Chapter 2
The IFIs Have Significant Responsibility for the Lack of Change

Introduction

The second chapter of this Report looks at the predominant role of the International Financial Institutions in maintaining aid relationships as relationships of power. It examines the direct and indirect conditionalities that the IFIs still apply to their loans and also looks at the hugely significant gate-keeper role, by which the IFIs exert tremendous influence over recipient countries.

Eurodad

An article from the European Debt and Development Network presents the results of its own research on IFI conditionality. This shows that despite contrary signals from the IFIs conditionalities are still being applied.

The IFIs are able to strongly influence the national Poverty Reduction Strategy Papers (PRSPs) and control the related lending schemes: the WB's Poverty Reduction Support Credit (PRSC) and the IMF's Poverty Reduction Growth Facility (PRGF). This gives them great power over countries' paths to development.

The average number of IMF structural conditions increased from 10 to 11 in the period 2002-2006. Although conditions attached to World Bank policy loans fell from an average of 46 to 37, up to 7% of the conditions where classified as 'bundled-conditions'. Unbundling these increases the total number of conditions by 12%. Research also shows that the number of (binding and non-binding) conditions has risen on average from 48 per loan to 67 per loan between 2002 and 2005.

Furthermore, the significance of the conditions imposed lies in their subject matter. Of all WB conditions for poor countries, 20% are economic policy conditions. Over half of these (11%) impose some sort of privatization and trade liberalization, which end up limiting poor people's access to vital services. Some 43% of all IMF structural conditions focus on economic policy reforms and half of those are privatization-related.

A major problem is that the IFI's advice is usually replicated by donor countries who see them as yardsticks against which to measure developing countries. Accordingly, many donors link their disbursements to the requirement of being 'on-track' with the IMF programme. There have been disastrous results of withholding aid when countries go off-track with the IMF programme, such as when Malawi experienced a severe food crisis.

Indonesia

A second article from the NGO INFID presents how structural adjustment requirements attached to programme aid by IFIs have had huge impacts on the social and economic livelihood of the majority of the poor population of the country. It argues that IMF policies have created a debt trap from which there is little chance of escape.

The article highlights the most controversial loan in the history of Indonesia, which was the specific funds deposited by the IMF in the Indonesian Central Bank to secure its foreign exchange reserve. Not only were these funds of no use to Indonesia, the country also had to repay the funds with interest and observe the long list of conditionalities attached.

The true power of the IMF over Indonesia was revealed by the fact that when Indonesia decided to end the IMF programme in 2003, the donors decided that Indonesia was no longer eligible for debt rescheduling through the Paris Club. Countries such as Indonesia are all but forced to accept the misdiagnoses and failed prescriptions of the IFIs or lose access to other donors. This gatekeeper role of the IFIs is one of the major obstacles to successful aid policies.

Bangladesh

Another article from the Bangladeshi NGO VOICE highlights yet further the significance of the signaling role of IFIs. It argues that the WB and IMF have spread their wings well beyond their original mandate in taking such a central and controlling position within the international aid system.

The sad reality is that governance of the WB and IMF is severely skewed towards rich countries that dominate decision-making in these institutions and thus loans come tied with conditions which do more to serve donor interests than those of a country such as Bangladesh.

The IFIs continue to impose policy conditions, particularly related to the liberalization of markets and the privatization of national companies along neo-liberal economic lines. They also impose rules on macro-economic stability, interfering in monetary policy in a way that does not allow countries to invest in their own development.

The article argues strongly that Bangladesh has suffered through the implementation of IFI conditions. The policies imposed have resulted in job losses, inflation, higher costs of key goods and services and reduced competitiveness on international markets. These have all impacted directly on the lives of everyday people and particularly the poorest. However, the country's room for maneuver is strictly limited because other donors accept the IFI assessments and the criteria for the allocation of aid.

Furthermore, even where things clearly go wrong, such as in the presented example of the Khulna-Jessore Rehabilitation Project (KJDRP) there is no accountability of donors for the cause of people's suffering.

Pakistan

An article from the Pakistani NGO PILER looks at the negative effects of IFI-funded projects in its country. Flawed projects emerge from the faulty development paradigm put forward by the IFIs which believes that investment in major infrastructure projects will generate economic growth that will then seep into local communities and reduce poverty. The question of accountability at local level is omitted at very outset, because the gains are measured at the macro-economic level

The article argues that mega-infrastructure projects have served to detach people from their historical entitlements to natural resources. The social disruption, loss of livelihood and environmental degradation associated with these projects push local communities into poverty and deprivation.

Furthermore, the IFIs seem to be unconcerned by the concomitant violation of rights such as to food, development and shelter, considering them to be merely 'transitory costs'.

This paper looks deeply into the case of a World-Bank-financed project - the Left Bank Outfall Drain (LBOD) in the Sindh province of Pakistan. This demonstrates how the World Bank failed to take into account the needs of local communities and ended up uprooting them from their means of survival, violating their fundamental rights. It also shows how the WB failed to take responsibility for its actions.

Nepal

This paper from the Nepal Policy Institute argues that whilst the rhetoric around aid policies is strong on ethical symbolism, the reality is dictated by the interests and calculations of global financial capital, represented by the IFIs and private global corporations.

The problem for poor countries like Nepal is that they will be punished heavily both economically and politically if they fail to comply with the global corporate agenda of development. But no punishment or enforcement measures are allowed in the event of violations of UN human rights and environmental treaty obligations in the pursuit of such corporate-led development.

By controlling the purse strings of international aid, the IFIs were able to have such control over politics in Nepal that not even strongly left-wing elected parties could stand up and implement the policies they wanted. This reality not only hindered development, but also encouraged political insurgency.

There are major problems with the IFI-supported contract frameworks including FIDIC (Federation Internationale des Industries et Consultants) and BOOT (Build, Operate, Own and Transfer). Whilst the former almost always leaves recipients liable for unexpected overspends, the latter often takes away communities' sovereign rights to their own natural resources for the duration of the contract, receiving an out-of-date and expensive to run system at the end.

Recent elections in Nepal have re-elected a left-wing government. The paper wonders whether this time the IFIs will allow the country's own political choices to determine its development agenda, taking a human-rights based approach.

The Netherlands

Finally the Netherlands considers to what extent the EU represents a better model of multilateral aid for the future. It argues that, whilst still being far from perfect, it goes some way to providing the kind of aid that is needed, particularly through the use of budget support.

The Commission provides the main share of its budget support on the condition that a country meets three general eligibility criteria: it should have a poverty reduction plan; it should work towards improving public finance management (PFM); and it should aim for macro-economic stability. The remainder of the funds are disbursed according to the country's performance against specific indictors on health care, education, and PFM.

In a study of the EC's general budget support agreements with 11 different African countries, over half of the performance indicators call for direct improvements in poor people's health and education, in particular for girls and women. By moving away from specific economic policy conditions, and instead often focusing on gender-specific outcomes in health care and education, the Commission sets a positive example to other providers of budget support.

Evidence suggests that the EC's budget support does change poor people's lives. Government spending on education has increased by nearly a third (31 per cent) in eight of the African countries that receive some of the largest amounts of the Commission's general budget support. In all but one country, this has resulted in an increase in the number of children enrolled in primary school.

The paper recognises that the Commission is not exclusively responsible for the positive results, but the evidence does show that where it provides large amounts of budget support, headway is being made in reducing poverty. Furthermore, the EC's conditions can sometimes be deemed somewhat intrusive. In Ethiopia, for instance, the EC required the introduction of a competition law, application for accession to the World Trade Organisation, and revision of urban land lease laws.

Conclusions

Whilst the previous chapter looked at how power relations still dominate the delivery of aid, this chapter argues that the IFIs are the worst offenders. They give loans without adequately considering or consulting the local communities most directly affected. They also continue to apply serious economic policy conditionalities to aid. Both of these factors often have devastating consequences on the livelihoods of the poorest people.

Furthermore, through their gate-keeper role, the IFIs often prevent recipient governments from accessing funds from alternative sources as many donor countries accept the IFIs' assessments and criteria. In the context of current aid practices, harmonization of donors is only serving to strengthen this influence. Poor countries often find themselves with little choice but to follow the conditions applied.

Of all the multilateral donors, the European Commission shows the most promise as being ready to apply good principles in allowing recipient countries to plan their own development strategies through the use of budget support. Even here, however, much progres is still needed towards optimizing the benefits of aid for developing countries.

The Impact of IFI Conditionality on the Development Aid System

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Introduction

Among the International Financial Institutions (IFIs), the International Monetary Fund (IMF) and the World Bank (WB) are the most well known. Their history can be traced back to the Bretton Woods agreement and, through the years, they have attained and maintained a leading role in the global economy. This status as keepers and champions of the global economic order has, by extension, made them two of the most influential players in the field of development and they rule over aid flows with the golden sceptre of conditionality.

Despite both internal (Guidelines on Conditionality and General Good Practice Principles) and external (The Paris Declaration) initiatives, they are failing to hand over their power. Perversely, as more and more countries increase their budget support to developing countries, they reinforce the WB and the IMF's stronghold by buying-in to their conditionalities.

The main instrument through which both the IFIs influence development is the Poverty Reduction Strategy Paper (PRSP) and related lending schemes. This initiative, endorsed by the Executive Boards of the World Bank and IMF in September 1999, articulates the High Indebted Poor Countries (HIPC) debt relief initiative and laid the foundation for two lending schemes: the WB's Poverty Reduction Support Credit (PRSC) and the IMF's Poverty Reduction Growth Facility (PRGF). The IMF and the WB thus play a double role as donors and advocates of development policies.

In 2005, both the WB and the IMF signed the Paris Declaration on Aid Effectiveness, committing as donors to increasing recipient countries' ownership of development aid and aligning and harmonizing aid flows under recipient countries' leadership. Furthermore, the PRSP was intended to address the criticisms aimed at the WB's Structural Adjustment Programs of the 1990s. By definition, a PRSP should be "country-driven, comprehensive in scope, partnership-oriented, and participatory",[1]

However, criticism remains high and doubts persist about the real extent of PRSP ownership and participation by recipient countries. If IFI conditions are supposed to be aligned to national PRSPs, loans have been usually granted under stringent conditionality, pursuing objectives not always shared by recipient countries' governments. Ghana's last PRSC, signed in 2005, contained the striking number of 197 conditions.[2]

The following sections analyse why conditionality plays such a central role in the WB and IMF's development aid. They also discuss whether the Paris Declaration has had any impact on the practices of these two IFIs from the perspective of recipient countries and in light of their experiences.

IMF Conditionality

Following the introduction of the PRSP scheme, both the IMF and WB have been the target of severe criticism as a consequence of conditionality practices. The IMF was the first organization to react to criticisms about conditionality and in September 2002, it published its Guidelines on Conditionality.[3] The WB took a little longer to react, publishing its Review of World Bank Conditionality,[4] conducted between November 2004 and July 2005 and containing the Good Practice Principles on Conditionality (GPPs) in September 2005.

Both these internal initiatives are in line with the commitments made in the Paris Declaration and any outcomes of these 'new approaches' should have been reinforced by the international agreement. Enough time has elapsed to allow for results to be observed. Unfortunately, however, NGO research reveals that even the most positive appraisal can only claim piecemeal progress.

Six years after the Guidelines on Conditionality and three after the Paris Declaration, the IMF shows a not altogether surprising lack of results. Research carried out by Eurodad on 20 developing countries shows that the average number of IMF structural conditions increased from 10 to 11 between 2002 - when the IMF issued its new staff guidelines to reduce the number of conditions it imposes - and 2006.[5]

Moreover, the evaluation of the IMF conditionality carried out in 2007 by the Independent Evaluation Office (IEO) of the IMF concluded that "the streamlining initiative did not reduce the volume of conditionality".[6] The latest data made available to Eurodad by the IMF, covering the first half of 2007, shows that this trend has not changed.

On average, half of all IMF structural conditions imposed on poor countries via the PRGF are binding conditions. The IMF imposes policy reforms that have to be acted upon prior to receiving funds and others that must be enacted within one year of receiving the funds. The proportion of binding conditions has stayed relatively steady over time.

Furthermore, the PRGF agreements signed in 2007 still meddle with extremely sensitive issues, most of them far from the IMF's field of expertise. Some 43% of all IMF structural conditions focus on economic policy reforms and half of those are privatization-related. The large majority of privatization conditions are focused around banking. Nine out of the 11 poor countries (including Bangladesh, Benin, Ethiopia, Mozambique and Tanzania), facing privatization-related conditions from the IMF had some form of banking privatisation imposed upon them, whilst the energy sector was the second most common target.

In Nicaragua, conditions still push for the reform of the country's pension fund system. This system is still in tatters after the attempted privatization heralded by the WB and the Inter-American Development Bank, which was halted because the government could not cover the expenses and guarantee the pension to its citizens at the same time.[7] The IMF also continues to push for the reform of the cotton sector in Burkina Faso with the privatisation of the public company SOFITEX (Société de Fibres Textiles).

WB Conditionality

Current Eurodad research appears to show a slightly better picture of WB conditionality.[8] Comparisons between the number of conditions before and after the GPPs – the research compares the number of conditions attached to the PRSCs before 2005 and those in the period 2005-2007 - confirm that the average number of conditions attached to World Bank policy loans has been reduced from 46 to 37.

However, up to 7% of the conditions where classified as 'bundled-conditions' – general conditions whose fulfilment requires a number of reforms and policy actions; unbundling these increases the total number of conditions by 12%. More than fifty conditions were attached to each of the current World Bank grants for 14 out of the 20 low-income countries studied and three had more than 100 conditions. The research shows that the number of (binding and non-binding) conditions has risen on average from 48 per loan to 67 per loan between 2002 and 2005.

In addition, the World Bank is continuing to impose a significant number of controversial economic policy conditions on low income countries through its development lending. Eurodad assessed that 15 out of the 20 poor countries have privatization-related conditions as part of their World Bank lending. These cover sectors of the economy such as agriculture, banking, and water. Of all WB conditions for poor countries, 20% are economic policy conditions. Over half of these (11%) impose some sort of privatization and trade liberalization, which end up limiting poor people's access to vital services.

