes. Also, companies in donor countries have benefitted from commercial credits.

Therefore we believe that debt relief should be counted separately from aid. All debt cancellations payments made by donors are counted as substandard aid.

Debt cancellation has fallen sharply in the last few years, and now represents only 3% of ODA. Almost all 2009 relief came from France – to its former colonies such as Côte d’Ivoire and Cameroon – so France is the donor that incurs a significant substandard aid score in this category.

However, debt relief could rise sharply in the next few years if the independence of south Sudan leads to cancellation of its debts of \$39 billion, although this will be a temporary phenomenon.

**4.4.3 Poor quality technical assistance – 14.7%**

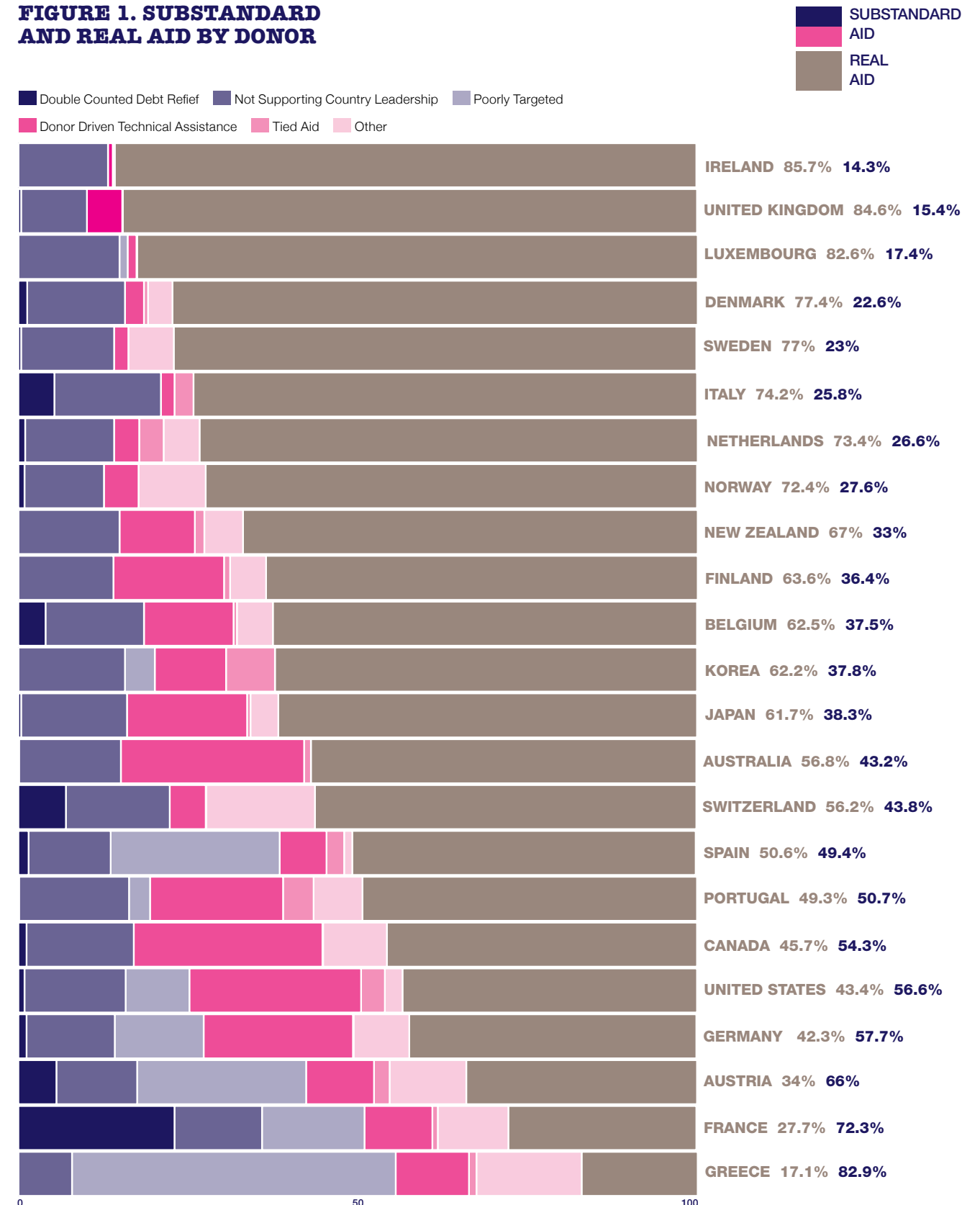
Technical assistance (TA) is outside expertise such as consultants, research and training, and can be a very good thing if it is wanted by the country and supports building of local expertise. However, if TA involves replication of national staff or establishing parallel institutions, it can distort country priorities and spend valuable money without doing any good.

