The Changing Roles of Multilateral and Bilateral Foreign Assistance

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CHAPTER 13 JOHN W. MELLOR AND WILLIAM A. MASTERS

The Changing Roles of Multilateral and Bilateral Foreign Assistance

In the four decades since Harry Truman's Point Four program was announced,[1] there have been five major trends in foreign assistance: (1) steady, moderately rapid growth in all forms of foreign aid, accompanied by large but highly unstable private flows to and from developing countries and considerable instability in aggregate flows to individual developing countries; (2) increasingly large flows through multilateral agencies, including private portfolio investment in development banks; (3) an increasing number of donors and aid channels, with a change from one dominant donor (the United States) to many donors, and a switch from a dominant bilateral channel (the U.S. Agency for International Development, or USAID) to a dominant multilateral one (the World Bank); (4) large changes in aid allocations among countries, including reversals in the direction of some flows; and (5) explosive growth in explicit knowledge, documentation, and experience in development processes, accompanied by continued and perhaps increasing dissatisfaction with the pace of development and the efficiency of foreign assistance.

As the number of foreign assistance agencies and donors has increased, strong comparative advantages among them have been revealed.[2] The

We are grateful to Uma Lele and Ijaz Nabi for their detailed comments and substantive suggestions as well as to the Talloires conference participants.

differences between aid channels have given each one relative advantages in mobilizing resources from particular constituencies, in directing aid to particular countries, and in carrying out particular aid activities. All agencies have, to some degree, specialized to capture the benefits from these relative advantages.

Unfortunately, much of the potential benefit from larger aid flows and greater diversity among donors has been lost, principally because of weak leadership in the aid community, which has encouraged few shared objectives and little common understanding of development processes. Consequently, aid agencies have been periodically overrun by fads in development thinking. These fads make aid flows more unstable in terms of both country allocations and functional activities, and they keep diverse agencies from exploiting their various comparative advantages. At the same time, fads distract recipient countries from making the best use of their resources, and the less the national capacity of a recipient country to formulate its own long-run development strategy, the worse the impact of this problem.

Fashionable ideas are typically true in their original context, but their success in a particular place and time propels them too far, too fast, grossly oversimplifying the complex processes of development. For example, the growth successes of the 1960s did call for efforts at direct poverty alleviation, and poor growth in the late 1970s did require more emphasis on open markets and greater economic efficiency, but both of these responses were only partial solutions. Similarly, deterioration of the global environment today cries out for policy actions in all countries, but this too may be taken too far.[3] In each case, excessive and simplistic concentration on a popular idea brings confusion, duplication of effort, and wholesale reversals in institutions and ways of thinking. These problems are often attributed to a lack of coordination, and formal cooperation arrangements are suggested as a solution. But formal links are no substitute for genuine consensus. The critical task is providing the leadership to build a consensus through defining the common goals of the aid community and delineating effective strategies to deal with the diverse problems of extreme poverty, market structure, environmental deterioration, and many others. Such leadership was provided by the United States in the 1950s and by the U.S. and the World Bank in the 1960s, albeit with a heavy hand. The case studies in this volume clearly show the role that this leadership played; in India, for example, the Bell mission in 1964 generated an overall aid strategy, a sectoral strategy, and policy guidelines that provided the basis for dialogue and forward movement of policy that was helpful to consensus even while bringing out contentious issues.

Since the 1960s, the increased dispersion of bilateral aid and the rise of multilateral agencies have created a vacuum of leadership. It is doubtful if any organization but the World Bank, which is important to all countries, has the strength and legitimacy to sustain a major leadership role. However, neither the World Bank nor any other donor has prepared itself to play that role. To do so would require a deep understanding of the processes of development; capacity to develop that knowledge into a coherent strategic vision; ability to help tune this strategy to specific, widely varying circumstances; and an ability to build a consensus not only among donors, but between donors and developing countries. Underlying such leadership must be a sense of humility gained from the knowledge of how dynamic, varied, complex, and uncertain are the processes of development.

Some suggestions for a consensus-building strategy are given in the final section of this chapter. With a broad consensus, the dispersion and diversity of donors could be turned into an asset, in the same way that resource diversity is an asset in the play of comparative advantage in trade. The diversity among agencies will become clear in the next section of this chapter, a brief review of the history of bilateral and multilateral resource flows. Then we will explore the theory and practice of comparative advantage in aid, survey the effects of faddism, and outline a strategy for aid around which a consensus could be built.