The number of conditions varies wildly from one country to another. Rwanda, for instance, faced 144 conditions in the PRSC approved in 2006, including the privatization of Rwandatel, Rwandex, the Nshili-Kivu tea plantation and the rice factories of Rwamagana, Gikonko and Bugurama. Similar stringent conditions have been applied to Afghanistan, a post-conflict 'fragile state' with less than 10% of workers in the formal economy, where more than 50 state-owned enterprises will be privatised and, according to government estimates, 14,500 jobs lost.

The research reveals that although the number of conditions which call for direct privatisation has marginally declined, there has been a massive increase in the number of conditions that push for reforms associated with facilitating privatisation, such as regulatory reforms, restructuring of certain sectors and corporate reform. The number of 'privatisation-associated reforms' have almost doubled between previous and current loans across the 20 countries assessed.

The Bank's new guidelines for development policy lending employ the concept of 'criticality'. This is meant to confine the Bank to setting conditions that are deemed critical for the implementation and expected results of a country program. However, there is a high prevalence of micro-management conditions in World Bank lending, and an inability by WB staff to make rational judgments as to what should or should not constitute a condition in development finance.

The Paris Declaration and Current Conditionality Practices

Since the introduction of the PRSP, 58 countries have approved this instrument. However, although an evaluation carried out by the World Bank[9] shows that it is starting to introduce more conditions drawn from the PRSP, this section explains that PRSPs have not been able to introduce real changes.

In the Paris Declaration, donors committed to "draw conditions, whenever it is possible, from a partner's national development strategy…"[10] In practice, what is happening all too often is that a PRSP and a national development strategy (NDS) are becoming one and the same.[11] In Afghanistan, for instance: "The Interim NDS will be submitted to the Boards of the World Bank and the IMF in the expectation that it will also meet the benchmarks of an Interim Poverty Reduction Strategy process, developed by the World Bank and IMF in 1999."[12]

Rather than independently designed national development strategies informing the PRSPs, it is obvious that the IMF and the WB have a strong say on the NDSs. The WB and IMF claim that the PRSPs are owned by recipient country governments, but the actions of these two behemoths contradict, once more, their statements of good will. During the drafting of the second PRSP for Niger, fifteen Nigerien representatives were flown to Washington DC where they met World Bank, UNDP, EC, Belgian and IMF officials. After this meeting a Senegalese consultant was hired and sent to Niger where he finished drafting the PRSP. [13] This example gives an idea of the real manoeuvre-space recipient governments have when designing these strategies.

Furthermore, researchers suggest that allies closer to the US receive fewer conditions in their IMF loans.[14] This indicates that conditionality is too often used as a political tool rather than an instrument to furthering reforms which are deemed necessary to ensure poverty reduction.

It is obvious that recipient country governments barely own their development aid strategies. The mechanism that allows for the IMF and the WB to dominate development aid processes is sadly summarised by the Head of the National Treasury Research Service of Niger: "we need the money; therefore we accept performance indicators even if we don't think we will be able to meet them. These negotiations are by their nature unequal as we need the money."[15] The IFI's hegemony will not be broken until the role of both institutions as an international reference is challenged and a more coherent and pro-poor system introduced.

Furthermore, beyond the waning role of recipient countries' governments with respect to the IFIs, the lack of democratic ownership outside of government is a key issue in developing countries. In Mozambique, neither PARPA I nor PARPA II – the local name for Mozambique's PRSPs - were subject to approval by Parliament.[16] Similarly, the Honduran parliament has also been bypassed with regards to development strategies.[17]

Additionally, the resulting PRSPs usually have vaguely-defined objectives and are inadequate for donors to monitor budget support. Accordingly, when donors want to provide budget support they form, together with the national government, a 'Budget Support Group'. This group drafts a Performance Assessment Framework (PAF), which sets out a number of benchmarks theoretically to oversee budget support flows in line with the objectives of the PRSP. Unfortunately, however, the PAF is not the result of a dialogue with the recipient country's government, but of a unilateral process led by donors. As the UK Department for International Development's Head of Operations in Sierra Leona points out: "initially the donors do a draft to agree on the conditions, and then these are taken to the government and discussed".[18]

If democratically-elected parliaments play such a feeble role, the power granted to civil society organisations in this process is even less. The problem is such that even the OECD has to remind donors that: "Parliaments, civil society organisations and the wider public, as well as political institutions at the sub-national level, are important 'owners' of development strategies and policies, and drivers of change. Genuine ownership requires political leverage and space as well as a legal-institutional framework that ensures that citizens – including the poor and the most marginalised women and men – are able to engage in decision-making processes and hold their governments accountable."[19]

The Real Weight of Conditionality

Conditionality is the most important tool the WB and IMF have to push reform. Furthermore, the IMF remains extremely influential despite being a minor donor – several of the IMF's three-year PRGFs signed in 2005 and 2006 provide a relatively small amount of funding: US$ 10m in Niger; US$ 38.2m in Ghana; US$ 9.2m in Burkina Faso; and US$ 9.1m in Benin.[20] There are several factors which explain the weight of WB and IMF's conditions in development aid.

Firstly, the WB and the IMF play a central role in the global and economic systems and their advice is usually replicated by donor countries who see them as yardsticks against which to measure developing countries. Accordingly, many donors link their disbursements to the requirement of being 'on-track' with the IMF programme. Recent Eurodad research confirms that this is the case, for example, in Nicaragua[21] and Sierra Leone[22], where this requirement has caused severe problems as a result of donors freezing predicted disbursements. WB and IMF conditionality allows for the existence of a self-perpetuating vicious circle. The real significance of conditionality rests in the power of cutting not only money flows directly from these two institutions, but also from other donors.

Another issue which helps to strengthen the grip of the WB and IMF on development aid is cross-conditionality. This word describes the phenomenon of finding one condition duplicated in both the WB's PRSC and the IMF's PRGF. The practice of cross-conditionality increases the pressure exerted by conditionality and is, furthermore, usually applied to push through the most sensitive reforms, such as the privatisation of public companies. This is the case, for instance, of IFI conditions requiring the privatization of the Rupali Bank in Bangladesh, the Bank of Ethiopia, the Inter-Bank of Mali and Nicaragua's telecommunication company Enitel.[23]

The Paris Declaration was intended to address these problems and to cede to recipient countries the driver's seat of development aid by promoting the principles of ownership; alignment; harmonisation; mutual accountability; and managing for results. Nonetheless, the unfortunate truth is that, by backing budget support, the Paris Declaration helps to close the circle in the sense that more and more donors will buy-in to this aid modality. This strengthens the link to conditions agreed in processes, such as the PAF, where recipient governments have very little say.

In 2002, Malawi endured a severe food crisis, during which it went off-track with the IMF programme. Subsequently, all budget support to Malawi was suspended, aggravating the humanitarian and economic crisis, creating a sort of catch-22 situation.[24] The power of the WB and the IMF to impose conditions and promote changes is founded on the possibility of this type of crisis. To solve this problem it is not only necessary to increase recipient countries' real ownership, but also to provide funds through longer term agreements which cannot be immediately broken when the conditions imposed by the WB and the IMF are not met.

One of the most remarkable failures of IMF and WB policies has been water privatisation in developing countries. In Bolivia, the privatization of the company Aguas del Tunari ended with the famous 'War of Water' after the prices rocketed and service standards dropped.[25] Following a similar case in Tanzania, last January the British company Biwater was ordered by a London tribunal, acting in accordance with international law, to pay £3m to DAWASA, a Tanzanian water utility, after it was found that the service had deteriorated under its management.[26] The privatisation of water utilities as demanded by the IFIs has experienced similar problems in other countries such as Puerto Rico and the Philippines, proving this problem to be widespread.

On the positive side, the Biwater case represents a breakthrough as it has opened the way to hold companies accountable for their wrongdoings in developing countries. Unfortunately, the chain of responsibility does not reach the upper links, and the ultimate perpetrators do not bear any burden other than their own conscience. When one tries to carry out research on the IFIs positions on these issues, the silence is shocking.

Conclusions

There is no doubt that policy conditionality affects recipient countries' policies far beyond simply ensuring fiduciary accountability and that neither the WB nor the IMF are undertaking reforms at the pace that is needed. Up to now, they have failed to fulfil the commitments made in the Paris Declaration and their own conditionality guidelines, impacting negatively on development and the lives of people.

A key issue in tackling conditionality is that it still seems reasonable to expect that there should be mechanisms in place to monitor how aid flows are being used and to stop aid being delivered incorrectly. The problem with the WB and the IMF's conditionality is that it is used as a tool to force changes, which are frequently highly sensitive, in recipient countries, sometimes pursuing developed countries' interests.

A possible solution would be to look again at the real meaning of the word 'monitor' and focus conditions on the output side of development policies, instead of on the input side. The European Commission has recently started to use an approach based on this principle. Outcome-based conditionality, as it is called, links aid to development results or outcomes and leaves recipient governments free to decide the way to achieve them. This is a much more desirable option to policy conditionality,[27] even though it is not free from problems; indicators are difficult to design and adjust and predictability problems still persist if long-term commitments are not applied.

Now is the right moment for change; this year the WB and the IMF will be closely scrutinized in Accra and both need to speed up reform to live up to the Paris commitments. Renovation is not always easy, but the reforms needed do not call for a revolution, just political will. Unfortunately, the WB and the IMF have shown very little willingness in the recent past to transform their current approaches to conditionality For the time being, the power remains in their hands.

Notes

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Multilateral Aid and Conditionalities:[1] The Case of Indonesia

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Despite amounting to a relatively small amount of Indonesia's overall economy, foreign aid has had a significant impact on the country's domestic economic and political situation. This has happened through the conditionality imposed on loans by the IMF and which has been reinforced by the wider donor community under the leadership of the World Bank.

Since 1966/7 Indonesia has received foreign aid (loans and grants) from twenty countries and thirteen multilateral agencies. Nevertheless, most of the donor countries and multilateral agencies to Indonesia have been organised in one "consortium". From 1967 to 1991 this consortium was the Inter-Governmental Group on Indonesia (IGGI), chaired by the Netherlands. This was replaced by the Consultative Group on Indonesia (CGI) from 1992 to 2007, chaired by the World Bank. From 2005, CGI was officially chaired by Indonesia but in practice was chaired and directed by the World Bank.[2]

The IMF was not a member of IGGI or CGI, but it was always represented in the meetings and its presence in Indonesia has had strong implications for the country and the donor community. Not only has the IMF imposed policy conditions on the funds provided, but bilateral and multilateral donors have referred to the IMF before making loan agreements with Indonesia.[3]

Structural adjustment requirements attached to programme aid by IFIs have had huge impacts on the social and economic livelihood of the majority of the poor population of Indonesia. The liberalisation and privatisation of state-owned companies and public services have influenced both state revenues and the costs paid by the poor for services.

Composition of Foreign Aid to Indonesia

The majority of Indonesia's foreign debts are bilateral with official development assistance making up the largest portion, via both concessional and commercial loans. Japan is the biggest bilateral donor, accounting for about 70% of the total bilateral aid to Indonesia. Bilateral aid mainly funds projects which are predominantly used to support physical and institutional infrastructure.

Multilateral aid is more heavily focused on programmes aimed at supporting crises in the balance of payments or state budget. In line with the policies of the IFIs, policy conditionalities are attached to this aid.

As the Table 1 shows, the Asian Development Bank (ADB) and the World Bank (through the IBRD) are the two major multilateral donors to Indonesia. The loans from the ADB have increased steadily and, in 2006, it became the biggest multilateral donor. IDA constitutes a relatively small portion of overall multilateral aid as does funds from the IDB (Islamic Development

Figure 1. Multilateral Loans (%)

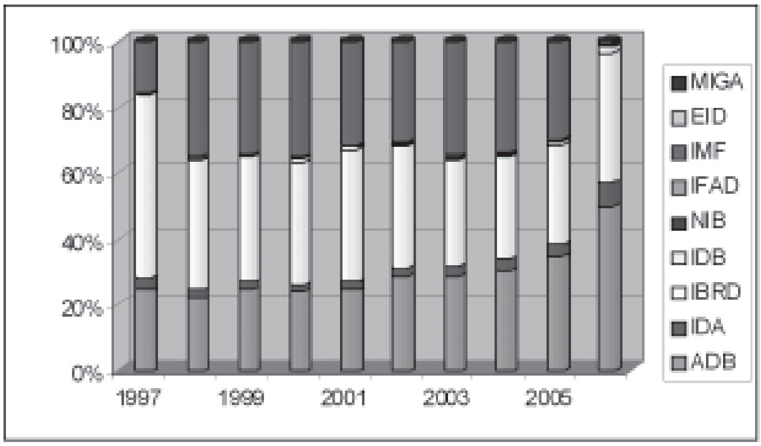

Table 1. Multilateral Sources of Loans (Million US$)

Donor	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
ADB	4,557.00	5,694.00	7,517.00	7,544.00	7,179.00	8,310.00	8,582.15	8,869.14	9,140.13	9,409.21
IDA	720.00	702.00	682.00	719.00	726.00	788.00	884.39	949.06	1,002.59	1,321.75
IBRD	10,307.00	10,229.00	11,494.00	11,774.00	11,577.00	10,802.00	9,776.10	8,942.99	8,106.53	7,420.81
IDB	27.00	32.00	51.00	215.00	184.00	138.00	151.47	162.58	202.85	396.70
NIB	-	217.00	214.00	200.00	186.00	170.00	155.00	139.16	120.91	105.46
IFAD	57.00	84.00	72.00	65.00	57.00	65.00	78.71	78.98	71.06	73.72
IMF	2,973.00	9,082.00	10,255.00	10,983.00	9,105.00	8,829.00	10,238.61	9,653.89	7,806.03	-
EID	4.00	8.00	8.00	8.00	7.00	7.00	110.77	109.12	116.14	109.09
MIGA	-	-	-	-	8.00	3.00	-	-	-	-
TOTAL	18,645.00	26,048.00	30,293.00	31,508.00	29,029.00	29,112.00	29,977.20	28,904.92	26,566.24	18,836.74

Bank), although both have become more important in providing loans to Indonesia.

