Localising Foreign Aid

Could localising aid help strengthen all sectors of society?

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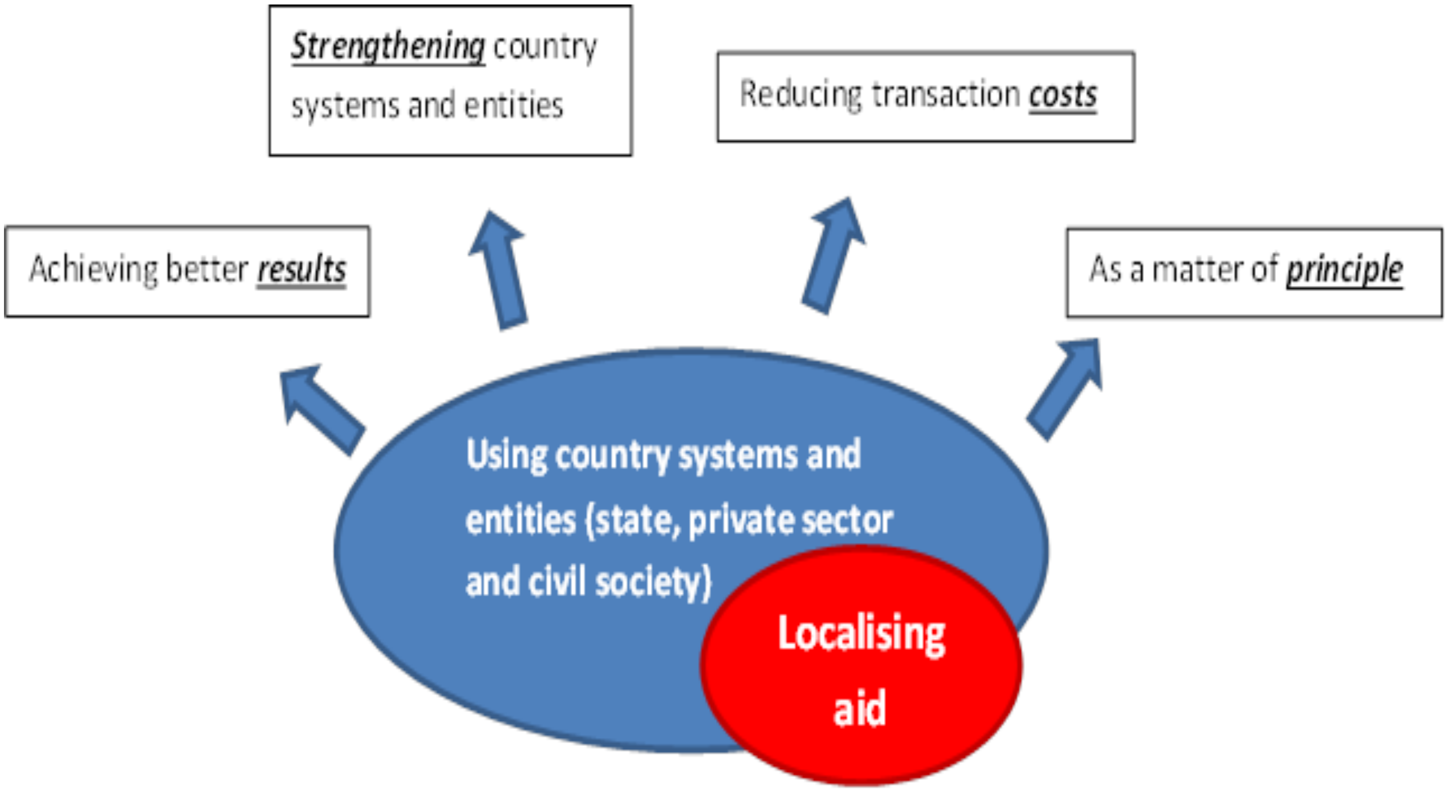
Overview