Resource Flows through Bilateral and Multilateral Institutions

Aid versus nonconcessional flows. To situate aid in the context of the market for capital flows between developed and developing countries, Figures

FIGURE 13.1 Aggregate Flows from DAC Countries to LDCs and Multilateral Agencies, 1960–85

a. Nominal flows

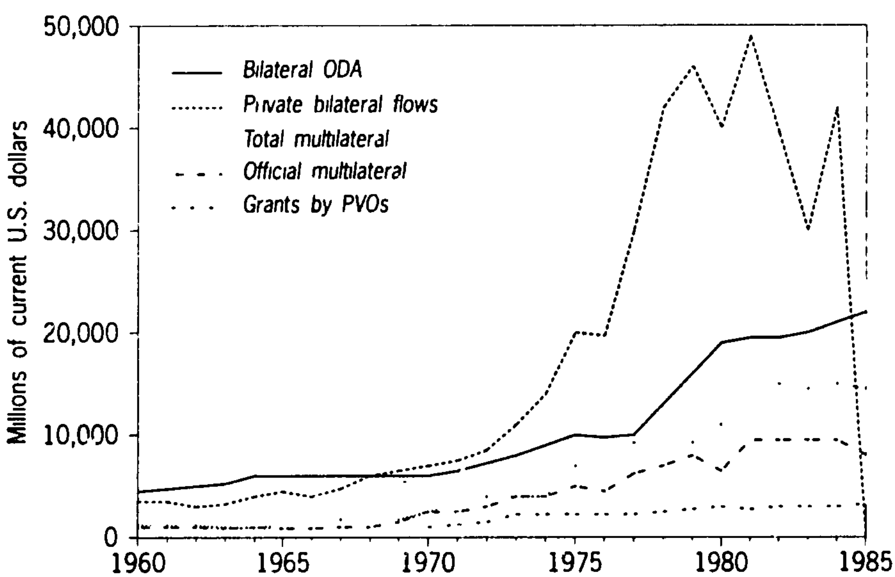

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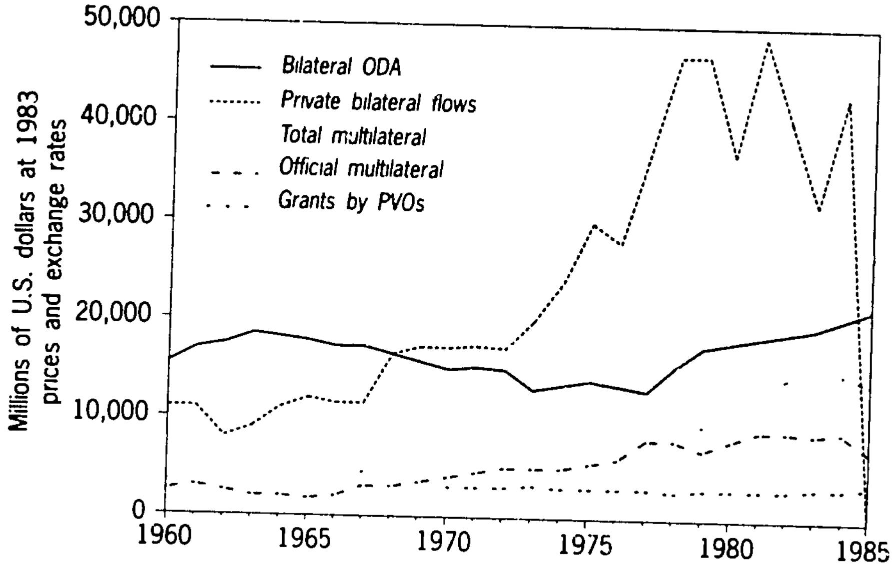
FIGURE 13.1 (continued)

b. Real flows



NOTE Private bilateral flows include bilateral portfolio investment, direct foreign investment, and private export credits They do not include private portfolio investment in multilateral development banks Total multilateral includes official contributions to all multilateral agencies, plus private portfolio investment in multilateral development banks Grants by PVOs includes only privately raised funds Official contributions to PVOs are included as bilateral ODA Data are from 1970 onward only

SOURCES for Figures 13 1–13 4 *Development Cooperation 1969*, p 38 (for 1960–61); *Development Cooperation 1973*, p 42 (for 1962–69), *Development Cooperation 1974*, pp 232–33 (for 1970–73) and pp 254–55 (for U S data, 1963–69), *Development Cooperation 1977*, pp 187–88 (for 1974–76), *Development Cooperation 1980*, pp 199–200 (for 1977), *Development Cooperation 1982*, p 219 (for 1978–81), *Development Cooperation 1986*, pp 283–84 (for 1982–85) GNP deflators are from *Development Cooperation 1985*, p 336 (for 1960–84), and *Development Cooperation 1986*, p 287 (for 1985)