In 1971, programme aid was 2.5% of GDP compared to only 0.5% of GDP allocated for project aid. The oil boom in 1974 that contributed to increasing state revenues, and stabilising the Indonesian economy reduced the percentage of programme aid. At this time, the World Bank started to engage more in supporting physical projects and the technical assistance group working in the National Planning Board and the Ministry of Finance.

For more than ten years (1974-1985) programme aid to Indonesia was not significant. However, the sharp decline in the world oil price in 1982 that caused a crisis in the balance of payment attracted programme aid to Indonesia once again through IMF/World Bank structural adjustment loans. In 1983, the IMF approved SDR260 million under Compensatory

Table 2: The World Bank Adjustment Loans to Indonesia

Type	Date of Approval	Amount Approved
Trade Policy Adjustment	1987	US$ 300 million
Policy Reform Support	1999	US$ 1.5 billion
Social Safety Net Adjustment	1999	US$ 600 million
Water Resources Sector Adjustment	1999	US$ 300 million

Source: BAPPENAS, 2001

Financing Facility (CFF). Indonesia received SDR463 million from IMF in 1987 under the CFF to compensate for the decline in exports. In the same year, Indonesia obtained $300 million from the World Bank under the Trade Adjustment Programme Loan.[4]

Impact of World Bank Loans

Though programme aid is less than project aid and not very visible, its influence on the Indonesian economic and political systems has been significant. Programme loans were meant to rescue the country from crisis, particularly related to balance of payments and the state budget. However, through programme aid, World Bank staff have worked as if they are part of the Indonesian bureaucracy, freely influencing the policies of the national government. The Indonesian bureaucracy has become so open to the World Bank that none of its policies are immune to influence.[5]

Aid from the World Bank group started in 1968, through IDA soft loans. The first IBRD loan to Indonesia was made in 1974 when the country had started to catch up with development momentum. The World Bank provided Trade Adjustment Loans in 1987. When Indonesia was hit by the 1998 economic crisis, the World Bank provided USD 26.5m of International Development Association (IDA) aid and tied it to the privatisation and liberalisation of public services, including the cut of subsidies in social sectors.

It is interesting to observe that whilst the IFC (a family member of the World Bank) has been making a fortune purchasing the cheap shares of the public services and privatised companies, poor Indonesians have paid a high price for the soft IDA loans.

After increasing critiques of the relevance of the World Bank in Indonesia, the Bank is now enthusiastically promoting its new *Community Driven Development* project. This consists of two project components: *Kecamatan Development Project* (KDP) for rural areas and *Urban Empowerment Project* for urban areas and is seen, by World Bank staff, as a bait for new loans for Indonesia to meet the main mission of alleviating poverty.

Scott Guggenheim's paper on KDP has been treated by World Bank staff in Indonesia as the main reference on the success of the project[6]. In fact, the project has made poor people responsible for poverty alleviation in terms that mean the poor themselves will repay the debts in the future.

A 2004 BAPPENAS study[7] raises the question of whether the loans being attracted are really for the benefit of the recipient country. The suggestion is made that, since more loans mean more overhead costs and project work for the donor agencies, the staff of these agencies are keen to encourage more loans to increase their job security rather than in the interests of the recipient country.

Impact of IMF Loans

The most controversial loan in the history of Indonesia, however, was the specific funds deposited by the IMF in the Indonesian Central Bank to secure its foreign exchange reserve. These funds were of no use to Indonesia, since they were deposited when the Central Bank had enough reserves already. Nevertheless, the country not only had to repay the funds with interest, but also had to observe the long list of conditions stipulated in the signed Letter of Intent and Memoranda of Economic Policy Monitoring. In this sense, the IMF deposits can be seen as a 'Trojan horse' used by the IMF to control the policies of Indonesia along the neo-liberal lines preferred by the developed countries and multinational corporations whose interests are represented in the IMF.

Rizal Ramli, the Coordinating Minister of Economic Affairs in 1997, warned that "involving the IMF in Indonesia's recovery programme would inevitably plunge the country into a deeper economic crisis"[8]. Nevertheless, from 1997 to 2005, the IMF and Indonesia signed 20 Letters of Intent (LoI) and Memoranda of Economic and Financial Policies (MEFP) on policy measures and other conditionalities to be implemented by Indonesia. While the People's Assembly Council (*Majelis Permusyawaratan Rakyat* – MPR)[9] decided the general guidelines to solve the crisis without dependence on foreign creditors, the government was not able to resist the pressures from the IMF and the donors' community.

On 5 November 1997, Indonesia and the IMF signed a three-year stand-by arrangement (SBA) aimed at restoring market confidence. However, the fiscal austerity, tight monetary policy, floating exchange rate regime and bank closures prescribed by the IMF brought a banking crisis, which caused social unrest and uncertainty in the whole economy, deepening the crisis.

Following the Stand-by Arrangement (SBA), the inter-bank interest rate sky-rocketed from 20 to 300 percent, causing a banking crisis. The closure of 16 banks, as recommended by the IMF in November 1997, caused capital outflow of USD 5 billion. This put further pressure on the Indonesian Rupiah provoking corporate bankruptcy and the loss of thousands of jobs.

To solve these problems, the IMF and Indonesian authorities signed the first Extended Fund Facility (EFF) of SDR 5.3 billion, imposing stricter structural measures on fiscal and monetary policies as well as banking and corporate restructuring. In

Table 3. The IMF Stabilisation Loans to Indonesia

Programme Type	Date of Approval	Expiry	Amount Approved	Amount Drawn (Disbursement ratio - %)
Stand-by	March 1972	1973	US$ 14 million	
CFF	August 1983		SDR 360 million	
CFF	May 7, 1987		SDR 463 million	
Stand-by	November 5, 1997	August 25, 1998	SDR 34 billion	SDR 3.67 billion (44.0%)
EFF	August 25, 1998	February 4, 2000	SDR 5.38 billion	SDR 3.79 billion (70.6%)
EFF	February 4, 2000	December 31, 2003	SDR 3.64 billion	SDR 1.99 billion (54.6%)

Source: IMF website (www.imf.org).

February 2000, when the first EFF expired, the government signed the second EFF involving a commitment of SDR 3.6 billion from IMF. The second EFF was accompanied by a long list of conditionalities, including stricter measures on privatisation and legal reforms.

The IMF recommended the conversion of private debts into public debts. The government's domestic debts increased by up to US$ 65 billion. At the same time Indonesia's public foreign debts increased from US$ 54 billion to US$ 74 billion, and the international private debts decreased from US$ 82 billion to US$ 67 billion, some of which had been converted into foreign public debts. As a consequence of the financial crisis and IMF policies, Indonesia's debt doubled over a period of just four years.

Each semester IMF staff monitored the implementation of the structural reforms required by the conditions of the LoI and the MEFP. The surprising thing is that reports from the IMF did not influence the market at all; rather the reaction went contrary to the reports. When the IMF reported that the Indonesian macroeconomy was becoming more stable, the exchange rate of the Rupiah weakened; and when the IMF reported that there should be stricter measures for reform, the capital inflow from foreign investors tended to increase.

What is more, the IMF funds that provoked these conditions were not even used. The net foreign reserves of Indonesia, which were about US$ 24 billion at the time when IMF and Indonesia signed the first EFF, were at a very healthy level, and there was no need for additional reserves to secure the balance of payments. Since Indonesia took the floating exchange rate regime, the Central Bank did not need to intervene in the exchange market on regular basis and therefore additional reserves were not necessary.[10]

Whilst Indonesia did not need to use the IMF money, it still ended up bearing the interest costs. In 2002 Indonesia paid US$ 2.3 billion to the IMF, consisting of US$ 1.8 billion in principal and US$ 500 million in interest payment[11]. On average the cost of this *idle* fund (fees and interest) was about 3.5 percent. IMF policies put unsustainable pressure on the government budget. For the 2002 fiscal year, debt servicing was estimated to total USD13 billion (IDR 130 trillion) including domestic and international payments. These payments amount to more than three times the total public sector wage bill including the military, and eight times the education budget.

Table 4: Disbursement and Repayment of IMF Loans (SDR)

Year	Disbursements	Repayments	Interests
2002	825,720,000	1,375,920,000	153,322,440
2001	309,650,000	1,375,920,000	369,498,855
2000	851,150,000	0	398,846,600
1999	1,011,000,000	0	267,539,445
1998	4,254,348,000	0	133,963,634
1997	2,201,472,000	0	0

Impact of IFIs on Other Donors

The programme loans during the crisis period - including the conditionalities detailed in the Letters of Intent - were used as references by both the multilateral donors and the bilateral donors.[12] Donors united in putting pressure on Indonesia to implement IMF's policy prescriptions and conditions by making the disbursement of both programme and project loans dependent on whether the government of Indonesia had implemented the conditions. The unity of the donors was made possible because of the presence of regular meetings of the CGI, where the government of Indonesia had to provide reports to the donors, in addition to the regular monitoring from the IMF.

Programme aid reached its peak during the crisis period, when the multilateral donors came with a rescue package. The commitments of this "bail out" package from IMF were matched by commitments from the World Bank and the ADB and the Government of Indonesia itself. This first line totalled USD 23 billion. It was followed by a second line totalling USD 20 billion from bilateral donors (see table below).

The main reason for involving other donors in the rescue package was to maintain and prop up market confidence by showing that the donors collectively were ready to help Indonesia financially with a large amount of money (US$ 43 billion). The second line was only to be issued after the first line was fully exhausted. In reality, the second line was never utilised.[13] The rescue package itself did not rescue the economy of Indonesia, but it was used as an instrument to impose the policy prescriptions of the "Washington Consensus" on Indonesia.

Loans from the World Bank, Asian Development Bank and other donors do not need to be tied to IMF conditionality. Nevertheless, when Indonesia decided to end the IMF programme in 2003, the donors decided that Indonesia was no longer eligible for debt rescheduling through the Paris Club.[14] So IMF's programme package was needed and used by the foreign creditors, such as the World Bank, to profit from the crisis.

Table 5: International Financial Rescue Package for Indonesia

Contributors	Amount (US$ Billions)
First Line	23.0
IMF	10.0
World Bank	4.5
Asian Development Bank	3.5
Government of Indonesia	5.0
Second Line	20.0
Singapore	5.0
United States of America	3.0
Japan	5.0
Australia	2.0
China	3.0
Malaysia	1.0
Hong Kong	1.0

Conclusions

The data and facts of multilateral aid show that most of them have been wasteful, with no clear advantage for Indonesia. Furthermore, they have been used by creditors and donors to dictate policies that should be left to the national government. Programme loans from multilateral agencies were used to justify the presence of the agencies and their staff in Indonesia rather than for promoting capacities of the government staff. The good governance that is promoted now in Indonesia is a result of the democratisation processes rather than the results of the works of the consultants paid by the programme loans.

Foreign debt amounts to less than 3% of the annual state budget, meaning its overall contribution to Indonesian economic development is limited. The major determinant is, in fact, domestic financial capacity. Nevertheless, the foreign debt becomes problematic and burdensome when the maturity of the debts is accumulated, putting pressure on the state budget in later years.

Most importantly, however, the relatively small amount of foreign aid caused heavy foreign intervention in Indonesia's economic and political system. The coordinated pressures from the donors/ creditors through IGGI/CGI tied Indonesia to conditions imposed by the IMF and made it difficult for Indonesia to get rid of the debt trap. Furthermore, the fact that the staff members of the donor agencies are driven by self-seeking behaviour, while they are working together with Indonesian officials in the offices of the Central Government of Indonesia, explains why the policy measures from Indonesian government are not more pro-poor, pro-job and pro welfare of Indonesians.

The programme loan from the IMF was the most striking example of wasteful and harmful loans in Indonesian history, and can become a case study of how an International Organisation undermined state sovereignty and ignored democratic processes in a country. The IMF policies created a debt trap from which there was little chance of escape. The IMF forced Indonesia to accept its misdiagnosis and failed prescriptions, including the conversion of private debt to public debts, or the transfer of the debts of the private corporations to the debts of the poor Indonesians.[15]

The World Bank has been rather successful at maintaining its image as a donor institution in Indonesia. When the country was burdened with structural adjustment programmes in the 1980s and the implementation of the policy conditionalities (privatisation and liberalisation) after the 1997/98 crisis, the World Bank could deny responsibility for the failure of policy reforms. However, whilst the IMF was the only institution to be publicly blamed, it was the World Bank that orchestrated the implementation of the IMF policy conditionalities through its leadership of the CGI.

Notes

1 Paper for the North-South CSOs consultation on aid effectiveness. (2007, November 15-18). Nairobi, Kenya.

2 Kwik Kian Gie was the Coordinating Minister of Economic Affairs (2000 – 2003) and Minister of National Planning (BAPPENAS) in 2003 – 2004. Paper prepared by Kwik Kian Gie to be presented in the CGI Meeting in 2002 was "edited" by the World Bank. Kwik complained that the content of the paper was changed and did not reflect his view and the GOI's but the World Bank's.

3 BAPPENAS study. (2004). (BAPPENAS is the National Development Planning Ministry).

4 Chowdhury, A. & Sugema, I. (2005). How significant and effective has foreign aid to Indonesia been? Center for International Economic Studies (CIES) Discussion Paper No. 0505. University of Adelaide, Australia, p. 15.

5 A documentary video presented during the farewell party of the Country Director of the World Bank, Andrew Steer, in March 2007, described clearly how the World Bank has been integrated in the Indonesian Economic Team (the Coordinating Ministry of Economic Affairs, Ministry of Finance, Ministry of Trade and the Ministry of National Planning). The documentary video could trigger the question of the independence of the Indonesian economic team, and to certain extent, the question whether Indonesia is still sovereign in making its economic policies.