For *Real aid 3*, we looked at the proportion of each donor’s aid spent on TA. We referred to recipient countries’ assessments, done for Development Finance International, of the effectiveness of different donors’ TA to them, and using this calculated the proportion of TA from each donor that recipient countries deemed effective. We counted the rest as substandard aid.<sup>92</sup>

The proportion counted as substandard aid ranged from 51 to 76%.

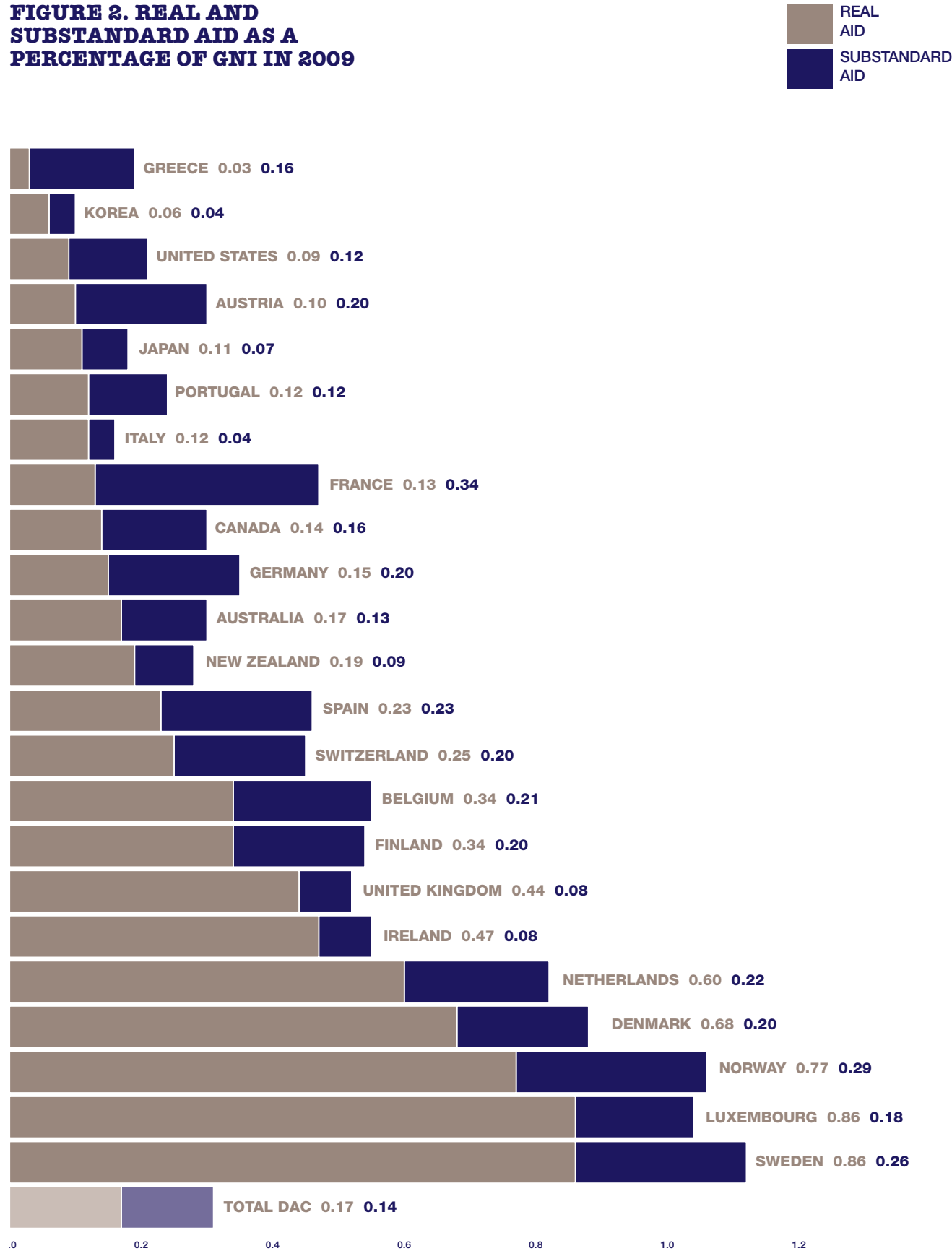
Overall around a third of global aid is spent on TA.<sup>93</sup> Some donors continue to provide extremely high proportions of their bilateral aid as TA. Australia, Canada and the US score particularly badly in this category. Ireland, Italy and Luxembourg do well. There is huge variation on how much substandard aid donors provide, partly reflecting the proportion of their aid given as TA.

