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Foreign Aid: What Works and What Doesn't

By Carol C. Adelman and Nicholas Eberstadt

The U.S. foreign aid system is broken and must be overhauled. That was the conclusion of the congressionally mandated Helping to Enhance the Livelihood of People around the Globe (HELP) Commission, on which we served and whose final report was released in December 2007.[1] *Our commission's consensus was no surprise: in Washington today, there are few other policy conclusions that elicit such universal and bipartisan agreement. Indeed, over the years, scholars and policymakers have acquired a better understanding of whether, where, and how foreign aid can promote growth and improve public services. With very few exceptions, those insights have yet to result in a new "business model" for U.S. foreign aid. Yet a new business model is manifestly required if development assistance is to avoid endlessly repeating past mistakes—or if it is to capitalize upon important emerging opportunities.*

Like many other bureaucratic organizations, foreign aid institutions are geared to fighting the last war—in this context, to meeting the development challenges of a world we no longer inhabit. Social, economic, and demographic changes in the developing world over the past several decades have been rapid, and they have transformed the low-income landscape in obvious respects, but these realities have yet to be internalized by many of our international development assistance agencies and programs. There are not just new problems to be faced. There are important new opportunities to be grasped. Three major, ongoing changes need to be recognized immediately, and they relate to demographics, health, education, and finance in the developing world.

First, in much of the developing world, especially in Latin America and Asia, economic and demographic changes—including declining fertility and infant mortality and rising life expectancy—are producing a "grayer" population structure and more affluent populations. These trends have tilted the locus of health problems in most developing countries toward such chronic illnesses as cancer, cardiovascular disease, and diabetes, and away from the traditional problems of infectious diseases and child survival. While "traditional" health problems are still predominant in sub-Saharan countries, the chronic disease burden is increasingly significant even in Africa, affecting the working-age population so vital to productivity and growth.

Second, there has been an increase in the skill-based talent pool as millions of people who have studied in developed countries have returned home to start businesses and NGOs. The rise in this pool of trained professionals and entrepreneurs in developing countries means that there are steadily increasing opportunities for aid organizations to partner with local talent. They have an enhanced opportunity to promote "local ownership," self-reliance, and sustainability through their projects.

Carol C. Adelman (carola@hudson.org) is the director of the Center for Global Prosperity at the Hudson Institute. Nicholas Eberstadt (eberstadt@aei.org) is the Henry Wendt Scholar in Political Economy at AEI. They were co–vice chairman and commissioner, respectively, of the U.S. Helping to Enhance the Livelihood of People around the Globe Commission.

Finally, there are major streams of international financial resources available today (some of them entirely new) that were not present when foreign assistance was conceived after World War II. Some 77 percent of total financial flows from the developed to the developing world are private resources in the form of investment, remittances, and philanthropy. These private flows now dwarf government aid to the developing world. Most important, they have opened up entirely new ways of addressing problems. Increasingly, private philanthropists are taking a venture-capitalist approach to aid, viewing themselves as problem-solvers and partners rather than as donors simply providing transfers to recipients. Private resources are flowing through new channels: the Internet, mobile-phone transfers, cause-related marketing, remittances, and social networking sites. Economic growth in emerging economies has been creating considerable wealth, and that wealth is itself local. Large NGOs, such as the Aga Khan Foundation (which focuses on needs in South Asia, Central Asia, and eastern Africa), have now been joined by thousands of community foundations in the developing world that are solving local problems with local funding from wealthy individuals and companies.

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What differs now is not only the nature of the problems in developing countries, but also the unprecedented array of new options for speeding up the tempo of material advance and the spread of prosperity. These changes call for a new business model for moving foreign aid resources. This model will require much more flexibility in aid programming in order to avoid "one size fits all" solutions for a diverse world, and it should be tailored to each country's evolving conditions and development opportunities. It should also be premised on leverage—that is, linking U.S. public resources to the myriad emerging streams of private endeavor that characterize global development and encouraging the emergence of more innovative and efficient ways of delivering assistance and better evaluating the aid's ultimate impact.

Foreign Aid's Role in Growth

Countries are much more likely to grow when they embrace policies that create open economies and encourage trade, private investment, business creation, savings, and innovation. Good governance and the development of a sturdy institutional domestic framework, including rule of law, individual rights, and property rights, are critical to prosperity.