6 Scott Guggenheim, "Crises and Contradictions: Understanding the Origins of a Community Development Project in Indonesia", paper 2003 downloaded from www.worldbank.org. The Project was started with a local-level institutions study (LLI), which came out with rhetorical conclusions that re-justify the intervention of the World Bank in Indonesia's development which in fact – as the study from BAPPENAS revealed – is only to secure the jobs of the World Bank staff in Indonesia. (Scott Guggenheim is the Director of the World Bank's Decentralisation Support Facility (DSF)).

7 BAPPENAS. (2004). op.cit.

8 Ramli, R. (2004). The IMF's Indonesian myths.

9 MPR is like a Congress in US democratic system, consisting of the House of Representatives and the Senate.

10 Ibid.

11 Ramli, R. (2002), p. 13.

12 In 1998, the Fund postponed loan disbursement three times: March, May and November. This automatically affected the disbursement of loans from the WB, ADB and some bilateral lenders.

13 Chowdhury, A. & Sugema, I. (2005). loc.cit.

14 BAPPENAS. (2004). The existence and roles of the consultative group for Indonesia (CGI). Summary, p. 9.

15 Ibid. In 1999 The IMF admitted its errors in Indonesia in its internal reports. Despite stopping further errors, IMF and the donors kept pushing the implementation of IMF's conditionalities.

IFIs - The Major Barrier to Change in the Aid System

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Introduction

The IFIs sit at the heart of the global aid architecture. The World Bank is a major source of finance for developing countries and the IMF has a crucial function in "signaling" which countries receive more funding from both official and private sources. These roles confer incredible power to these two institutions that have spread their wings well beyond their original mandates. The governance of the World Bank and IMF is severely skewed towards the rich countries that dominate decision-making in these institutions.

The World Bank (WB), International Monetary Fund (IMF), Asian Development Bank (ADB) and other donor agencies have, for the past few decades, provided Bangladesh with loans and grants in the name of such lofty pretexts as 'poverty reduction' and 'international development'. However, these loans inevitably come tied with conditions which hinder the country's economic growth and poverty reduction. The detrimental effects these conditions have had on Bangladesh are immeasurable, putting the country under increasing pressure to abide by the prescriptions imposed by the donors.

IFIs and Conditionality

As advocates of corporate globalization, IFIs and their allies work for international capitalism, exerting a heavy influence on global trade policies that mainly promote trade liberalization and public sector privatization. Many of the least developed countries (LDCs) have become a place of experimentation for trade liberalization at the hands of international financial institutions (IFIs) who pressure the government into liberalizing trade policies. This causes serious devastation in public service sectors including health, education, water, agriculture and food.

Despite the movement for democratization across the developing world, International Financial Institutions (IFIs) have continued to bypass parliaments, a trend at odds with donor insistence on 'good governance.' The WB, IMF and Regional Development banks attach conditions with an intention of economic reforms which they legitimize through a range of documents including Poverty Reduction Strategy Papers (PRSPs).

PRSPs contain conditions such as cutting social expenditures - also known as austerity - implementing user fees in basic services such as education and health, focusing economic output on direct export and resource extraction, devaluation of overvalued currencies or lifting import and export restrictions, removing price controls and state subsidies, privatization or divestiture of all or part of state-owned enterprises, enhancing the rights of foreign investors vis-a-vis national laws, improving governance and fighting corruption. Many of these have negative consequences for the situation of the poorest people in these countries.

IMF imposes two types of policy conditions, namely quantitative and structural. Quantitative conditions are imposed at the macroeconomic level of the poor countries, while the structural ones are for institutional and legislative policy reforms. All of them prove to be not relevant to tackling the challenges that the countries face, unfair, undemocratic, ineffective, and inappropriate mainly because they undermine democratic accountability within countries and deprive the poor of access to services (education, health, etc) at a low cost. Yet the influence of IFIs to open up the domestic market is so powerful that the government cannot resist or deny their illegitimate influence and power.

Since the 1980s, IFIs – backed by key G7 shareholders – have become increasingly preoccupied with the structural obstacles to growth and poverty reduction, and have sought to use loans to leverage the reforms that their Washington-based economists have deemed desirable. As a result, the average number of World Bank conditions per program tripled between the early 1980s and mid-1990s, and by the 1990s IMF 'mission creep' led to its bolstering the Bank's efforts with its own structural conditions.[1]

The World Bank provides most of its loans for a specific project on the basis of particular strategic policies, called Structural Adjustment Programmes (SAPs). The main conditions of SAPs have been: massive privatization of industries and major utilities; the blanket application of the 'free market policy' which actually means a unilateral canceling of all tariff restrictions by the country on the receiving end of the loans; withdrawal of all types of subsidies for the sake of 'efficiency'; and drastic cuts in government spending in order to ensure so-called 'macro-stability' of the economy.

The Dominant Position of the IFIs

In many cases, in terms of policies and projects, IFIs are directly violating the principles of the Paris Declaration. Aid is more aligned to structural adjustment policies striving for trade liberalization and privatization than nationally created development plans. The supremacy of donors continues to rule the day. Furthermore, by acting as the gatekeeper of aid disbursements by other countries, they act as a major hindrance to aid effectiveness reforms.

In the mid-eighties, when Bangladesh was under a military regime, Structural Adjustment Programmes (SAPs) were introduced. The main conditions of these SAPs were: massive privatization of industries and major utilities; the blanket application of the 'free market policy' which actually means a unilateral canceling of all tariff restrictions; withdrawal of all types of subsidies; and drastic cuts in government social spending to ensure macro-economic 'stability'.

This resulted in the disintegration of a number of industries including the Adamji Jute Mills, which left millions of jute growers and jute mill workers in crisis and displaced 26 thousand workers and their family members. The Bangladesh Petroleum Corporation (BPC) has been under tremendous pressure to privatize, as well as the Chittagong Port, a move that would put the oil and gas sector of the country at the mercy of the large multinational companies.[2] Similarly, the small and medium enterprises of the country are on the verge of collapse due to the misguided policy decisions of the IFIs.

Overall the SAPs proved of no use in Bangladesh, leading the World Bank to introduce Poverty Reduction Strategy Papers (PRSPs). However, this was still prescribed by the WB and IMF and agreed to by other donor agencies including the ADB. It reiterated the free market, privatization and liberalization conditions of the SAPs, and the country was forced to accept and implement this PRSP as a precondition for receiving money from the donors. Like other countries, Bangladesh is bound to prepare a PRSP every three years to qualify both for concessional lending from the World Bank and IMF and for debt relief under the Heavily Indebted Poor Countries (HIPC) initiative.

The PRSP does not reflect the needs or the participation of the people but rather violates their fundamental right to development and a quality life. The strategies prescribed in the PRSP are not recognized by the people at large since these were imposed on the country. Civil society groups have had discussions and debate opposing the prescribed document and also criticizing the government for accepting enforcement of this policy. The major reasons for opposing it were because it neither represents people's aspirations and expectations, nor deals with the priority sectors.

The IFIs prevent democratic ownership by applying their strategies as conditional tools over the country. Furthermore, people are kept away from the whole process of the project formulation and implementation and there is no accountability of the donors for their actions. No democratic consultation is practiced either in policy formulation or project implementation processes.

Further issues arise. Not only is the PRSP a set of conditional lending policies imposed by the IFIs, but later other official donor agencies also agreed with the PRSP to be in place. In this way, the IFIs act as a gatekeeper putting strategies in place which other donors and recipient governments are only able to follow. The national government has little choice since it requires the aid and is forced to comply with this. However, it is noteworthy that it did this without even raising the issue in the national parliament. Clearly, the national development priorities have been undermined in the PRSP and the principles of the Paris Declaration are totally ignored and sidelined by the IFIs and other donors.

This dominant position has not changed in recent times. The World Bank, ADB, DFID and Japan have prepared a joint Country Assistance Strategy (CAS) for Bangladesh for 2005-09. The CAS is aligned with the PRSP and encourages other donor agencies to collaborate at the sector level through improved coordination of implementation. By these means, the IFIs continue to dominate the other agencies and to get them to implement their strategies and policies.

Nor have the IFIs reduced their influence in the face of the emergence of Sector Wide Approaches (SWAPs) in the fields of health and primary education. They are yet to align themselves with these country procedures.

Impact of IFI Policies

Many projects undertaken by the IFIs in Bangladesh ignored the opinions of local communities. For example, Khulna-Jessore Drainage Rehabilitation Project (KJDRP), which was funded by the ADB and was implemented in the Southwest area of Bangladesh. The lack of consideration for local communities resulted in a project with disastrous consequences for the environment and communities' livelihood. More than one million people have directly suffered in the area.

Though the project was not successful - as admitted by the ADB - there was no accountability for causing the people's suffering. The victims have not been compensated, though the communities have been calling for this for the past few years. Donor's supremacy and the money-power nexus are imposed over the decision-making process and no accountability is practiced though there was a commitment by the donors to comply with the principles of the Paris Declaration.

In June 2003, the IMF provided Bangladesh with a loan to be released in three years in three installments, with some of the conditions being the renovation of government banks and the privatization of the Rupali Bank. The reform of the banking sector of Bangladesh has already been initiated by the Government of Bangladesh, the name of the project being 'Industry Development and Bank Modernization', with another one called 'Central Bank Strengthening Project' already in hand. The privatization of banks could hamper the capital market as well as the economy as the government would be dependent on foreign capital for a longer period and would lose control over the economy.

Bangladesh has become a place of experimentation for trade liberalization at the hands of international financial institutions (IFIs) which pressure the government into liberalizing trade policies within and beyond the WTO framework. Following conditionalities stressed by WB and IMF, the National Board of Revenue (NBR) decreased import taxes from 2% to 1.5% on 352 products. The IMF pushed for increasing revenue income and decreasing subsidies in the budget, and determined increases or decreases on product taxes. The government could not keep control over tax policies, and as a result, the price of essential commodities skyrocketed.

At the macro-economic level, the IMF has also played a major role in Bangladesh in fixing the national salary structure, reducing the interest rate of *Sanchay Patras* (savings scheme) and raising the exchange rate of the dollar against the local currency taka. These policies have significantly impacted upon people's livelihoods. When investment was much needed to accelerate growth and provide key services to reduce poverty, the IMF-imposed tightening of the credit supply brought strong protest from the country's business community. In the end, tightening the money supply and credit growth through raising interest rates failed to maintain macroeconomic stability; rather, it increased the cost of investment and thus had a negative impact on output and employment. The result, at the end of 2007, was that inflation was creeping up to double digits, but at the cost of investment, employment and GDP growth.

Also since conditionality relates not only to donor goals but also the process for achieving these goals, the people of the recipient countries are victimized in the process. For example, the de-industrialization programme and closure of the jute industry caused serious unemployment. Overall, people have had to bear the brunt of both higher inflation and reducing incomes due to IFIs policies and programmes.

Following IMF conditions, the developing countries' governments are forced to impose taxes on products to increases its revenue income. The Bangladeshi government had to commit to increase the price of oil and gas in order to obtain PRGF funding. The price of fuel has increased by 60%-75% in the past two years in Bangladesh. The price of petrol and octane has increased in the local market by just under 30%. The price of kerosene and diesel has increased by 50%-76%.[3]

The IMF is pushing to increase the price even further, which they believe is good for economic stability and GDP growth. But does that growth really help people? The price hikes of oil and gas have directly affected the livelihood of the people. Farmers and manufacturers, in particular, have been severely hit by the price hike of these core business costs. Even in the recent substantial food price increases, the IFIs are pushing to increase the prices of gas, electricity and fuels, whilst simultaneously prescribing reduced subsidies to agriculture and basic services. This 'double whammy' leaves farmers and people in general in desperate situations.

The goal of increased revenue is not achieved through tax control, a process detrimental to the livelihoods of the people. The IMF conditions are plunging people into misery. Revenue experts suggest that the government should take measures to protect local industries. However, Bangladesh has only experienced trouble with respect to industry and overall economy by following IMF conditions.

The Asian Development Bank in Bangladesh

International Financial Institutions stress quite explicitly the necessity of cost recovery and commercial profitability of water services. They also promote ‘reforms’ of the water sector and introduce ‘public-private participation’ or ‘increased private sector involvement’ that essentially results in the gradual withdrawal of the state from the domain of the utility sector. To make things a little more complicated, the market for water is highly subsidised and especially so in crowded cities, which offer the most potentially lucrative markets, the policy regime is not favourable to commodify or commercialise water and there is a fundamental question of whether the poor should pay for their water.

‘Bangladesh has cumulatively received over US $ 8 billion in aid from the Asian Development Bank (ADB), ostensibly earmarked for the ‘public sector’. Unfortunately, much of this money is used to finance projects supporting private sector growth and trade liberalisation. In fact, one of the ADB’s key operational objectives in its South Asia regional Cooperation Strategy is explicitly stated as “promoting private sector cooperation.” In other words, by “addressing policy constraints,” the ADB proposes to open up Bangladesh’s industries and expose them to the vagaries of the global corporate economy.

The ADB’s Dhaka Water Supply and Sewerage Authority (DWASA) Project envisages eventual privatisation of the water distribution system. The ADB’s massive $838 million Dhaka Water Supply Project is also underway, which it notes will require substantial private investment.

The World Bank has also confirmed its commitment to support the water sector in Bangladesh and noted that the sector requires about $8 billion dollars’ worth of investment over the next 20 years. An obvious means, and presumably the one preferred by both the agencies, to finance the water projects would be private investment gradually pushing the water sector towards privatisation.[4]

The ADB’s recommendations for the future operational strategy are set out in its water sector ‘Roadmap’ of November 2003. It notes that Bangladesh had prepared a ‘sound’ National Water Policy, which was in fact funded by the World Bank and conformed to the set of prescriptions that lending agency must have provided, as well as a draft 25-year National Water Management Plan. Implementation of this draft management plan ‘also needs to be initiated with continuous strengthening for strategic sector development’, notes the roadmap.