**FIGURE 1. SUBSTANDARD AND REAL AID BY DONOR**

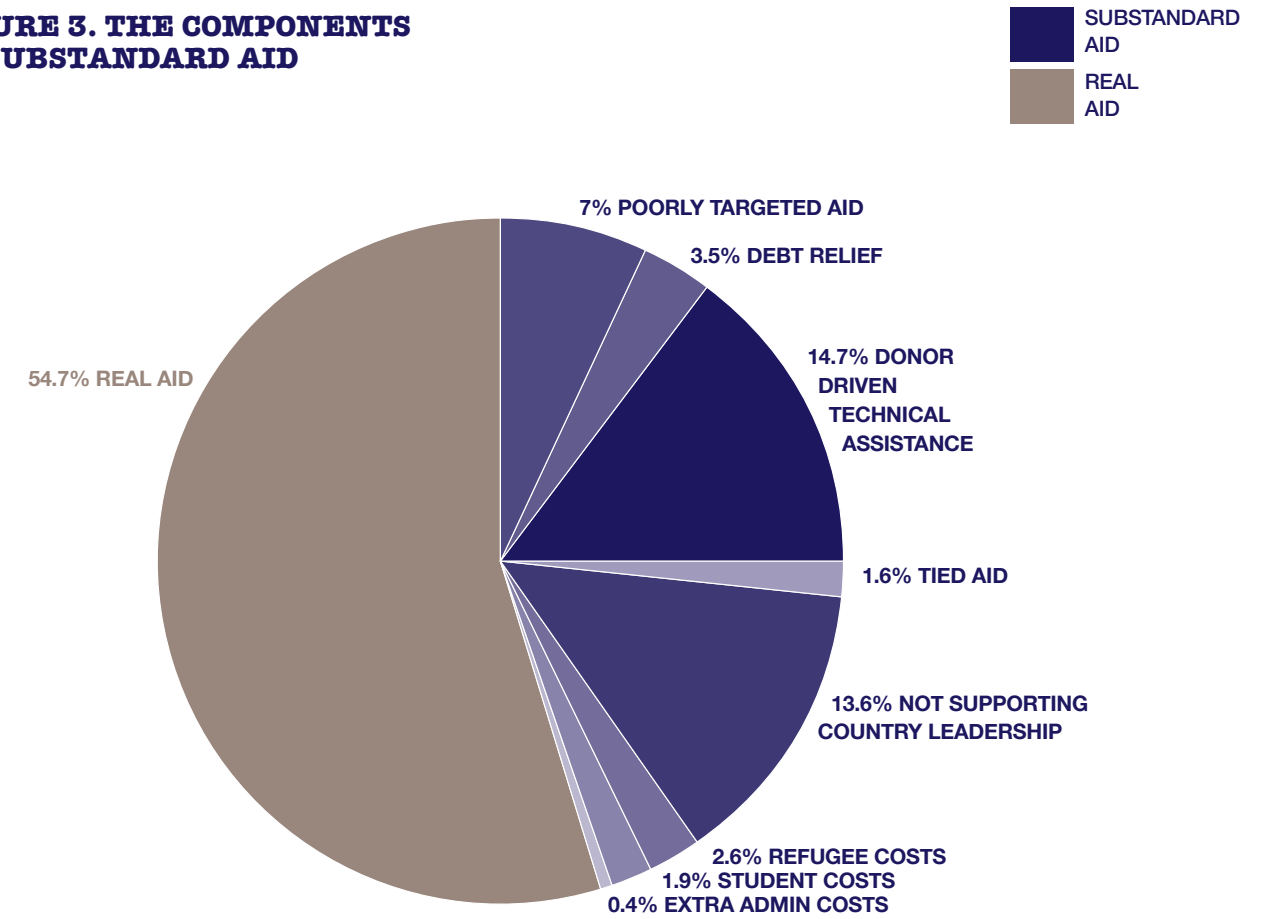




**FIGURE 2. REAL AND SUBSTANDARD AID AS A PERCENTAGE OF GNI IN 2009**



**FIGURE 3. THE COMPONENTS OF SUBSTANDARD AID**



**REAL AID AND GENDER EQUALITY**

According to the OECD, \$23 billion of bilateral aid in 2009 contributed to reducing gender inequality.<sup>91</sup>

This monitoring is done with the aid 'marker' system. Aid projects are marked by donors according to whether the issue in focus, in this case gender equality, is a 'principal' or 'significant' part of the project. Programme aid is sometimes also added in proportionately. The large majority of markers on gender equality do not mark it as a principal objective.

This system is complicated by the fact that not all donors use the gender equality marker, and those that do don't use it all the time. But the \$23 billion is only 28% of bilateral aid. Clearly aid is nowhere near mirroring the fact that 70% of the world's poor people are women.

#### 4.4.4 Aid tying reducing value for money – 1.6%

Aid is tied when recipients are obliged to purchase goods or services from the donor country with the aid. The option of local spending allows recipient countries a wider choice, enabling them to support their local or regional economies, usually achieving better value for money. There is some agreement that tied aid is a bad thing. There was a clear commitment by donors in the 2005 Paris Declaration to reduce the amount of untied aid, and in 2001 and again in 2008 the OECD recommended that aid to least developed countries should be untied.

In this report we look at the portion of each donor's aid that is tied, subtracting technical assistance to ensure we avoid double counting. We assume 29% of it is substandard aid, based on the OECD estimate of the costs aid tying adds for recipients.