BUt what about aid? For over half a century—since the early 1950s—a great many scholars and students of development have debated whether and to what extent foreign aid helps countries grow. The studies have been strikingly inconclusive. In other words, it has not been demonstrated that official development assistance makes a regular and predictable contribution to overall macroeconomic growth. We reviewed nine major studies, and the majority of them show no categorical relationship between aid and growth, with only one asserting an unqualified positive relationship.[2] The two most dramatic and consequential modern cases of rapid growth and poverty reduction in the Third World—post-Mao China and India during the past two decades—are not attributable in any appreciable measure to flows of official aid. On the other hand, the ratio of aid to GDP is generally quite high in sub-Saharan countries, but more foreign aid has not resulted in increased per-capita GDP in the region. A majority of countries have experienced declining growth as aid has increased, and long-term increases in foreign aid have accompanied long-term declines in per-capita output in more than a few of these states.

Among the reasons adduced in the literature for the lack of identifiable macroeconomic impacts of development aid are that these state-to-state transfers inhibit competitiveness, create dependency, and absorb or misallocate political resources or energies in recipient countries; that aid is motivated by nondevelopment donor and contractor interests; and that aid engenders a lack of feedback and accountability, encouraging host country graft and corruption.

Do Foreign Aid Projects Work, and Why?

Since recipient countries' policies are almost always far more important than the volume of foreign assistance in hastening the pace of material advance in recipient countries, we need to ask: where and how can foreign aid matter? This requires a shift in focus from the macro level to the micro level, to projects on the ground. From the nearly $2.7 trillion in official development assistance transferred to recipient countries since 1960, what evidence of program-level success do we have? And why have the projects been successful? Even if the macroeconomic impact of aid transfers has been debatable, aid projects could still be justified by policymakers, and perhaps even by taxpayers, if they have generated high and sustained returns for their beneficiaries in low-income countries. Determining these characteristics of how foreign aid has positively affected the lives of individuals and communities in poor countries can inform our approach to future aid programs.

Successful projects and programs demonstrate collaboration between American and developing-country institutions, especially private institutions. Indeed, such collaboration seems virtually essential for a sustained engagement that brings benefits valued by all.

In recent years, many bilateral donors have examined the effectiveness of their foreign assistance. By and large, their findings have not been encouraging. In its stark evaluation of Canadian foreign aid, the Canadian Senate's Foreign Affairs Committee concluded that the Canadian International Development Agency has failed to make a difference in sub-Saharan Africa, despite $12.4 billion in aid expenditures between 1968 and 2007.[3] The failure was attributed to slow, unaccountable, and poorly designed development assistance and ineffective foreign aid institutions in Africa. Maintaining that vibrant economies and good governance are the answer to prosperity and that these can only be generated from within African countries themselves, the committee recommended that Canada move to a foreign aid model similar to the U.S. Millennium Challenge Corporation: providing assistance only to those countries that can demonstrate progress in building strong private sectors, creating employment, and strengthening governance.

Australia, Ireland, the Netherlands, and Sweden have also completed assessments of their aid programs that call for improved evaluation, more local ownership, and better institutional capacity in governments.[4] They found that successful projects involved local initiative, good governance, measured results, and the creation of local institutions for sustainability.

Other donors, particularly the World Bank, have attempted to measure programs for results such as poverty reduction. The Bank's evaluation unit found that its poverty reduction record remains problematic. In a 2006 evaluation of twenty-five Bank-assisted countries, only eleven were said to have reduced the incidence of poverty between the mid-1990s and early 2000s, with poverty either stagnating or increasing in the remaining fourteen countries.[5] (Private sector organizations in the United States and other developed counties have also been actively engaged in projects bearing on development in low-income areas for many decades. With some notable exceptions, foundations, private and voluntary organizations, and corporations have not generally evaluated their projects for results at the impact level.)

The U.S. Agency for International Development (USAID) has a long history of evaluation using primarily process and output measures. While some serious, impact-level evaluations have been conducted, the numbers have been low relative to total projects and money committed by USAID. Nor does information from these evaluations or others seem to be used to inform USAID design and implementation decisions.

We reviewed projects from USAID's Impact Evaluation Series and other projects by USAID, the World Bank, foundations, and corporations that have been identified as having measurable impact. We then analyzed them for their shared characteristics. Examination of successful and unsuccessful programs reveals the shared characteristics and principles of foreign aid projects that work.

Shared Characteristics of Successes

Local Ownership and Initiative. Successful programs and projects reflect actual needs of the recipient countries as expressed by local actors, rather than simply reflecting instructions of what projects and programs may be available for local recipients from USAID. Local ownership increases the prospects of long-term success by involving local institutions. Such partnerships can, indeed, lead to the continuation of institutional relationships between American and partner leaders long after the end of USAID funding. The Rotary Club campaign to eliminate polio succeeded because of the ownership and financial commitment of local Rotary Clubs throughout the developing world.