Localising aid

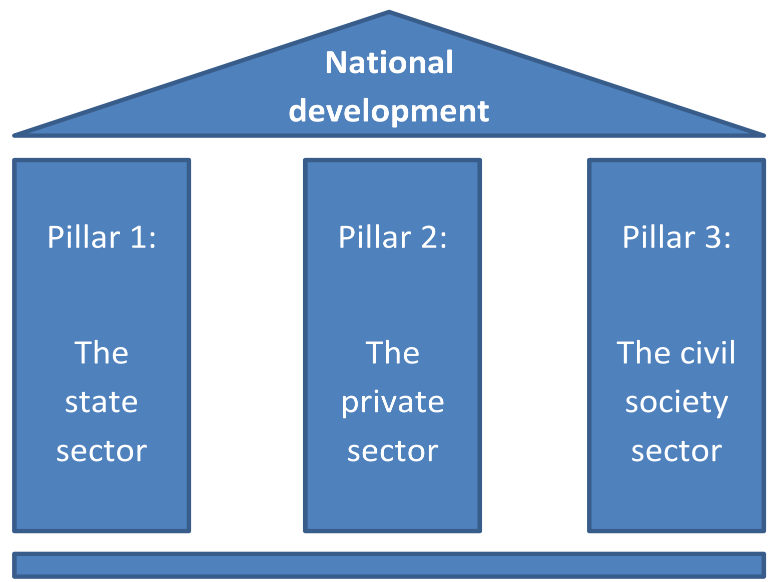
- Research was an extension of the Paris/Accra/Busan agenda which focused on:
  - Development results
  - Sustainability – strengthening local actors
  - Value for money from foreign aid.
- Localising aid is transfering money directly or through national entities:
  - Includes use of national systems
  - Easy to count as transfers to accounts of local entities.

Why use country systems and localise aid?



Research looks at areas neglected in Paris/Accra/Busan agenda

- Country context beyond stable LICs to include MICs and fragile situations.
- Different donor strengths, weaknesses & risk tolerance.
- Three research pillars:



State Sector

Aid to the state sector: What we found

- Consensus in literature that development and the transition from fragility to resilience rests upon transformation of national institutions, i.e. capacity development.
- This process arises from the interrelation between state and society, takes place over many decades and is endogenous.
- Literature indicates that project based aid to deliver public services in parallel to the state can be harmful to the capacity of the state.
- Some positive evidence that localising aid is associated with strengthening national capacity, but lots of evidence that *not* localising aid damages country systems.
- Paris/Accra/Busan recognized the centrality of institutions and the role of aid using country systems to build them, but donor behaviour has lagged behind donor commitments.

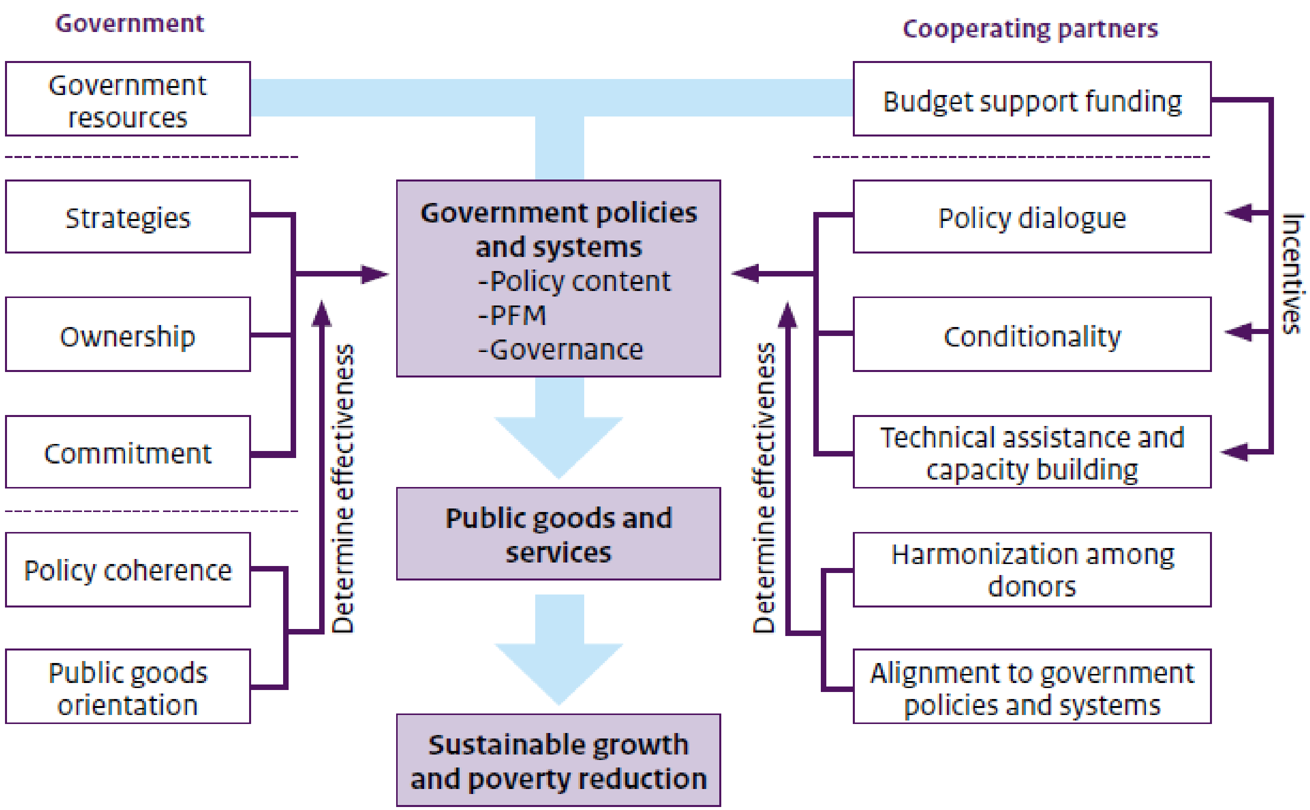
What are country systems?