There has been some progress in reducing tied aid over the last few years – untied aid overall increased from 46% in 2000 to 76% in 2007.<sup>94</sup> The countries with the highest remaining proportions of substandard tied aid in their bilateral ODA are Greece, Portugal and Korea; Italy, the US and Austria do next worst. Meanwhile the UK, Ireland, Norway, Luxembourg and Sweden have no or virtually no tied aid, and serve as models for other donors in this respect.<sup>95</sup>

#### 4.4.5 Donor policies that fail to support country leadership – 13.6%

Aid achieves much better and more sustainable results when development is led by the developing countries themselves. This phenomenon was described in detail in Chapter 3. This has been recognised for at least the last decade, with the Paris aid effectiveness process trying to lead aid in this direction.

It includes targets on many relevant issues in this category. The targets aimed at donors include: increasing the proportion of aid reported to recipient governments so they can take it into account in their budgets; using country financial management and procurement systems; reducing projects implemented separately from, or in parallel with recipient governments; making aid more predictable by disbursing it within the year it was scheduled; increasing use of programme - not project - based approaches; increasing joint donor missions; and using transparent, monitorable, country led performance assessment frameworks.

For the *Real aid* report, we used the recipient country assessments of the quality of donor aid done for Development Finance International, which look at donors' performance on many criteria related to giving space for country leadership. Thirty poor countries have taken part in this assessment and the results are averaged for each donor. Donors who do worse in it have more of their aid counted as substandard aid; donors who do better, less. The proportion counted as substandard varies between 7 and 18 percent.<sup>96</sup> Policies of both bilateral and multilateral donors are assessed and the results combined to give the overall figures. For example, about half of the UK's score in this category comes from the policies of multilateral donors to which it contributes.