The Asian Development Bank hails two specific initiatives regarding Bangladesh and both involve non-state actors. Its publications highlight a particular initiative of organisations that have established 126 locations where they buy water at the subsidised rates and sell it to the slum dwellers at four times the government rate, making a neat 300 per cent profit. This can only be seen as a precursor to wholesale water privatisation since the private operators would find it easier to increase water tariffs.

ADB has also tagged a lot of prescriptions onto its aid, providing a policy prescription to restructure and downsize public sector organizations in order to create space for foreign private sector. It encourages Foreign Direct Investment as a means to provide an inflow of foreign currency, arguing that this would ensure remarkable development of the energy sector and would contribute to develop other sectors as well. At their behest, blocks of the gas sector were awarded to the Multinational Corporations. As a result of these contracts, Bangladesh became obliged to purchase its own gas at triple the price of local companies and in foreign currency. The national exploration agency has been kept idle. The budget deficit and negative effect on foreign exchange reserves increased due to the obligations to foreign companies.

The results of these steps have been disastrous for the economy and the people:

1. the price of gas and power has continuously increased
2. the cost of production at every level has increased, resulting in a fall in competitiveness of Bangladeshi products
3. hard-earned foreign currency is being used to purchase gas and electricity which could be bought with local currency at a much cheaper rate
4. dismantling of local production skill and exploration establishment
5. huge financial losses of state agencies
6. common property becomes private property being used to maximize corporate profit
7. public non-renewable resources like natural gas becomes huge liability.

Conclusion

The International Financial Institutions represent a significant barrier to the achievement of the Paris Declaration principles and the achievement of development goals more generally. They play a very significant role in shaping the policies, strategies and priorities of the developing countries that they work with. They continue to impose policy conditions, particularly related to the liberalization of markets and the privatization of national companies along neo-liberal economic lines. They also impose rules on macro-economic stability, interfering in monetary policy in a way that does not allow countries to invest in their own development.

Not only do the IFIs have a direct impact on developing countries through the conditions they impose on their own aid, but they are also able to exert tremendous influence over other donors who accept their assessments and criteria for the allocation of aid. This reduces the room for manoeuvre available to recipient countries because it reduces the competition between donors and prevents them from being able to seek out alternative funding sources.

The result of this reality is that developing countries are not just held back, but also pushed back into situations of poverty and deprivation. The policies imposed have resulted in job losses, inflation, higher costs of key goods and services and reduced competitiveness on international markets. These have all impacted directly on the lives of everyday people and particularly the poorest.

Overall, the various positive noises coming from initiatives such as the Paris Declaration and IFIs own commitments can be seen to be more rhetoric than reality. The gatekeeper role of the IFIs needs to be challenged along with their undemocratic approaches to policy-making. Rather than a mere reform agenda in the current aid system, a change of paradigm is needed based on democratic ownership, full engagement of civil society, transparency, openness and accountability. Only then will the right policies come about to deliver the best opportunities out of poverty for the poorest countries and the poorest communities.

Notes

1 www.dfid.gov.uk

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The World Bank in Pakistan: See No Suffering, Hear No Cries, Speak No Truth

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Introduction

There is a wide power gap between the World Bank and local communities. The decisions made from a distance by powerful institutions are beyond the control of local communities. In this context, investments in mega infrastructure projects from donors such as the World Bank have served to detach people from their historical entitlements to natural resources. The social disruption, loss of livelihood and environmental degradation associated with these projects push local communities into poverty and deprivation. The concomitant violation of rights such as to food, development and shelter is considered a 'transitory cost' in the Bank's terminology.

Water infrastructure projects funded by IFIs have not only generated huge economic waste, but also caused irreparable damage to the environment and livelihoods. The World-Bank-financed Tarbela Dam and link canals project in the early 1970s reduced fresh water flow to lower riparian zones, especially the Indus Delta. Previously prosperous deltaic communities were forced to migrate. Ecological costs have included sea intrusion, loss of mangrove cover and the disappearance of flora and fauna species. The prevalence of massive poverty in the area is a direct consequence of upstream structures funded by the World Bank.

Similarly, the Asian Development Bank financed the Chashma Right Bank Canal project, which massively disturbed the ecological and livelihood pattern of the area. Flooding caused by alterations in the course of water flows force communities to migrate and negatively impact on the long-term potential of ecosystem functioning and sustainable development, pushing people into vicious cycles of deprivation. Such infrastructure projects are instrumental in extending state and capital control over natural resources through dispossession and limiting people's choices and autonomy.

The reason these projects come about is the dominance of a faulty development paradigm and inadequate accountability. Projects are implemented under the flawed economic belief that investment in major infrastructure projects will generate economic growth that will then seep into local communities and reduce poverty. The question of accountability at local level is omitted at very outset, because the gains are measured at the macro-economic level. The past sixty years have witnessed donors in competition with one another to pour money into such flawed projects, ignoring the fact that previous projects based on economic growth ideology had basically robbed natural resources from poor people and created situations of extreme deprivation.

Poor communities bear the brunt of these projects and yet they are kept away from decision-making processes at all the levels. In developing countries that lack sufficient democracy, the state authorities are unaccountable to the people. Furthermore, the international donor institutions enjoy immunity from domestic laws and there is no mechanism of international law to hold them accountable. Thus, violations of human rights go unchecked and accountability remains an illusion. Nevertheless, indigenous people all around the world have fought around issues of accountability, transparency and governance in powerful institutions like the World Bank, particularly since the last decade of the previous century.

This paper looks deeply into the case of a World-Bank-financed project - the Left Bank Outfall Drain (LBOD) in the Sindh province of Pakistan - which demonstrates how the World Bank violated people's fundamental rights, uprooting them from their means of survival in southern Pakistan. It also shows how the WB failed to take responsibility for its actions after inspection panel findings.

Left Bank Outfall Drain Project

<u>Background</u>

The Left Bank Outfall Drainage (LBOD) project was initiated in 1984. The project aimed to provide a drainage facility for irrigated agriculture in three districts covering about 516,000 hectares through the construction of a network of surface drains, installation drainage tube wells and the Chotiari reservoir.[1] The initial estimated project cost was US $ 635 million. The cost was agreed upon by seven external co-financiers: IDA; ADB; Saudi Fund for Development (SF); Canadian International Development Agency (CIDA); Overseas Development Administration (ODA-UK); Swiss Development Corporation (SDC); and the OPEC Fund for Development. The IDA and ADB were the major donors, contributing US $150.0 and $122.0 million, respectively. The early environmental assessments indicated positive effects for the project. It was considered that drainage would improve the productive capacity of farmland and the quality of vegetation, whilst reducing malaria.

<u>The problems</u>

The implementation of the project was disastrous and both the World Bank and ADB have accepted that their performance at the preparation and appraisal stages was not satisfactory. The work of the LBOD project could not be finished to the estimated cost and time and remaining works were included in the National Drainage Program (NDP) launched in 1998 and co-financed by ADB, the World Bank, and the Japan Bank for International Cooperation. The total cost of the LBOD at project completion was estimated to be US $1021.0 million by the World Bank, $385.3 million or 60% higher than the appraisal estimate.

Even more seriously, the project design was too focused on physical and engineering aspects, with insufficient emphasis on social, financial, communication, and environmental aspects.[2].The consequences for local communities have been devastating:

- The project has made communities so vulnerable that in any monsoon rainy season the upcoming drainage effluent could displace them.
- In the 2003 rains, flooding, breaches and sea intrusion caused the deaths of more than 50 people, thousands of houses were damaged and thousands of acres of agriculture crops were destroyed.

Damage Caused By Project-Induced Flooding In 2003

Type of damage or loss	Number
Human life[3]	56
No. of villages affected	506
No. of households affected	21,134
No. of people affected	126,804
Crops (acres)	
Rice	49,330
Sugar cane	13,699
Others	10,530
Total crop acres	73,559
Livestock (numbers)	
Buffalo/Cows	885
Goat/Sheep	2,623
Others	157
Total loss of livestock	3,665

Source: District Administration Badin Pakistan.

The total estimated cost of losses during the 2003 flood was Rs.1, 287 million.

- The drainage network has badly affected the environment of the Indus Delta. There is now no fresh water available to maintain the ecological value of the delta, which is essential for coastal forests and marine life. In the absence of fresh water, the disposal of toxic drainage effluent has contributed to the destruction of the remaining natural resources.

- Agricultural land is increasingly encroached by seawater channeled through the project infrastructure and entire grazing areas have been lost.

- The ground water - which is a unique drinking source - has become badly polluted causing severe impact on human health.

- Important wetlands ecosystems (including two Ramsar sites) have been destroyed with severe loss of habitats and fish. These Dhands (wetlands) provided livelihood resources to forty villages of fishermen having a population of 12-15,000 living around these water bodies.

- After the loss of other sources of livelihood, pressure on scarce forests has increased.

- The project has badly affected the indigenous *Mallah* community. The flooding and devastation that ensued during the 1999 cyclone and 2003 monsoon changed the economic base of these people. Both these shocks were interconnected with the operation of LBOD and aggravated by the overflowing and breaches of infrastructure installed by the project.

A large number of people who either owned land or were happy with fishing, agriculture or livestock rearing have been impoverished. Local communities which were heavily dependent on natural resources for their livelihood have been robbed of the very means of survival and denied the right to life, livelihood and development. These effects and costs were not included in the cost-benefit analysis of this infrastructure project.

The project design and implementation suffered from major defects, many of which contributed directly to the displacements and dispossession experiences during the extreme events of 1999 and 2003. The construction of a tidal link invited sea intrusion and the tidal link canal subsequently collapsed. The Choleri weir was a flawed engineering structure. Its subsequent collapse caused sea water to flow into and degrade wetlands. The Chotiari reservoir and related irrigation infrastructure was always unfeasible as there was no water to fill it. The tube wells and drains were dysfunctional. The project wasted money, took longer to implement than anticipated and cost more than planned.

Flawed accountability

When looking for the explanation of why such a bad project was able to come about, one sees quickly that the lack of accountability to the people most affected by it is a key issue. Since the project designers, donors and national government did not consult the people most likely to be affected by the project and there was no information sharing with the people, they were not made aware of all the issues and problems that needed to be tackled. They undervalued the importance of the wetlands to the environment and people's livelihood and totally failed to adequately consider the sustainability of the project's management.

The idea to dispose of drainage effluent through the southern coastal belt in Pakistan by connecting a drain with an active sea tide was never discussed with coastal communities. Historical routes where rivers use to drain into the sea were bypassed and an artificial drain in the form of a tidal link was created, cutting through coastal lagoons. Local wisdom would have been enough to avoid future disaster, but it was not sought. Where local communities became aware of what was happening and raised their voice against ill-planning and the future threat to their lives and livelihoods, they were ignored.

Violation of Human Rights by the Project

The project clearly violated human rights, for which the Government of Pakistan and multi-lateral donors must be considered responsible.

All these violations of the fundamental rights of people came in the name of development and development cooperation. The blind eye of international capital and its collaboration with local non-democratic elite structures forced people from their ancestral land and destroyed or removed their access to other resources. This case indicates the serious lack of accountability mechanisms in place to make aid work for the poor or at the very least not make them more vulnerable to shocks.

The only accountability mechanism available was to approach a World Bank Inspection panel. The owners of resources whose rights were massively violated did just this, raising their concerns and complaints. The investigation of the panel members backed up many of the communities' claims, thus endorsing the community's view of how irresponsibly the Bank played havoc with the livelihood of people.

The panel found:

1. Technical flaws in design

- The alignment of the main disposal drain was technically and environmentally risky. Remote sensing data confirmed doubts expressed by the local people.

- A more appropriate technical option would have been to follow the natural route (known historically to the communities) and link the LBOD with Shakoor Dhand.

- Significant technical mistakes were made during the design of the Tidal

Human Rights Obligation	Violation
Article 3 of Universal Declaration of Human Rights which says "Everyone has the right to life, liberty and security of person"	56 people were killed in the 2003 floods and many more are at risk of flood and hunger.
Article 1 of the Declaration on the Right to Development "The right to development is an inalienable human right by virtue of which every human person and all peoples are entitled to participate in, contribute to, and enjoy economic, social, cultural and political development…"	The project not only excluded people in its development, but the infrastructure created caused people to migrate and lose control over their natural resources and means of livelihood and developing.
The Covenant of Economic, Social and Cultural Rights, which calls on States Parties to take appropriate steps to *"improve methods of production, conservation and distribution of food by making full use of technical and scientific knowledge, by disseminating knowledge of the principles of nutrition and by developing or reforming agrarian systems in such a way as to achieve the most efficient development and utilization of natural resources";*	The project induced displacement, loss of crops, fishing and agricultural land. Malnutrition is very common in the area as local communities, after losing control over productive resources, are unable to meet their food requirements. The local communities' capacity to live healthy lives has been reduced whilst their vulnerability to disease - particularly amongst children - has increased.
Right to Safe Drinking Water, *General Comment 15 on the right to water mentions that "The human right to water entitles everyone to sufficient, safe, acceptable, physically accessible and affordable water for personal and domestic uses."*	The project caused flooding and the pollution of surface as well as ground water resources used for drinking.
Ramsar Convention	Project structures have completely damaged two Ramsar sites i.e. Narreri and Jhubo lagoon

Rio Declaration on Environment and Development, including: *Principle 1: Human beings are at the center of concerns for sustainable development. They are entitled to a healthy and productive life in harmony with nature.Principle 3: The right to development must be fulfilled so as to equitably meet developmental and environmental needs of present and future generations.Principle 4: In order to achieve sustainable development, environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it.*	The project was too focused on physical infrastructure, with people never being at the center of the development logic. An environmental management plan was not properly prepared and implemented. The project caused severe damage to the natural environment and reduced the future development potential of communities.

link embankments and the Choleri Weir. Tidal link structures were critical to the performance of the system but the design had substantial inherent risk. The underestimation of risk and lack of appropriate technical measures contributed to the suffering of local people in lower Badin.