- The systems in the country used for:
  1. Planning, decision making, monitoring and evaluation
  2. Financial management
  3. Implementation of projects and service delivery

- Note that decisions on public expenditure are political as well as technocratic in almost all countries.
- Donor agency staff tend to take a technocratic perspective and may not understand or like local politics.
- Donors may expect higher standards of decision making and financial probity than in their own countries, or turn their blind eyes for geopolitical reasons.
- Tensions can arise between donors and host governments over issues such as environmental management, land acquisition & involuntary resettlement, gender, use of public funds for political purposes, etc.

Budget support has a complex intervention logic: Difficult to disentangle the impacts of actions by government and donors.

Figure 2.1 *Interaction of budget support inputs*

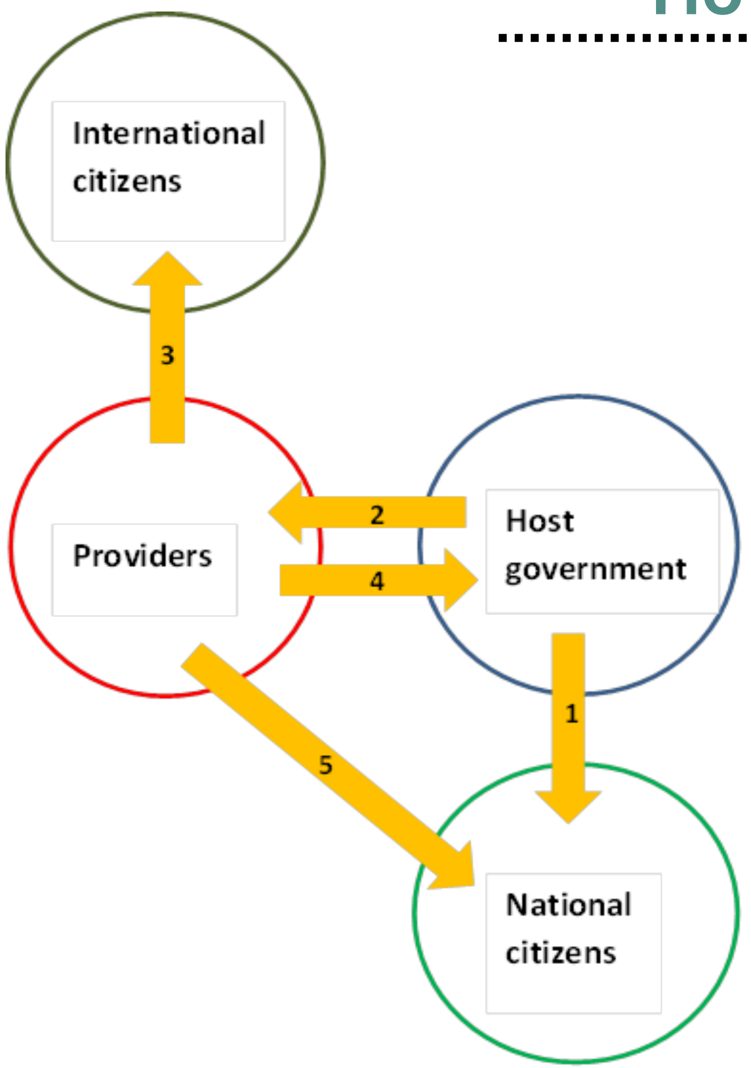


Source: Leiderer and Faust (2011).

1. *Localising aid has created incentives for increased oversight and technical and political engagement* from donor agencies, civil society (national and international), national accountability entities, and the executive branch of government. This effect has also helped to increase donor knowledge of government systems which can lead to better capacity building support.

2. *Second, localising aid has bought donors "a seat at the table" from which to pressure for systemic change*. This pressure has sometimes included applying system-strengthening conditions ("conditionalities") to their aid, but less prescriptive forms of policy dialogue have been more effective and have fewer negative effects.

Incentives and aid
How do accountabilities change?