Looking at their bilateral aid, the UK, Norway and the Netherlands do best for aid supporting country leadership, and Italy and Portugal worst. Of the large donors, the US and Japan also do relatively badly.

Recent evaluation of the Paris process shows that recipient countries seem to have made more progress on their sides

of the deal than donors; a small amount of progress has been made overall but not enough.

#### 4.4.6 "Aid" spent on refugees and education in donor countries – 4.5%

Under OECD rules donors can count money spent on refugees in their first year of arrival in the donor country as well as the costs spent on educating students from developing countries at institutions within the donor country, as aid. While such expenditures are vital, ActionAid believes they should be counted as part of domestic expenditure rather than ODA, because the expenditure is clearly incurred in the donor country. We counted all the money spent in this way as substandard aid.

Switzerland does worst on refugee costs; next worst are Norway and Sweden. It is hard to say who does best, because Australia, Italy, Japan, Korea and Luxembourg do not include any aid in this category, but this may be due either to political choice or to reporting weakness.<sup>97</sup>

Finland and the UK have also decided to include refugee spending in their ODA since the *Real aid 2* report was written – the UK from 2011.

In terms of spending on their home country education systems, Greece does this the most extensively, followed by Austria, France, Germany and Portugal.

#### 4.4.7 Aid spent on excess administration costs – 0.4%

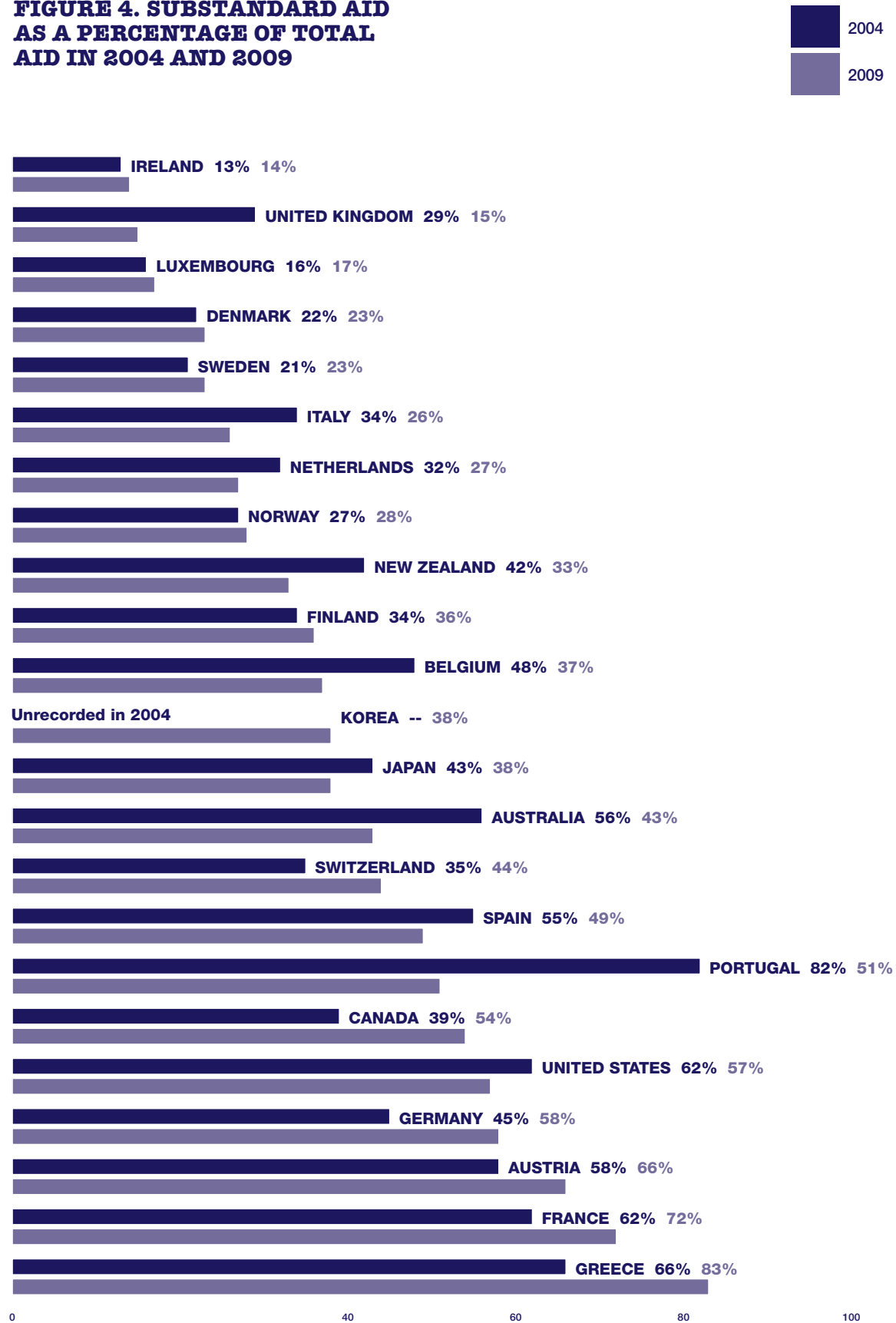
Spending on administrative expenses by donors can also be counted as aid. Some administrative spending is important to ensure effective aid programmes. However, donors such as DFID allow NGOs to spend a maximum of 8% of any project funding on administration, and we therefore allow a similar threshold for official donors, deeming spending above that level substandard.