Partnership. Successful projects and programs demonstrate collaboration between American and developing-country institutions, especially private institutions. Indeed, such collaboration seems virtually essential for a sustained engagement that brings benefits valued by all. The U.S. government should always attempt to ensure partners are committed to a program before it makes an investment; as a general rule, the U.S. contribution should be the second or third dollar on the table, not the first. When everyone is committed to common priorities and has made an investment, then everyone will be accountable for the results. With mutual accountability comes sustainability. The Consultative Group for International Agriculture Research, which spawned the Green Revolution, was a partnership among governments, foundations, and the private agribusiness sector.

Leverage. The U.S. government can take advantage of the myriad new sources and techniques of global support for developing countries, including foundations, private voluntary organizations, corporations, universities, and remittances. USAID alliances with new American philanthropic activities overseas can help leverage resources that far exceed those contained in federal budgets. Such partnerships can recognize the priorities and expertise of philanthropic leaders and their institutions. Similar strategies can be used to link U.S. programs to emerging local business leadership in developing countries. Within this framework, USAID would become not a controlling taskmaster of U.S. development programs, but an aggregator or facilitator of effort, the creator of syndicates of resources targeted at self-reliance. While small in scope, USAID's Global Development Alliance has successfully leveraged government funds with contributions from private companies, foundations, charities, and universities. This type of partnership should constitute the business model for virtually all U.S. foreign assistance in the future.

Flexibility. Efforts by today's aid projects to tackle new problems are often hampered by decades-old legislative mandates. USAID's popular child survival program began with a legislative earmark more than twenty years ago. Having spent over $15 billion since 1986, it provides education and preventive services primarily for childhood communicable diseases. Today, however, noncommunicable diseases in adults—such as cardiovascular disease, cancer, and diabetes—have overtaken infectious diseases as the leading causes of death in most of the developing world. Child survival funding has dominated USAID's health budget, leaving little for helping with diseases that are sapping adult productivity and economic growth in the developing world. Where the nature of the problems and opportunities for change are evolving, aid must be able to anticipate and respond to such changes. U.S. governance and democracy programs have demonstrated a flexibility in helping countries. For example, a USAID democracy project in 2001 helped the Nigerian National Assembly improve its budget process to put needed checks on the president's budget. The strengthened legislative arm of Nigeria then voted down then-president Olusegun Obasanjo's attempt to run for office for a third term. Democracy programs, through a variety of tools such as election assistance, media development, and support to civil society, can help countries with what they need at different stages of their political development.

Peer-to-Peer Approaches. Long after USAID's financial role has ended, U.S. foreign assistance can allow America's professionals and institutions to build relationships with their developing country counterparts on the basis of perceived professional self-interest. Such opportunities are exemplified in USAID's Hospital Partnerships Program, through which U.S. physicians volunteered their time to work directly with physicians in Eastern Europe and the former Soviet Union. This peer-to-peer approach is patently superior to the contractor model that currently dominates USAID programming.

Technology Adaptation and Adoption. Some of the most widely acknowledged foreign assistance successes, such as the Green Revolution, have at their core the application of technology to improve the human condition. As the scientific and technological capacity of developing countries expands, so does the potential for technology partnerships in foreign assistance. Local ownership is also important in this context, as integration of technology such as bed nets and oral rehydration salts is vital to ensuring their effective use within the communities where they are introduced. Local foundations' growth and social entrepreneurship's successes in developing countries have shown how technology can work for poor people throughout the world.

Self-Reliance. The most important steps taken to improve the long-term success of developing nations will come from within those countries. In successful and self-sustaining projects, local leaders are the engines of change. Conversely, encouraging leadership and good policies may mean ending or reducing aid to a country. We must not be afraid to withdraw funds to ensure that assistance does not result in dependency in recipient countries.

Continuous Information Feedback. The best evaluation systems are not simply tasks that result in reports. They are continuous information loops that give information to managers in real time so programs can be constantly adjusted to improve performance. Success comes from a sustainable, continual process, not one event, and it requires flexibility to adjust programs to changing situations.

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Risk. A partnership and venture-funding culture implies a tolerance for risk and a frank willingness to recognize failures. Such an attitude, unfortunately, is widely lacking in our aid programming today (for all-too-understandable political reasons). But USAID must be willing to experiment with new approaches to development assistance. If it hopes to increase the likelihood of project level successes, USAID will need to develop a mechanism for rewarding the willingness to take calculated risks within its own personnel and programs.