- Designers did not evaluate the likelihood that, under prevailing metrological conditions, high surface water run-off from upstream areas would coincide with high water levels in the Arabian Sea causing flooding.

- The construction of the Tidal Link and embankments cut off and diverted the surface flow and consequently destroyed grazing areas in the area of Runn of Kutch. The overall morphology of the region is being changed.

- The outlets of low-lying drains linked to the LBOD such as the Seerani drain are now under the influence of tidal movement. At high tide, water flows back into these drains causing salinization of groundwater and of adjoining land.

2. Social Problems

- Fifty-four breaches in the embankments occurred at different locations, bringing devastation and loss of life to adjacent communities.

- The LBOD system, combined with the partial destruction of the Tidal Link, has heightened the risks to local people from flooding. The situation is particularly bad when heavy rainfall inland and high tides and storm sea coincide. Floods during rains in 2003 led to the loss of many lives.

- The Bank failed to identify emerging risks during appraisal that LBOD/Tidal link problems could lead to significant harm and even displacement of local people, even though the project had plans to complete and expand LBOD.

- The Bank failed to take the necessary actions under OD 4.30 to identify and prepare for the possibility of such displacement, and the extent to which it has occurred.

3. Environmental problems

- Tidal link failure led to major harm to the Dhands ecosystem, wildlife and fisheries, upon which many people depend for their livelihood.

- Although it is difficult to separate impacts of the LBOD system from those of investments financed under the NDP project, the evidence indicates that the two, in combination, have contributed to significant adverse impacts on the internationally recognized wetland sites.

- Under the NDP project, neither the potential environmental nor the potential social impacts of the project in the area of concern to Requesters were considered in a meaningful way until the submission of the Request.

- Increased salinity has affected large tracts of agriculture land.

- Saline intrusion up the Indus Delta has harmed agriculture, including damage to 1.5 million acres of farmland in Thatta and Badin, causing dislocation and extensive economic losses.

- The water supply has been reduced and contaminated (by saline drainage and biocides), in Hyderabad, Karachi, Thatta and Badin.

- The 1993 DSEA analysis of alternatives rapidly became out of touch with the situation on the ground. Most importantly, the analysis underestimated the potential negative environmental effects in southern Sindh of relying upon and expanding the LBOD.

- There was a failure to develop and, in particular, to implement adequately an Environmental Management Plan for the project.

- The project focused on ensuring the evacuation of LBOD effluents, and paid little attention to impacts on, or means to rehabilitate, the Dhands as a habitat and ecosystem. The negative effects on the Dhands amount to a “significant conversion or degradation” within the meaning of OP 4.04.

- The Bank did not adequately consider the risks of further degradation of the Jhubo lagoon, a critical natural habitat.

4. Other Issues

- Unfortunately, the people of Southern Sindh, whose lives were already recognized as being affected by the Tidal link, fell outside the field of vision of those who designed and appraised the project.

- The Choleri Weir collapsed only one week after the publication of the implementation completion report (ICR). There is concern that the ICR that was circulated to the Board was insufficiently transparent on important shortcomings of the project.

- Management was slow to visit the site of the Tidal Link failure, and did not have a consistent approach to interacting with the local population to understand and address the social and environmental implications of this failure. Management's failure to consult with people affected downstream for over half a decade following the breaches in the Tidal Link is of great concern.

5. Conclusion

- To a very large degree, the damages suffered by people in the project-affected areas have not been redressed, and many of the same conditions that led to these are still in place.

The World Bank's Refusal to Take Responsibility

In the wake of the independent panel's observations, it was expected that the Bank would accept the truth and take responsibility. However, it refuted all of the panel's observations. By not accepting the communities' concerns and trying to place responsibility on government institutions, the Bank called into question the validity of its own accountability mechanism (inspection panels). There was no other accountability mechanism available to make the Bank take responsibility for the damage it caused and the lack of respect of the people's right to natural resources.

The communities have used all the peaceful means at their disposal to protect their rights, but all in vain. They are still waiting for justice. Frustratingly, the Bank rightly identifies the problems facing the delta and surrounding areas, but is silent about the causes of this situation. In its management report and recommendations for the area it says: "While salinity may be the biggest challenge, other important threats to development benefits in the Indus Basin are growing in importance… urgency-management of the coastal zone and the delta, conservation of wetlands and related environmental services, and management of pollution and water quality. In Sindh and Badin District in particular, the major changes in the Indus Delta that have occurred sine the development of the Indus Basin's water resources have resulted in sea intrusion, increased salinity and loss of mangrove forest diversity and extent, and reduced productivity of the estuary."(Para 17)

The management recognizes the degradation of the Indus delta and the poverty and environmental risks in lower Badin and Thatta districts but wrongly highlights natural disasters as the main cause. It also recognizes the suffering of Badin and Thatta as a result of inequity in water distribution. However, the plan of action prepared by the management to address the problems raised in the inspection request and backed up by the panel experts is a joke. None of the communities' concerns have been addressed, but rather the Bank has approved another loan to fix the problem created by two earlier projects.

Conclusions

World Bank-funded projects, including the Left Bank Outfall Drain Project, construction of the Tarbela Dam on the river Indus and other upstream structures to divert water on the river Indus are major causes of the degradation of the Indus delta and sources of livelihood for local communities. Flawed designs and inadequate implementation have reduced fresh water flow, increased the risks from flooding and caused sea water to flood delicate fresh water ecosystems.

The bank used a totally misplaced analysis of the sustainability of the infrastructure projects it chose to implement and failed to take into account the needs and risks facing local communities. None of the projects recognized the need of water for the delta because they were all focusing on inequitable economic growth models, based on the idea of producing for export markets, rather than sustainable human development and meeting local needs. The projects totally disregarded the feasibility of alternative approaches such as drastically reducing water use and hence drainage by switching to ecologically-friendly crops and organic farming or reducing crop intensity.

The absence of accountability at both state and IFI level has encouraged these institutions to continue with the same water resource development paradigm in the face of all the disastrous impacts on the livelihood of local communities. They continue to push a model, which only serves to increase existing inequalities in the control of natural resources, perpetuate poverty and keep violating the basic human rights of local communities.

By putting the burden of proof on communities, with only the limited scope to request an inspection, the existing accountability mechanism has been shown to be inadequate and counter productive. It is lengthy and time consuming, overly technical, builds false expectations in the communities and ultimately fails to hold the Bank to account. Even after establishing the fact that people have been severely negatively affected by projects, no justice has been provided to the communities.

In such a situation, aid has been used to strengthen existing power structures, which keep denying peoples' sovereignty over natural resources and facilitates exploitative forces to extract private benefits at the cost of historical owners of resources. Genuine and effective mechanisms of accountability are essential to put a stop to such practices and ensure that aid is used to support local communities in tackling poverty and deprivation.

Notes

1 See Staff Appraisal Report (SAR), Left Bank Outfall Drainage Stage 1 Project, South Asia Projects Department Irrigation 1 Division, World Bank Report No. 5185-Pak, November 5, 1984.

2 See para. 36 of the Implementation Completion Report, LBOD Stage-1 Project, Rural Development Sector Management Unit South Asia Region World Bank Report No. 18037.

3 People died in one sub-district Badin, of district Badin in Sindh province Pakistan. Information collected through police.

Democratic Ownership and Mutual Accountability to International Human Rights: A Reality Check of Nepal

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Introduction

Nepal's developmental failure over the past five decades is attributable not so much to the paucity of resources as to the lopsided consequences of the international aid-based economic and fiscal system. As happened in other countries of the world, aid-giving in Nepal gradually became the preserve of the most unaccountable, undemocratic and opaque international financial institutions (IFIs), working in tandem with private multi-national corporations (MNCs).

There is a crippling paradox at the heart of the international system of power. The rhetoric is strong on ethical symbolism, exemplified by the ratification of a profusion of human rights, developmental and environmental instruments of the UN and other regional organisations, mainly the European, Inter-American and African system of human and people's rights. The reality, on the other hand, is preponderantly dictated by the interests and calculations of global financial capital, represented by the IFIs and private global corporations which flagrantly violate all the international instruments of rights that are supposed to govern the relations between states and with their peoples.

IFIs Undermining UN Principles

Although the IFIs and other trade organisations - such as the World Bank, International Monetary Fund (IMF), Asian Development Bank (ADB) and World Trade Organisation (WTO) - ostensibly aim at promoting national development and claim to uphold the apparent values and principles of the UN, based on equality and human rights without any discrimination, their actions have primarily served more to de-legitimise and erode the credibility of this international organisation. It has also led to undermining of the funding for the UN's rights-based human rights and development programmes.

Inter-institutional conflict was clearly revealed at the 1993 UN World Conference on Human Rights in Vienna, the 1995 World Social Summit in Copenhagen and other follow up processes. By this time, the notion of the collective rights of individuals, peoples and the communities was under attack from the well-packaged global corporate framework of economic and trade liberalisation, privatisation and globalisation. This will not change until there is a well-defined balance of approach, translating the concept of profit into collective national interests, and not narrow corporate profit.

The problem for poor countries like Nepal is that they will be punished heavily both economically and politically if they fail to comply with the global corporate agenda of development. But no punishment or enforcement measures are allowed in the event of violations of UN human rights and environmental treaty obligations in the pursuit of such corporate-led development. UN obligations are confined within the parameters of member states' moral and voluntary obligations and are invoked only if there is no conflict with corporate-led development or the geo-political interests of donor countries.

The tragedy is that the UN system of obligations is more strict and supreme in formal legal terms compared to those of the profit-led corporate institutions. However, what prevails today is the rules for profit and real politik. As a result, even national court systems have abdicated the responsibility to guarantee and protect the constitutional rights or international human rights of citizens. IFIs and MNCs not only enjoy all diplomatic privileges but also impunity for the human rights violations and the economic crimes they commit during the course of their operations.

The UN is reduced to a cash-strapped organization that has to rely on the largesse of tycoons like Bill Gates, who donate a small share of their corporate profits in return for unpublicised but obvious benefits, giving them a standing superior to the governments of the developing countries who make up the majority of the organisation's 193 members!

Why the Paris Declaration?

The Paris Declaration on Aid Effectiveness (2005) is no more than a reflection of the departure from or destruction of the international commitments made during the adoption of the UN Charter (1945), the Universal Declaration of Human Rights (1948) and numerous other instruments developed subsequently between the 1950s and 1970s. These instruments were gradually put in cold storage as soon as the rich countries saw the UN promoting the cause of the third world countries and their billions of poor people.

All the development agencies of the UN were reoriented to conform to market principles and corporate interests and thus rights-based development was repudiated. The old and strong UN framework that the developing countries desperately need has been replaced instead by the Paris Declaration, the principles of which are legally weak, non-binding and unenforceable, with limited moral value. To compound matters, even this inadequate framework is routinely flouted by aid-giving countries and international agencies.

There is no doubt that the effectiveness of aid can be enhanced if all the Paris Declaration principles, limited though they are, are complied with by those who are managing, dictating and controlling the global development process and its outcomes. Even the Paris Declaration of mutual accountability can serve as a meaningful tool to measure development effectiveness. However, that is not the case today because aid and development have become the most effective post-colonial, neo-colonial and neo-liberal tool of the day to continue with the past legacy of domination and exploitation in a more indirect, more faceless and apparently more civilised manner.[1]

Past Failures of Aid Effectiveness in Nepal

In Nepal as a country case study, it is important to highlight some of the characteristics of aid-funded projects and activities, particularly after the democratic changes ushered in after the 1990 peoples' movement. Nepal, relatively speaking, had a fair constitution that guaranteed most of the civil and political rights, and recognised all the basic economic, social, cultural, environmental and developmental rights (although not explicitly as ‘rights’, but at least as directive principles of the state). They were to be enforced by law whenever possible.

However, the new democratically elected governments that replaced some three decades of absolute monarchical dictatorship were forced by the IFIs and bi-lateral donors, mainly the World Bank, the IMF, the ADB, the US and the United Kingdom, to put in place the globally designed free-market policies as a condition for receiving aid. As a result, even a Nepali Congress government with the strongest leftist opposition in parliament and, subsequently, a full-fledged but a minority government of the Communist Party of Nepal (Unified Marxist & Leninist) (or CPN-UML) could not do much in protecting Nepal’s national interests and priorities in the economic and development sectors.

Any attempts these political groups made at formulating pro-people policies, such as the social security provisions for the elderly, or subsidies in food, drinking water and electricity, or grants for local government were heavily criticised by the aid agencies. Whatever the UML government tried to achieve on the fiscal, economic and developmental fronts provoked the ire of the liberal parties, leading to the collapse of the government in nine months in 1995. All Nepal’s major aid agencies were involved in the political manoeuvring that led to the downfall of the first ever elected communist government. If the UML government had been given a chance to run the country for some years, the face of Nepal today would have been drastically different. The country could have been spared the 10-year Maoist insurgency launched by the Communist Party of Nepal (Maoist) (or CPNM) and the ensuing claim that Nepal had become a ‘failed state’.

In fact, the same aid agencies and IFIs were mainly responsible for all the fundamental failures of the 15 years (1990-2005) of the multi-party system. This was one of the main reasons behind the systematic growth of the Maoist insurgency and the successes of the People’s War (1996-2006). Even the World Bank has recognised this fact and described the Maoist rebellion as an ideology-based political movement catalysed by the economic and development failures and corruption of the period.[2]

Two examples of failed initiatives by aid agencies are part of the development folklore of Nepal. In one instance, the UNDP failed to eradicate poverty even in the one district, Syangja, that it chose for intensive intervention. Its programme failed despite all its vision statements, missions, programmes, staff and funds. There is also the curious case of the USAID’s development project in the Rapti zone. Soon after the completion of this project was announced amidst much fanfare, the Maoist uprising began in this very area. One main reason is that their development approach and process created more poverty and intensified the inequality between the ‘haves and haves not’ and, thus, rural youth were ready to join an armed struggle once they were provided the visionary Maoist leadership.