1. **Host government to citizens: Somewhat strengthened**
   - Governments have greater role in service delivery prompting greater oversight
   - Donors encourage accountability entities
   - Progress in PFM may go broader than aid accountability and lead to improvements across government
   - Governments more able to respond to needs of citizens articulated through local political system

2. **Host government to provider: Somewhat strengthened**
   - Government provides fuller accounts for monies spent

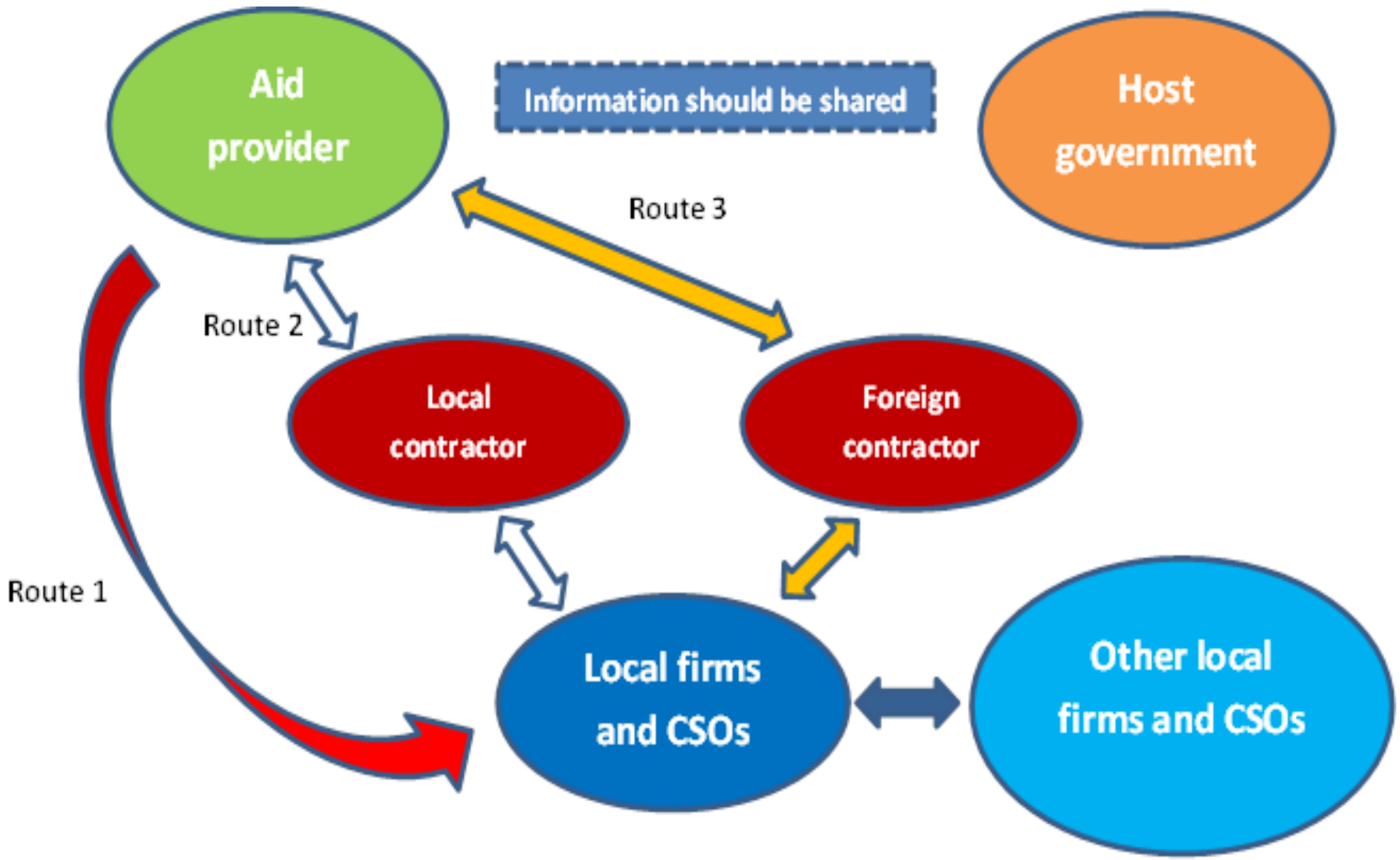
3. **Provider to own citizens: Possibly weakened**
   - Provider somewhat less able to link specific results to own spending as financing streams merged with other donors
   - Provider less able to guarantee non-corrupt or politicized use of all funds if financial controls are weaker
   - Provider less able to implement the development agenda favoured by its citizens

4. **Provider to host government: Somewhat strengthened**
   - More information provided to host government, allowing it to plan & evaluate external interventions more effectively.