Excessive administration spending has fallen considerably in the last five years. The donors which still spend most over the threshold are Japan, New Zealand and Finland.

Finally, achievements in real aid may be under threat from several recent and not-so-recent trends which include:

- Increasing numbers of countries are declaring refugee spending as aid.
- All countries double-counting spending in developing countries to combat climate change as aid – and if current pledges are fulfilled, the figures will be substantial.<sup>98</sup> ActionAid opposes this for the same reason as debt relief – that this is not aid but money spent to offset policies of developed countries.
- Aid is increasingly being linked to security spending, spent in countries of key strategic interest to donors, or implemented by security-related organisations – which has been shown in many cases to produce far fewer results<sup>99</sup> – and as a result is NOT being spent in countries which have less strategic interest but just as much need, and where aid could have greater results.
- A new agenda in some quarters is saying that results need to be more micro-managed through parallel procedures and systems, which will undermine country ownership and increase the amounts spent on donor-driven administrators and auditors; or that results which are less easy to count – such as empowerment and gender equality – should be made lower priority.

**FIGURE 4. SUBSTANDARD AID AS A PERCENTAGE OF TOTAL AID IN 2004 AND 2009**



**OTHER AID QUALITY ASSESSMENT SYSTEMS**

Our *Real aid 3* finding that there has been a modest increase in aid quality is in line with findings of other assessment systems.

In recent years, various organisations have developed systems for assessing the quality of donor aid and distinguishing which aid has more development impact.

These include:

The survey of Paris Declaration aid effectiveness indicators, reported in 2006 and 2008, and due to be reported in 2011, which now includes gender equality indicators.

OECD “Country Programmable Aid” (CPA), which excludes aid which is not able to be programmed at country level, such as emergency aid, debt relief, spending on refugees and education in developed countries, and administrative costs.

The HIPC CBP recipient-led system for assessing aid quality and alignment with country leadership.

The AidWatch system for monitoring aid quantity, quality and transparency of EU donors, including a concept of “inflated aid” which is similar to substandard aid.

The Brookings Institution/Center for Global Development Quality of ODA (QuODA) system, which is somewhat more driven by donor concerns such as allocating based on recipient country performance.

These systems, using different criteria and databases, find results similar to “Real Aid”, including:

1. An important share of aid which is not reaching recipient countries, or having a major development impact, with major variation among donors. The OECD CPA finds that the average share of CPA/total aid is 42%, with a minimum of 9% (Austria) and a maximum of 65% (Japan). Aidwatch sets the share of “inflated aid” (debt relief, refugee and student costs) at 10% or 5.2 billion.
2. A gradual but significant increase in “aid effectiveness” or “aid quality”. Both the Paris Declaration survey and the HIPC CBP evaluation, though monitoring different levels of ambition, find only very slow progress by donors towards making aid more effective in producing development results.