Another instance of failed development intervention was an international NGO’s model projects in the districts of Sindhuli and Sindhupalchowk which were withdrawn after a decade. The INGO not only left these two districts in a mess but also disturbed the local farming pattern and methods which they are now correcting gradually.

There were other potentially damaging interventions that would have had long-term damaging consequences, but which were stopped by popular struggles. The Arun 3 hydroelectric project was one such instance. It was to be implemented in 1993 with over four dozen lending conditionalties of the World Bank that would have made Nepal a virtual donor colony, but which was eventually cancelled in 1995 due to massive local and international campaigns offering better alternatives to implement smaller, cheaper and better hydropower projects.[3]

The ADB-funded Kali Gandaki 'A' hydroelectric project also had adverse lending conditionalities. The Khimti and Bhotekoshi hydropower projects funded by the private sector aid/loan window of the ADB and the International Finance Corporation involved conditionalities that resulted in power purchase agreements signed under duress by which inordinately high electricity tariffs were imposed. Due to the aggressive stance taken by donors on the aid/loan conditionalities imposed by the ADB on the Melamchi river diversion and Kathmandu water privatisation projects, even the Maoists are now afraid of pushing ahead with the cancellation of patently unnecessary and corrupt projects.

There are other examples of such projects which are heavily controlled by donors, with the national government not even exercising the right to decide which projects should be implemented and which should be rejected. There is never any transparency in the process and decisions are made unilaterally. Most of the experts, consultants, equipment and raw materials are procured from outside Nepal, so national capacity is never developed, and no information is ever furnished to the public about any of the details, procedures and consequences of the project in a timely and meaningful manner. Under such circumstances no underdeveloped country can ever progress.

The Latest Reality

Despite all the criticism that has been raised around such flawed projects and practices, these foreign-aided projects come with more strings attached than ever. They create more contractual obligations for the recipient countries to comply with, thereby raising the financial and environmental costs.

One of the main reasons for this is that IFIs support a contract framework known as FIDIC or Federation Internationale des Industries et Consultants. Once a project is signed as a FIDIC contract, the recipient countries or governments are bound to pay any amount of additional costs or cost over-runs to the contractors as recommended by the consultants. Contractors win most of the cases that go to international contractual litigations and arbitrations. In Nepal project costs have increased up to 70 percent, such as in the case of Kali Gandaki 'A'. There are several on-going water supply and hydro projects in Nepal financed under the FIDIC framework.

Another aid-financed project framework is called BOOT, or Build, Operate, Own and Transfer, under which recipients as well as local communities lose almost all their sovereign and traditional rights to co-own the projects and associated natural resources such as access to rivers and water for future use or even daily use in some cases, e.g. the proposed controversial West Seti hydroelectric project.

As this is becoming the standard practice worldwide to guarantee the highest amount of profit for corporations, recipient countries are always on the losing side. Although these BOOT projects are supposed to be beneficial to recipient countries as they get it back 'free of cost' at the end, what they really get is the transfer of ownership of the project after its useful life is over, typically with unbearable maintenance costs.

No questions are or can be raised as regard disclosure of information to ensure transparency in such projects. The opportunities for participation and involvement throughout the project cycle are limited.[4] Environmental assessments and compliance with mitigation plans are usually fictitious. No effective attempts are made at benefit sharing with the local beneficiaries. Moreover, such projects have violated international and domestic rules, regulations, norms and standards of human rights and socio-economic justice. Even the ordinary and accepted rights of labourers and workers as per international law are not respected.

In such an aid regime, there is simply no possibility of establishing mutual accountability and transparency in aid-funded projects. There is certainly more willingness on the part of recipients to comply with such standards or principles, such as the Paris Declaration, but less or none on the part of the IFIs and major lending/donor countries or agencies.

A New Political Reality in Nepal: The Rise of the Left

In the case of Nepal, there is now a new dimension that the corporate world of aid and lending has to contend with—the institutional rise of radical left-wing politics. The recent and first ever elections to the Constituent Assembly amply demonstrated that Nepal is overwhelmingly a left-wing country, with the Maoists and the UML alone garnering more than 50 percent of the vote. Nepal now has another opportunity to correct the mistakes of the past, reforming existing aid policies and projects that are harmful for Nepal, removing the constraints to the growth of the country's trade and entrepreneurship and coming up with a comprehensive socio-economic and fiscal transformation package addressing the needs of a broad spectrum of Nepali society, in accordance with national requirements, national priorities and local capacities.

For the donors, the extraordinary performance of the Maoists has come as a surprise since they were confident that they would win only a small number of seats. While they have reluctantly come around to accepting the outcome, they are extremely unhappy with it. Accustomed to dictating terms to Nepal for decades, they have suddenly come face to face with the reality that the people of Nepal wish to make their own independent decisions. The dilemma for them is whether to stand by norms of electoral process or to express their ideological biases beyond their territorial jurisdiction or legitimate concerns. If a new Nepal is to be considered a fully sovereign state, then the donor community will have to abstain from interfering in its domestic development priorities as has been their wont in the past.

The lesson that all the donors of Nepal need to learn immediately is that development effectiveness cannot be ensured in the country if they persist with their old ways. The spirit of welfare-based democratic socialism has been born in Nepal and reactionary forces will find it difficult to suppress it. The usual slogan they chant, "*communism is dead,*" will not work in Nepal. For the majority of rural Nepalis and poor urbanites, the world of Bush and the US war on terror simply do not exist and their priorities are more focused on everyday issues of livelihood. The change that has come about in the Nepali polity is due not only to the Maoist People's War and the UN-monitored peace process but also to the desire for everyday transformation.

There are only two options in front of the Maoists. Either they will have to confront the donor community and take a strong stand or they can simply cave in to international pressure for the sake of remaining in power - a suicidal mistake the UML made in 1994-1995. The communist-phobic West must be made to realise that the dominant mood in Nepal is anti-neo-liberal and anti-imperialist. The aid community must understand that the power structure of the new republic of Nepal will reflect the pluralism of society and must, therefore, pursue a progressive national agenda of independence and people-led development. This is difficult for members of the international community in Kathmandu to swallow since they have used their financial clout to purchase the loyalty of the entrenched upper caste vested interests that had been running Nepal.

International Civil Society as Donors

It is relevant also to touch upon the reality of aid that comes through international civil society as intermediary donors. Known as international non-governmental organisations (INGOs), many of these organisations channel their aid through national or local non-governmental organisations (NGOs). Some of these INGOs are not very different from official donors as they practice the same values of development and adopt the same corporate managerial style.[5]

This type of INGO takes money from their governments and establishes its own bureaucracy and control mechanisms in its own capital. The mutual agreement between such INGOs and their supporting governments is that the same philosophy of development will be perpetuated through the aid disbursed through them. Even the better INGOs are not allowed to go beyond the boundaries fixed by their governments as the original donors. There is now a new practice that development aid cannot be given to NGOs or civil society organizations in the south unless they have an INGO partner in the north – which then becomes a new form of dependency!

As a result, a huge part of the money allocated for the south goes towards operations, salaries and travel expenses of INGO officials in the north. The rest of the money is then invested in development through national or local NGOs that are more accountable to their paymasters in the north and proportionately non-transparent to local society in the actual areas of their operation. These I/NGOs are often actively engaged in undermining national states and political organisations through subtle and explicit propaganda in the areas where they work. In many cases, local NGOs then hijack the prevailing social and political agenda and establish family and party-cadre-based NGO empires.

The main motivation of many of these civil society professionals is the easy access to huge foreign money they have, the capacity it gives them to build patronage networks and the freedom from local control and accountability that they enjoy in the absence of strong laws and a regulatory framework to monitor and ensure the effectiveness of the development work. The way these I/NGOs work is not very different from the operational style of private corporations and the perks of office are equally generous.

In Nepal, it is not difficult to understand why so many professionals and experts have left political and social movements and joined the NGO world or have established their own home-based NGOs for development. These same people are paid money by IFIs and I/NGOs for critiquing their national governments who have, through aid, been reduced to a state of supine dependence and acceptance of internationally driven development agenda.

Given this situation, it will not be surprising if the political struggle against the Maoists or a government led by the Maoists with radical agendas is led by the various NGOs in Kathmandu and elsewhere in the name of human rights. They will try to maintain their stranglehold and with the backing of the international community become focal points for reaction against any progressive and radical policies initiated by the new Nepali state. They will almost certainly also try to undermine all state agencies responsible for delivering public services in the social sector, such as drinking water, food, electricity and healthcare.

It is important to understand that NGOs should never attempt to replace the state and its agencies and they should focus their civil society work instead on advocacy. Learning from the lessons of various national and regional civil society consultations held in Nepal for the Accra process, it was reaffirmed that NGOs like those involved with the International Steering Group (ISG) of the civil society parallel process to the OECD's HLF on Aid Effectiveness can play the role of bridging and liaising with the donor governments and agencies in changing their development policies according to the needs of recipient governments and national development entities. National or local NGOs can also facilitate policy formulation and planning of development within the country, particularly in favour of rural communities and their civil society organisations.

Conclusions and Recommendations

It is imperative to recognise that aid is a temporary instrument and should not be converted into a permanent and institutionalised mechanism of new forms of resource extraction, policy distortions, economic exploitation and political control by international financial institutions and major donors. Aid should not be regarded as money given by the poor of the rich countries to the rich of poor countries. Aid must follow national needs and priorities as proposed by its democratically elected governments in a true sense and not be dictated by IFI conditionality, whether formalised or not. The practice of aid conditionalities, and contractual arrangements such as BOOT and FIDIC in supporting large and destructive infrastructure projects must be stopped and discouraged.

The framework of any aid must be within the boundaries and obligations of UN and other multilateral or regional human rights, environmental and development frameworks, including the Paris Declaration. Aid should be directed towards those who need it most, should reach recipient communities directly and should be spent in the manner most suitable for the local public good. Local government and development authorities must have a significant role in governing aid money and these institutions should be accountable to local communities and not beholden to the IFIs. Civil society can play an important role in ensuring a multi-stakeholder process of democratic decision-making and monitoring development effectiveness. Priority should also be given to budgetary support and national capacity-building and not to project-based approaches.

Developing countries should not be forced to do anything against their national and international framework of human rights and environmental obligations in ensuring equal access and opportunity to all rights and resources, including aid money, and the guarantee of not only civil and political but also economic, social, cultural, environmental and developmental rights. The aid community, and IFIs in particular - who play such a dominant role in this - should also refrain from disengaging with governments that may differ with them on the policies of liberalisation, privatisation and globalisation and rather take an alternative path of development such as that which may emerge in Nepal.

Nepal is now ready to provide an alternative model of development based on UN human rights principles, the Paris Declaration and other emerging norms of the right to development. However, the question remains as to whether the IFIs and aid agencies will allow the dream of a new Nepal to be translated into reality, or whether they will try to make Nepal continue to follow the existing pattern of aid packages or even pull out from the country. Furthermore, will Nepal be allowed to govern itself with full sovereignty by its giant neighbour and donor, India, whose main aim is to control the country geo-politically and to utilise its resources?

Notes

[1] For a better aid framework, for example, see, Oliver S. Saasa, Galio C. Gurdian, Zenebeworke Tadesse & Gopal Siwakoti 'Chintan', Improving Effectiveness of Finnish Development Cooperation — Perspectives From the South, Ministry for Foreign Affairs of Finland, 2003.

[2] See The World Bank, Nepal Country Strategy Pprogramme Document (2004-2007), Report No. 26509-NEP, p. 7-9.

[3] Gopal Siwakoti 'Chintan', 'Constraints and Challenges for Building a New Nepal' in *Contemporary Perspectives: History and Sociology of South Asia*, Volume 2 Number 1, January - July 2008, p. 151-158 (published by Centre for Jawaharlal Nehru Studies Jamia Millia Islamia, New Delhi and Cambridge University Press, India).

[4] For details, visit *www.wafed-nepal.org, www.bothends.org* at Encyclopaedia of Sustainability under the Integrated River Basin Management (Successful Campaigning against Large Dams: The shelving of Arun III in Eastern Nepal) and also *www.inspectionpanel.org* under Requests for Inspection at Nepal: Arun III Proposed Hydroelectric project and Restructuring of IDA Credit (1994).

[5] In Nepal, a western-funded community NGO professional can earn more than of a full-time permanent university professor does. The affluence of the NGO world is evident also in the kind of vehicles that they purchase—Sports Utility Vehicle's like Pajero and Prado. See, Gopal Siwakoti 'Chintan', Foreign Intervention in Politics through NGOs: A Case of the Left in Nepal at Juha Vartola, Marko Ulivila, Farhad Hossian & Tek Nath Dhakal (eds), *Development NGOs Facing the 21st Century: Perspectives from South Asia*, Institute for Human Development, Kathmandu, pp. 134-143.

European Commission: Providing the Kind of Budget Support That is Needed?[1]

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Introduction

Access to basic health care and education is a distant dream for millions of people, mostly wome, around the world. Every day, 72 million children, mostly girls, do not go to school. Every minute a women dies during pregnancy or in childbirth. Every three seconds a child dies, mainly due to diseases that could easily be prevented with access to a doctor.[2]

A key factor in this needless deprivation and suffering is the chronic shortage of health workers and teachers in the world. An estimated two million teachers and more than four million health workers are needed to reach the Millennium Development Goals (MDGs) on health and education.[3] The workers that are there are often grossly underpaid and work in appalling conditions.

Access to basic health and education are human rights, and governments are responsible for delivering on these rights. Over the past decade, many poor-country governments have made extraordinary efforts to increase access to health and education. Countries such as Tanzania, Uganda, and Malawi, for example, have made education free, allowing millions of children to go to school. However, many poor-country governments simply lack the resources by themselves to guarantee access to quality health care and education for all. External aid is needed to fill the gaps in their budgets for health and education.

Unfortunately, many rich countries not only fail to provide the level of aid they have repeatedly promised to give, they also fail to provide the right kind of aid. This article will show that the European Commission, which currently is the biggest provider of multilateral aid, does provide some of the kind of aid that is needed. However, it is still far from enough, and it will need to make some key changes if it is to lay down a challenge to other donors.