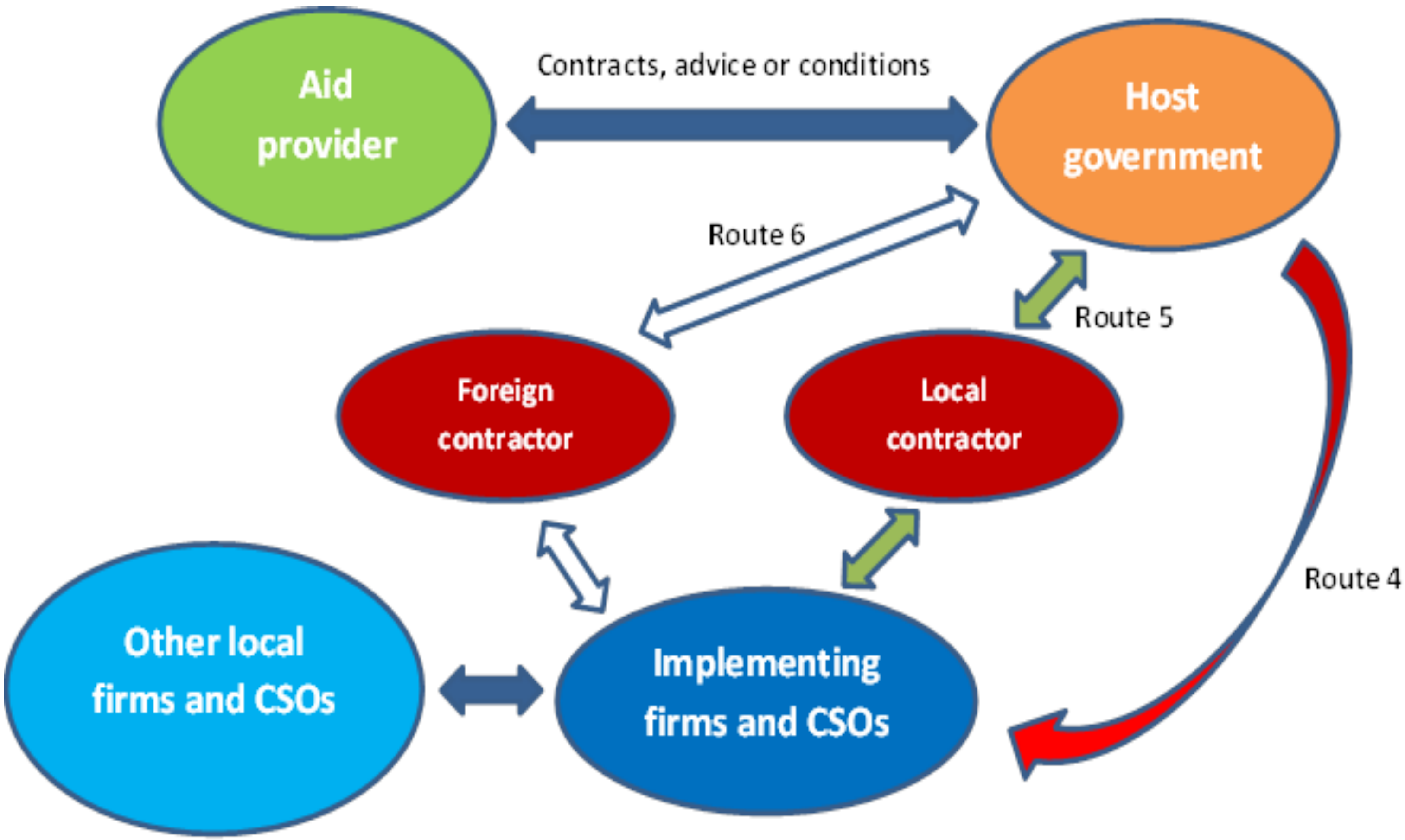
5. **Provider to host country citizens: No significant change**
   - Possibly more information in the public domain, allowing citizens to hold providers more effectively to account

Non-state sectors
Overview

Aid & contracts with non-state actors: (1) Donor issues contracts.



Aid & contracts with non-state actors: (2) Government issues contracts.



Why localise aid to non-state sectors?

- Benefits national economy:
  - Keynsian multiplier effects;
  - Greater local employment;
  - Less distortion of local labour market.
- Increased government revenues.
- Less waste, greater value for money.
- Incentives for local actors to develop capacity.
- Incentives for local firms to become more productive.

But contractual arrangements critical as they can create incentives too for aid dependency by local actors and for higher costs.

The Private Sector

Localising aid to the private sector. What is private sector capacity?