The systems also agree broadly on which donors perform best and worst, with more than two thirds of donors having the same ranking in the different scoring systems.

## AID FROM NON-TRADITIONAL DONORS

Since the previous *Real aid* reports, there has been a dramatic diversification in the sources of aid. Aid from non-DAC governments (mainly China, India, Gulf governments and Brazil) has risen from US\$8 billion in 2005 to US\$18 billion in 2008, and aid from CSOs and foundations reached at least US\$24 billion in 2008. How much of this aid is “real”? Data do not exist to allow for precise calculations, but the following overall trends are clear. Information for this box is sourced from work for the UN Development Co-operation Forum.<sup>100</sup>

### AMONG DEVELOPING COUNTRY GOVERNMENTS:

There are many elements of “substandard aid” which they do not count as aid including debt relief, spending on refugees and students, so overall a higher proportion of aid is likely to be “real”.

Some, such as China, India and the Gulf states, provide relatively low proportions of TA, focusing instead on infrastructure projects, whereas others such as Argentina and Malaysia provide almost exclusively TA and South-South experience sharing. Recipients indicate that this TA is likely to be much less overpriced and more oriented to building capacity than much OECD TA, but at the same time is not necessarily any more country-designed or managed.

Almost all aid, with the notable exception of Gulf governments, is tied to exports of their goods and services. Because, their goods and service are cheaper this does not necessarily mean that tying brings overpricing, but it can cause problems for local procurement.

Their performance on policies and procedures varies dramatically across recipient countries and issue areas, very like DAC donors. They are better on funding all sectors of the national development programme, especially infrastructure, and have much less policy and procedural conditionality, but also often insist on using their own financial and procurement procedures.

Virtually nothing is known about their administrative costs.

### AMONG FOUNDATIONS:

- There are many that provide what might be regarded as substandard aid, because it is supporting education for developing country students in developed country institutions, or providing support to religious institutions whose primary goal is not development.
- Administration costs can be high, and in extreme cases can absorb more than half of the funding.
- A large proportion of money is spent on TA via volunteers or paid staff.
- Very little money is given directly to governments and therefore doesn’t directly support the national development strategy of the recipient country. Where the support is intended to play another purpose – for example empowering citizens groups – this is not a problem; the issue comes where nationally-led services are being provided.



**Rebecca Doduo**, lives in Mampehia, Ghana, a village community that ActionAid supports to ensure accountable spending in its primary school. Rebecca has 14 grandchildren and like everyone in the village she helps the school through its teacher parent association (PTA).

PHOTO: NANA KOFI ACQUAH/ACTIONAID

## CHAPTER 5 THE WAY FORWARD: RECOMMENDATIONS FOR BUSAN AND BEYOND

This third Real aid report has shown that real aid gets results, that aid dependency is going down, and that aid that supports country leadership helps to reduce aid dependency. It has shown that there has been progress since 2004 in increasing the share of aid which is real – aid that reaches the countries it is supposed to help, and is delivered in ways which maximise its results.

**Progress is not consistent across all donors. However it shows an increasing will from the international community to ensure that aid maximises its contribution to the Millennium Development Goals, and national and global development.**

Recently real aid has also helped many countries to reduce their aid dependence and its potential negative impact on development. These are strong precedents for recipient countries to lead the aid dialogue through mutual accountability for aid results, be accountable to their own citizens for government spending, and enhance their mobilisation of domestic tax revenue, savings and investment. There are also precedents for donors to support recipient leadership by providing more real aid, being more accountable and transparent, ensuring some aid can be used to generate domestic resources, and focussing on the right types of value for money and results. This can be done by untying aid, reducing conditionality, accelerating delivery, using recipient systems, combating corruption, and providing budget support.

Nevertheless, much more needs to be done. Much more aid must reach developing countries and achieve all it can for their development. Reducing long-term aid dependence also needs to be planned and implemented in every country.