Recommendations and Conclusions

The pervasive lack of convincing evidence of significant macro-impact from past foreign aid efforts, the changing nature and capabilities of the developing world, and the emergence of new sources and approaches to resource transfers for development all point to a single conclusion: U.S. foreign assistance needs an entirely new business model.

Sectoral and project earmarks, directions, and limitations in foreign aid legislation are a "design for failure" and should be removed, with the exception of those deemed essential to U.S. national security. U.S. foreign assistance programs should be able to respond fully and flexibly to demand-driven opportunities emerging within developing countries.

With the exception of expenditures deemed essential to U.S. national security, the United States should avoid distributing foreign aid without monetary or monetized resources coinvested in and by the recipient country itself. Such in-country organizations may include local affiliates of U.S. NGOs and corporations, indigenous foundations, local businesses, and public agencies. Allocations of U.S. development aid should favor sustainable public-private partnerships in the host country.

The main competition for U.S. foreign assistance dollars should not be among consultants but among ideas coming from the multiple actors now involved in foreign aid and philanthropy, particularly on the demand side of the equation in developing countries. Those who wish to attract U.S. resources should bring to USAID their best ideas and their own resource contributions from private sources, explaining their goals in terms of economic and social impact, local ownership, partnership with local institutions, and achievement of community self-reliance. USAID should operate more like a foundation (and less like a disbursement agency), articulating areas or problems of interest and inviting competition for new approaches.

One fruitful approach for USAID might be to create a venture fund, through which any individual or organization with a new idea about how to solve a problem in development in an innovative way, fostering economic impact and community self-reliance, can apply for a seed grant. The grant would be for limited duration and a limited amount of money, and "risk" would be welcomed. The judgment for awardees would be made twice a year by a peer board. No one receiving USAID money (or who has received USAID money in, say, the last three years) would be allowed to sit on the board. Grantees would report directly to a panel consisting of all government agencies contributing to official development assistance.

America's private charitable donations to low-income areas now exceed U.S. government aid by one-third.[6] Thus, USAID should provide for regular, substantive consultations with private-sector players involved in global development, including foundations, charities, corporations, religious organizations, universities and colleges, and individuals. (Beyond the philanthropic sector, millions of migrants throughout the world are sending more than $200 billion in remittances back to their low-income home countries every year—a sum double all donors' annual official development assistance commitments.) USAID must not only be aware of but also work with the vast array of new players in global development who are transforming the ways in which resources are reaching low-income regions.

The new business model for foreign aid proposed here departs from the past in at least three important ways. First, it is based on flexibility. The programs pursued, the opportunities seized, the partners aligned, and the ways in which funding creates self-reliance are driven not by earmarked legislation, not by the capacities of contractors, not by the world of 1970, but by the nature of the problems and the presence of opportunities from the promises of a changing world.

Second, it reduces centralized control. USAID becomes not the taskmaster of U.S. development programs but an aggregator or facilitator of efforts and a creator of syndicates of resources targeted at self-reliance.

Third, it permits—indeed, even emphasizes—innovation. USAID would seek fresh faces, new approaches, new technologies, and new mechanisms for allocating its resources. It would seek out and link its activities to new streams of resources, looking for leverage for every dollar it dispenses—or, more hopefully, invests—and constantly searching for emerging cofinancing leaders. This business model transforms USAID from a passive funder of projects to an investor in innovation.

Too often, the focus on "fixing" foreign aid is dominated by discussions of organizational structure, the volume of resource commitments, and the configuration or harmonization of objectives and players in the U.S. government. Such preoccupations, of course, are all too easy to understand: they reflect the force of habit, offering "new" prescriptions for "aid reform" that represent essentially iterative adjustments benchmarked against the last round of reform recommendations. Such thinking, however, is based upon and conceptually trapped within a world that existed forty years ago, when the public sector was the leading player in financial flows to poor countries.

Today, the U.S. government's development aid constitutes just 12 percent of total U.S. financial flows to developing countries.[7] It is time to give serious thought to making these expenditures work more effectively. What matters here is less a redrawing of organization charts than a serious focus on how these dollars are delivered and whether they are responding to local ideas and actually reaching partners with stakes in the outcome of the investments. A new business model for foreign aid is the main hope—and perhaps the only hope—for fixing a broken foreign aid system.

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Notes

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