- Our research adopted a productivity approach to defining and measuring private sector capacity, i.e. the efficiency with which the firm can deliver outputs.

The output of firm i in period t, Q_{it} can be shown as:

$$Q_{it} = TFP_{it}.K_{it}^{\alpha}.L_{it}^{\beta}.M_{it}^{\gamma}$$

Where:

K_{it} = capital of firm i in period t

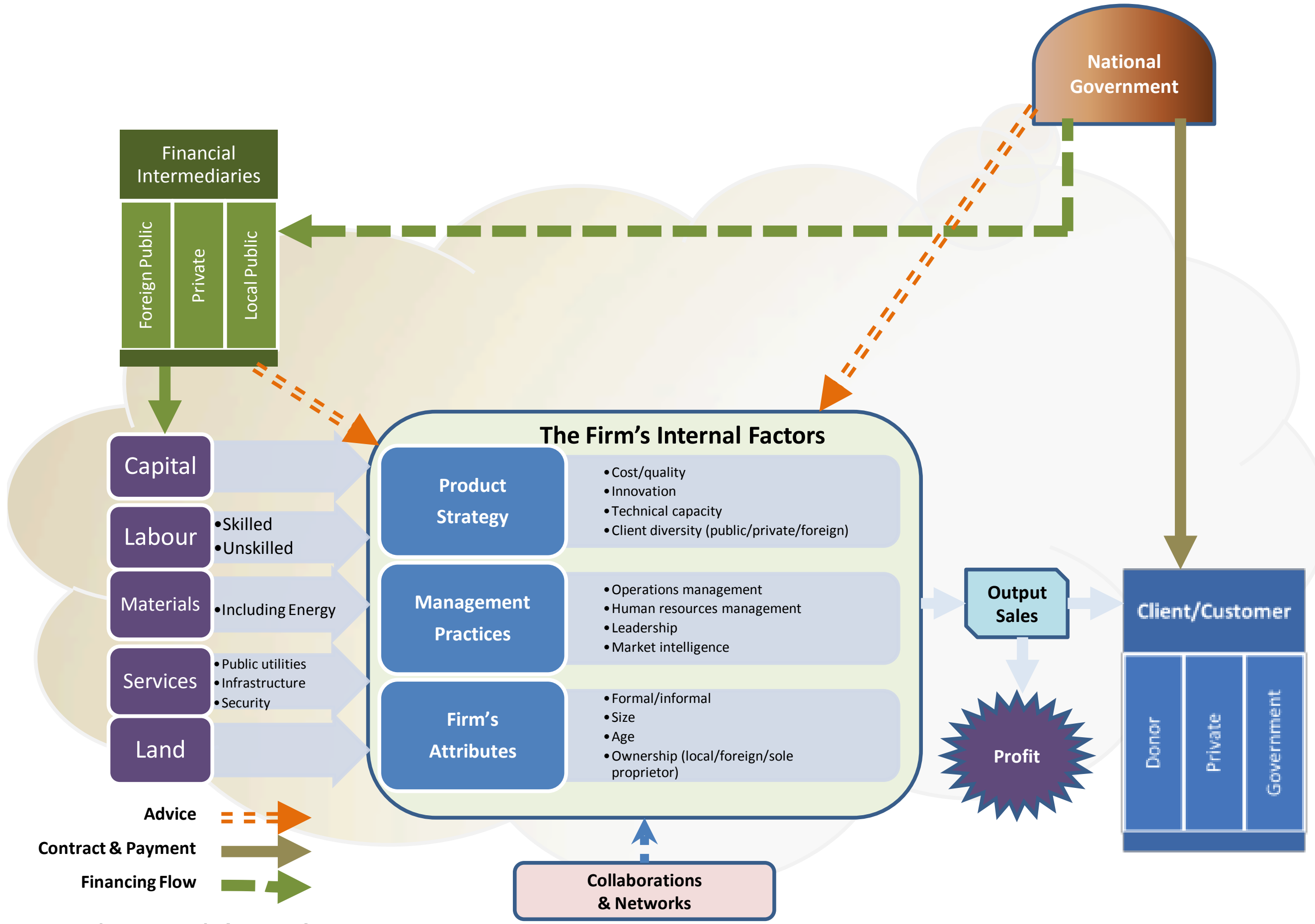
L_{it} = labor of firm i in period t