The Need for More Budget Support

Today's aid system is extremely fragmented, with hundreds of different providers of aid. Most of them mainly give project aid, which is short-term by nature, is outside the government's discretion, and cannot be used to finance recurrent costs such as salaries for teachers and health workers. This scattered system is highly inefficient and comes with great costs attached. For example, every single week the Tanzanian government receives 19 donor missions and every quarter it writes 2,400 donor reports.[4]

Furthermore, too much aid is still being spent on expensive foreign consultants. For instance, as much as 70 per cent of aid for education is spent on technical assistance.[5]

Some of this is clearly necessary and useful, but in some countries 100 days of consultancy bills cost cost as much as the salaries of 100 teachers for a year, or the cost of keeping 5,000 children in school.[6]

Many donors provide aid only on the condition that poor-country governments implement specific economic policies, including, for example, the privatisation of services and liberalisation measures. Such conditions, frequently imposed by the World Bank and the IMF, can undermine ownership as they leave no room for poor-country governments to design their own economic policies. They can unnecessarily delay aid flows and sometimes do more harm than good, actually increasing poverty. In Mali, for example, aid from the World Bank and the IMF was tied to cotton sector reforms, which according to the World Bank itself would actually increase poverty by more than 4.6 per cent.[7]

Instead of this kind of aid, poor countries need more long-term and predictable aid, which is provided for at least three years and which becomes part of poor-country governments' budgets. This budget support – which can be provided either as general budget support or as sector budget support - should be aligned with national plans to fight poverty, developed in close consultation with civil society. Furthermore, it should be de-linked from economic policy conditions and instead be tied to outcomes related to poverty reduction that do not undermine ownership, and which provide space for poor-country governments to design their own policies.

There is increased international consensus about the need for enhanced levels of budget support and other government-based approaches, as for instance reflected in the Paris Declaration, a set of principles and targets that aim to increase the quality of aid, which were agreed by donors and partner countries in Paris in 2005 and which will be reviewed at a High Level Meeting in Accra in September 2008. Nonetheless, only about 5 per cent of global aid is currently given as general budget support.

Risks of Budget Support

There is a widespread fear that giving aid to poor-country governments is a risky business, and that precious aid money could be wasted by corrupt governments. However, as a joint review of general budget support in seven countries shows, budget support is not affected more by the risk of corruption or waste than other types of aid.[8] In fact, there is no type of aid that is immune from the risk of waste; the rationale in providing aid, despite the risks, is that the returns in terms of poverty reduction are very high. Choosing to completely avoid this risk would mean not giving any aid, which is not an option.

This does not imply that all countries are well placed to receive general budget support. It should only be given to governments that can demonstrate a strong commitment to fighting poverty, in particular to increasing access to health care and education for all and to promoting gender equality. It is equally important that governments have reasonable financial systems to account for the use of resources and that they have plans in place to continually improve these systems, and in particular to enhance accountability towards their citizens.

In countries where the overall government environment is more risky, but where a particular ministry is functioning well, it may be more advisable to give sector budget support rather than general budget support.

The Positive Impact of Budget Support

Evidence shows that budget support does indeed help countries to expand access to basic health and education. A 2005 independent review of general budget support in Burkina Faso, Malawi, Mozambique, Nicaragua, Rwanda, Uganda, and Viet Nam, commissioned by the OECD, reveals that recipient countries have stepped up pro-poor spending and have scaled up social service delivery.[9]

Furthermore, a more recent evaluation of the impact of general budget support, published by the UK auditing office in February 2008, demonstrates that, as a result of general budget support, in Rwanda, India, Zambia, and Ethiopia, many more children go to school and many people have gained access to medical help. The study notes that in Rwanda, for example, budget support has helped the government to increase vital recurrent expenditures in health, supporting the recruitment, training, and salary costs of health workers.[10] In addition, it highlights the fact that defence spending in Rwanda fell between 2003 and 2007, demonstrating that budget support does not necessarily lend itself to abuse.

The European Commission's Budget Support

The European Commission (EC) is the biggest multilateral provider of aid and a strong proponent of budget support.[11] The European Consensus, a key document agreed upon in 2005 that lays out the development vision of the Commission and the EU member states, declares, for example, that general and sector budget support are "the preferred aid modality where conditions allow."[12]

The Commission's preference for budget support is reflected in its spending. Between 2002 and 2005, the EC committed a total of €4.9bn to budget support, or 18.6 per cent of all aid committed. Of this total, €3bn was for general budget support and €1.9bn for sector budget support.[13] African countries are the biggest recipients of the Commission's general budget support, while sector budget support is focused more in the other regions. A positive feature of the Commission's general budget support is that the Commission links it to improvements in health care and education.

The Commission provides the main share of its budget support on the condition that a country meets three general eligibility criteria: it should have a poverty reduction plan; it should work towards improving public finance management (PFM); and it should aim for macro-economic stability. The remainder of the funds are disbursed according to the country's performance against specific indictors on health care, education, and PFM.

Research by Oxfam and the European Network on Debt and Development (Eurodad), based on general budget support agreements with 11 different African countries, shows that each agreement includes performance indicators on health, education, and PFM. Overall, over half of the performance indicators tied to the eleven agreements call for direct improvements in poor people's health and education, in particular for girls and women.

To be more precise, health indicators, such as the rate of deliveries attended by skilled health workers, make up 29% of the total. Education indicators, such as the number of girls going to school, make up another 23%. In addition, 11% of the indicators call for increases in the national budgets for health and education. Another 28% of indicators are PFM indicators.

Sometimes the agreements include other indicators, such as roads, water, and private sector development. Very occasionally, these can be deemed somewhat intrusive. In Ethiopia, for instance, the EC required the introduction of a competition law, application for accession to the World Trade Organisation, and revision of urban land lease laws.[14]

By linking its budget support primarily to outcomes in health and education as well as improvements in PFM, the EC distinguishes itself from other donors such as the World Bank. Research by Eurodad based on 32 agreements in 16 different countries shows that a quarter of the World

Bank's conditions consist of specific and sensitive economic policy conditions, such as privatisation and liberalisation.[15] By moving away from specific economic policy conditions, and instead often focusing on gender-specific outcomes in health care and education, the Commission sets a positive example to other providers of budget support.

Furthermore, evidence suggests that the EC's budget support does help to make a change in poor people's lives. Government spending on education has increased by nearly a third (31 per cent) in eight of the countries that receive some of the largest amounts of the Commission's general budget support: Ghana, Kenya, Madagascar, Mali, Mozambique, Niger, Rwanda, and Zambia. In all but one country (Rwanda), this has resulted in an increase in the number of children enrolled in primary school. In Madagascar, the proportion of children enrolled in primary school increased from 69 per cent in 2001–02 to 92 per cent in 2005. Of course the Commission is not exclusively responsible for these positive results, but the evidence does show that where it is giving large amounts of budget support, headway is being made in reducing poverty.

Longer-Term Commitments

Another advantage of the EC's budget support is that it is fairly long-term. At present, it is usually provided for a period of three years. Furthermore, the Commission is working on a proposal for 'MDG contracts' which it aims to introduce in 2008 (see box). By providing general budget support for a period of six years, with just one mid-term assessment, this ambitious proposal could be a major step forward in terms of increasing long-term predictability. It is a proposal that European Union member states should support.

On-Going Challenges

But while there are several positive aspects to the EC's budget support, it is still far from adequate. The first main problem is that it is still not fully free from harmful conditions. It is particulary problematic that – like most other providers of aid – the Commission generally only gives budget support if countries have an IMF programme in place. IMF programmes commonly have a series of quantitative conditions, which insist that poor-country governments achieve a series of targets such as reducing inflation to single digits, reducing the budget deficit, imposing a ceiling on the wages paid to public servants, or committing to use aid to build up international reserves.

While these aims may not all be wrong in themselves, the IMF approach tends to be far too conservative and to subsequently act as a barrier to more ambitious spending by governments on poverty reduction. This can be counterproductive. Recent independent assessments have shown, for example, that much of the aid increases to some African countries have been ploughed into increasing international reserves at the behest of IMF programmes, meaning that poverty spending has not increased as much as it could have done.[16]

The second main problem is that too often the Commission's aid comes late because of its own burdensome bureaucratic procedures. In fact, according to a 2005 Special Programme for Africa review, as many as 29 per cent of the delayed disbursements are due to the Commission's own internal procedures. Although this is a major improvement compared with 2004 – when as many as 40 per cent of the delays were related to EC procedures – it is still worrying. While acknowledging that in the past five years the EC has shown 'significant improvement in financial management, contracting and processing of Commission paper work', a peer review of EC aid also stresses that partner country governments feel that the

Box 1: Key Features of MDG Contracts

The details of the proposal are not decided yet. The likely features of MDG contracts will be:

- Funds will be committed for six years, instead of the usual three years.
- The main share of the funds will be disbursed on the condition that there is no breach in the eligibility criteria; the remainder will be largely tied to performance criteria on MDGs and public finance management.
- Annual payments for the first three years will be fixed; annual payments for the next three-year period will be set after a mid-term review of performance with respect to MDG-related indicators.
- There will be annual monitoring of performance; under-performance will not immediately lead to cuts in funding (as is currently the case) but rather to a reinforced dialogue.
- If the country is not performing well on the eligibility criteria, this may lead to a temporary withholding of a small part of the annual allocation.
- In addition to the regular entry conditions, there are three further eligibility criteria: countries must have a good track record on implementing budget support over three years; they must show a commitment to monitoring and achieving the MDGs; and there should be an active donor co-ordination mechanism to support performance review and dialogue.
- Up to ten African countries are likely to be eligible.

Source: EC (2008) 'The MDG Contract. An Approach for Longer Term and More Predictable General Budget Support'.

Commission should simplify procedures further still and accelerate programme implementation.[17]

The third main problem with the Commission's aid is that it suffers from a severe lack of transparency and genuine ownership by poor countries. The EC's budget support is usually well aligned with national poverty reduction strategies. However, these often lack true democratic ownership. The EC could do more to ensure that poverty reduction strategies reflect what citizens want and more generally, to ensure that citizens are able to hold their government to account. Through parliament and civil society organisations (CSOs), citizens should be able to influence the design of national policies and the budget, and they should be able to monitor whether the government's spending is in line with the promises made. The EC can support this by including indicators in budget agreements calling for improved downward accountability and by providing financial support to civil society organisations.

At another level, the Commission should do more to make the dialogue on budget support more inclusive. At present, involvement of CSOs or parliamentarians in the dialogue on sector and budget support is a rarity.[18] In Malawi, for example, CSOs are sometimes invited to meetings of the joint donor budget support group, which includes the European Commission, but not to key meetings, and often too late.[19] Contributing to this lack of involvement is the fact that CSOs often have limited access to information. It is not common practice for official documents, such as budget agreements, to be publicly available.

There are exceptions. In Ghana, for instance, the donor community has created a working group to promote a deeper involvement of civil society in the budget support process. In Zambia, civil society has been involved in reviews of the budget support programme.[20] Such examples are encouraging. The next step is for the Commission to embark on a more systematic approach by establishing a more formal mechanism to ensure the involvement of civil society and local members of parliament in the dialogue on sector and budget support.

In addition, in the case of general budget support, the EC should involve the line ministries in its dialogue, rather than only inviting the Finance Minister as is the common practice.

Recommendations

Considering the need for increased levels of budget support based on social sector outcomes, the EC is an important player in international development. In particular, its ambitious proposal for MDG contracts could constitute a positive challenge to other donors, suggesting the provision of budget support tied to social sector outcomes for a period of six years, which goes far beyond current common practice.

However, if the Commission is to show leadership and to challenge other donors to improve the quality and quantity of their aid, it must implement some key changes.

The European Commission should:

- Continue to increase spending on budget support, including by significantly stepping up sector budget support for health and education, in particular to African countries.

- Continue to tie budget support to gender-specific social sector outcomes, while also adding outcomes that promote women's civil rights.

- Continue to tie its general budget support agreements to targeted increases in spending on health and education. These targets should reflect an ambition to reach the Abuja Declaration target of spending 15 per cent of a national budget on health and the Global Campaign for Education recommendation to spend 20% of a budget on education.

- Delink its aid from the approval of the IMF and at the same time put pressure on the IMF, together with the other major budget support donors, to come up in its advice with more flexible fiscal targets and more ambitious spending scenarios. In countries that have achieved macroeconomic stability, the Commission should work with other donors to see a rapid exit from the country by the IMF.

- Reduce unnecessary delays caused by cumbersome bureaucratic procedures to a maximum of 5 per cent of the total by 2010.

- Make its budget support more predictable by implementing MDG contracts and expanding the principles of MDG contracts to more countries and to sector budget support.

- Ensure the involvement of civil society, members of parliament, and line ministries in all steps of the budget support process, including the design, monitoring, and review of the programme.

- Adopt a policy of automatic disclosure of relevant information, with a strictly limited regime of exceptions.

- Strengthen the capacity of civil-society organisations, local government bodies and parliaments to engage in national policy development and budget processes.

European Union member states must:

- Support the plans of the European Commission to implement its proposed MDG contracts, including by providing financial support.

- Increase the amounts they give bilaterally as budget support.

- Use their collective voice on the board of the IMF to push for the institution to leave countries that are stable at the macroeconomic level, and in remaining countries to press for more flexible fiscal frameworks.

- Use their collective voice on the board of the World Bank to push for it to adopt similar processes to the Commission's best practice.

- Increase expenditures on health to 15 per cent of the national budget (as recommended by the Abuja Declaration) and expenditures on education to 20 per cent of the national budget (as recommended by the Global Campaign for Education).

- Tackle corruption and guarantee full transparency and accountability for government expenditure by ensuring genuine participation of local government bodies, parliamentarians, and CSOs in the development of national poverty reduction policies and enable parliament and civil society to monitor and influence the national budget process and government spending.

Notes

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