To achieve these goals, ActionAid makes the following recommendations for Busan and beyond:

#### **5.1 Aid donors need to:**

- increase real aid sharply by:
  - i. targeting aid to the people with the most need.
  - ii. ensuring technical assistance is managed and developed by recipients
  - iii. untying all aid, including food aid and technical assistance, and supporting

the spending of more aid locally.

- iv. eliminating policies and procedures which undermine country leadership.
- v. replacing debt relief, refugee and education spending with real aid (whilst maintaining this spending from other budgets).

- Ensure aid benefits women, monitoring progress by improving the OECD marker system and agreeing to compulsory use of it.
- Increase the value for money and results of aid by:
  - i. making aid more predictable, by ending detailed policy conditionality and committing to 5 years of indicative aid forecasts.
  - ii. using recipient systems including for monitoring and evaluation and fighting corruption, by providing budget support to enhance recipient government accountability to citizens.
- Focus on true policy coherence for development or, put simply, fair non-aid policies like trade, tax co-operation, energy and agriculture, that will support the good work that aid can do, rather than undermine it.

#### **5.2 Aid – receiving governments need to:**

- Take clearer leadership on making aid more effective for development results by designing their own aid policies, and eventually aid exit strategies, with locally-driven results targets for themselves, and for each individual donors' aid and non-aid policies to support development, with progress reviewed annually independently.

- Be fully accountable to domestic stakeholders, by involving parliament, local government and civil society including women's organisations fully in national accountability processes on aid and wider government spending and development planning, making data and documents on aid, government spending and plans openly accessible online, and introducing freedom of information legislation.
- Mobilise domestic resources, by improving tax systems and encouraging domestic savings and investment.
- Continue to improve their systems for financial management, procurement, monitoring and evaluation and fighting corruption, to accelerate delivery and enhance results of all spending.
- Incorporate gender responsive budgeting principles into their country processes.
- Base national development plans on existing gender equality and women's empowerment commitments such as the Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW) and the Beijing Platform for Action.

#### **5.3 Donors and recipients jointly need to:**

- Design (recipients) and support (donors) strong national development strategies based on democratic ownership which aid will then finance, including respect for human rights, and measures to maximise results and fight corruption.
- Give preference to local procurement to promote private sector development.
- Accelerate aid delivery to reduce losses through implementation delays.

#### **5.4 Citizens of developing and developed countries need to:**

- Participate fully in national accountability processes on development planning, spending and aid, for parliament, local government and civil society.
- Build their capacity to hold governments and donors accountable, by mobilising far more support and funding via their representative community-level, national and global organisations.
- Demand greater tax justice globally and nationally by ensuring that wealthier citizens and corporations pay their fair share of taxes, especially in poorer countries.

Finally, to implement these commitments, all stakeholders should agree strong mutual accountability frameworks, both globally in Busan, and via national-level targets for each recipient and donor, and dramatically increase aid transparency and support for accountability (in donor and recipient countries). This will help to respond to the principles of the UN and reform the current aid architecture towards a more democratic system.

## ENDNOTES

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90. There has been much recent discussion about whether 75% of the world's poor now live in countries classified by the World Bank as "middle-income". However, most of the countries accounting for most of the world's poor have only recently graduated from low-income status and are still among the world's poorest countries, and are therefore still eligible for funding from the World Bank's cheapest window, IDA. On this basis, and in order to maintain continuity in assessing donor performance, we

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93. DAC donor-by-donor numbers indicate a lower figure than this for TA, but these represent only the standalone TA projects. The figure of one third is reached when TA incorporated in other projects and programmes is included.
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96. We took an average discount of 15% based on previous Real aid reports, and varied it according to Development Finance International's assessment of each donor by recipients. In this category multilateral scores (where available) have been attributed back to the bilateral that fund them. The 30 criteria recipients assess donors on include: budget support rather than projects or TA; aid given via the recipient country budget; aid for national priority sectors; flexibility; predictability; aid virtually without policy conditions; aid without complex bureaucracy; advance disbursement; payment via government accounts; full funding for projects; using countries' own financial management, procurement and monitoring systems. For more information see <http://www.development-finance.org/en/services/guide-to-donors.html>
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