M_{it} = materials used by $firm\ i\ in\ period\ t$

TFP_{it} = total factor productivity of firm i in period t

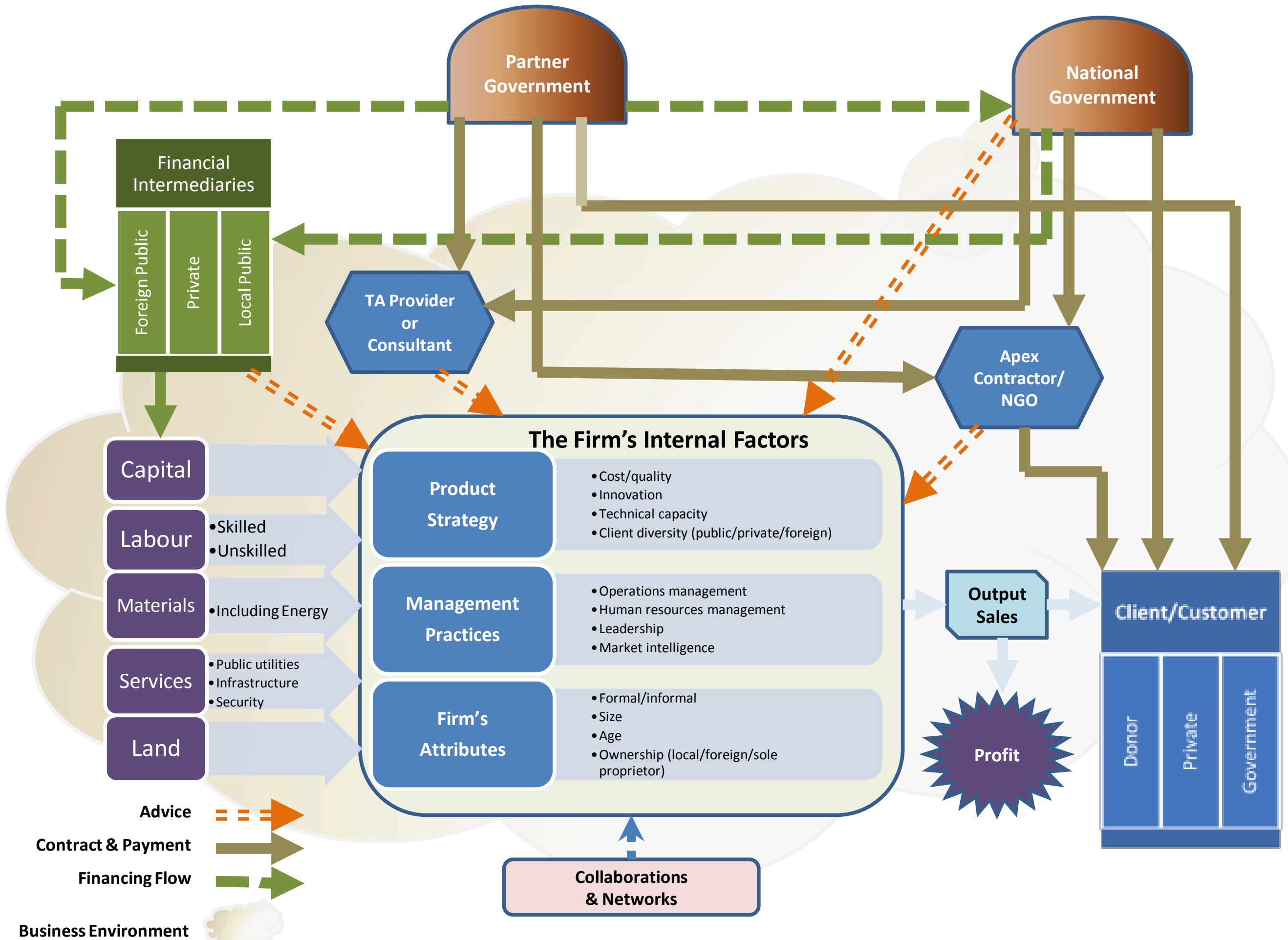
- We used results from the literature that further broke down TFP into components such as quality of management and then we assessed how localised aid might influence them

The private firm in its environment



Adapted from Bewley et al (2010)

Foreign aid and the private firm



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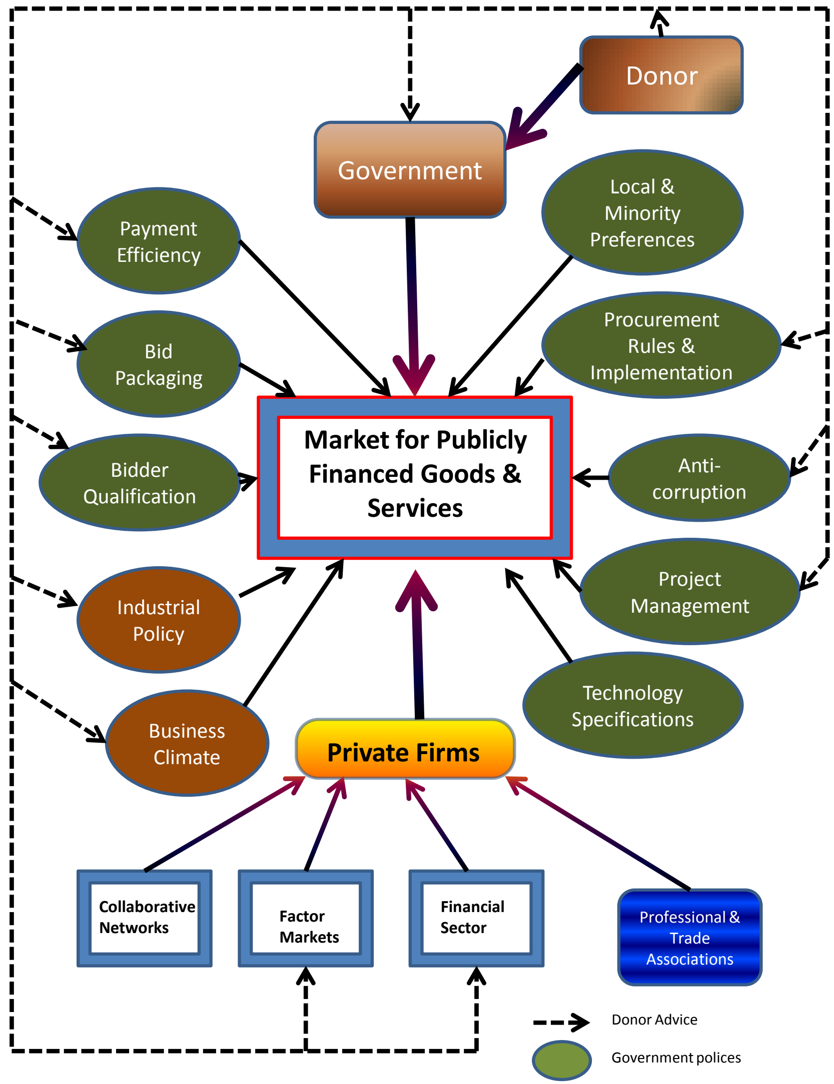
Localised aid influences private firms through the market for publicly financed goods & services



How can foreign partners strengthen the local private sector?

- Make strengthening the local private sector an explicit objective when it is involved in donor financed activities.
  - Take a “whole of market approach;”
  - Look at incentive in the process for awarding & managing contracts;
  - Promote competition and enable local and indigenous firms to compete.
  - Measure impact of aid on local private sector.
  - Manage economic rents & anti-corruption to balance open access to PUGS market with development of local private sector.

A more nuanced approach to economic rents & corruption

- All governments create & distribute rents to some extent and these can serve political objectives.
- Neo-patrimonal systems tolerate ("licence") corruption & allocate rents to maintain their clients. Public procurement may overlap this system.
- Rents & corruption can be associated with successful economic development ("growth enhancing") or associated with growth retarding, extractive regimes.
- Positive rents include information rents & rents which enhance technological innovation and learning.
- Transition from a limited to open access order can take decades.
- Challenge for international partners to understand politics of rents & corruption and intervene so as to create incentives to reduce those that are most adverse to development.

The Civil Society Organizations (CSO) Sector

Localising aid and civil society organizations. Some findings (1):

- CSOs are strengthened when their use & scrutiny is promoted, weakened when they are neglected or subverted.
- Apex contractors/INGOs may save costs, but not certain whether project effectiveness improves, or whether local CSOs are strengthened.
- Whether localising aid strengthens CSOs depends on whether this is a donor objective, whether recipient CSOs are legitimate and represent citizens, accountability & reporting incentives, length & flexibility of project. Local CSOs may struggle to meet donor requirements and be squeezed out by INGOs.

Localising aid and civil society organizations. Some findings (2):

- More core funding would strengthen CSOs, but donors have been reluctant to finance overhead costs.
- Donors working outside government could do more to share information, plan effectively and complement state-led programmes.
- Donors are also not providing incentives to their partners to support systems development, particularly in health.

Some additional lessons for donors

- Concerns about corruption & waste are valid, but are insufficient reasons not to localise aid, which can be managed well.
- Even in countries which have low international corruption scores, islands of excellence can be found, and theft of public money may not be the most significant form of corruption.
- Non-localised aid may complement localised aid as well as undermine it.
- Short vs Long Term tradeoffs are important with localised aid, e.g. short term results vs long term capacity and sustainability.
- Localised aid complicates the donors' results agenda.
- Donors need to recognize the political aspects and complicated impacts of their interventions.

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