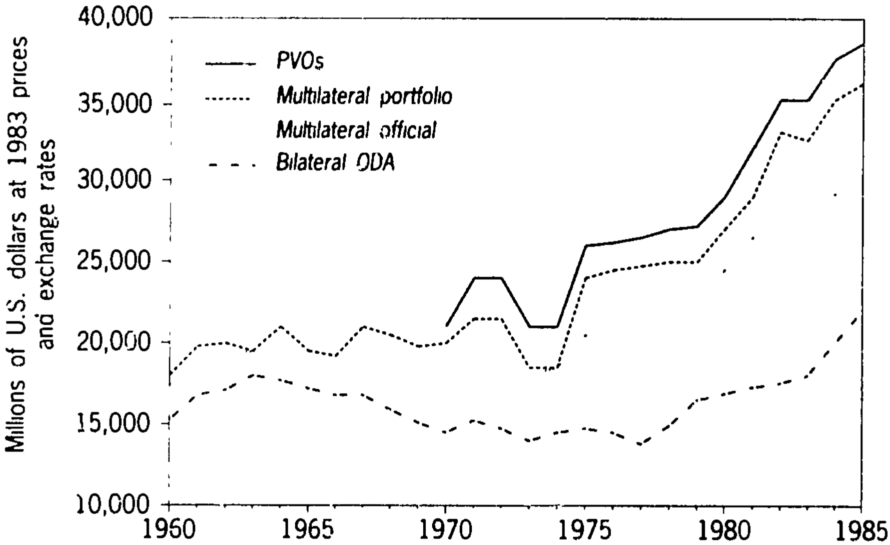
13.1a and 13.1b chart aggregate flows from all members of the Organization for Economic Cooperation and Development/Development Assistance Committee (OECD/DAC)[4] to all developing countries, in both nominal and real terms. Although private flows[5] far surpassed aid during the decade between 1975 and 1985, they have now fallen back to their level of the 1960s, and in general have been characterized by extreme instability.

The balance between bilateral and multilateral flows. When modern aid agencies were established, they were almost exclusively bilateral. Figure 13.2a shows, in real terms, how the balance between the various channels for aid from DAC countries to developing countries has shifted since then. Figure 13.2b shows these aid flows as percentages of total resources net (TRN), which includes private flows.

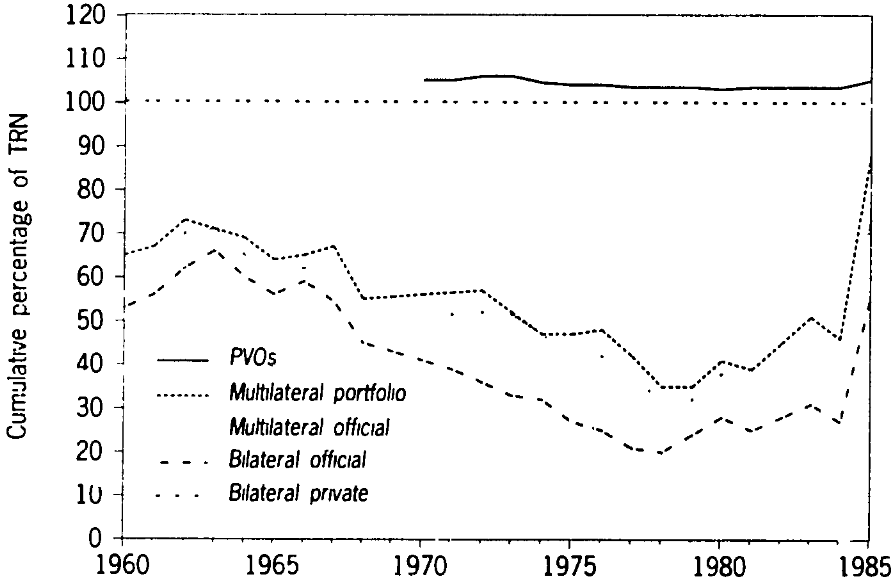
For the decade beginning in 1963, all nominal growth in official aid was channeled through multilateral agencies; in constant dollars and as a proportion of all flows, bilateral programs fell off dramatically. But since the

FIGURE 13.2 Composition of Aid and Total Resource Flows from DAC Countries to LDCs and Multilateral Agencies, 1960–85

a. Composition of aid flows



b. Composition of total resource flows



SOURCE See Figure 13 1

mid-1970s, bilateral programs have expanded again, without appreciably cutting into official contributions to multilaterals or into the private fund-raising activities of private voluntary organizations (PVOs). Some of this expansion consisted of security-related assistance from the United States, but most of it was development aid from other donors.

In the late 1960s and again after 1974, another major source of additional funds has been private portfolio investment in multilateral banks. By 1985, these flows had grown to over $6 billion per year, accounting for almost half of multilateral funding, and 7.5 percent of total resource flows to developing countries and multilaterals. It was largely additional to what developing countries could borrow individually and was obtained on much better terms. And most important today, private investment in multilaterals is more stable than other private lending. In 1985 multilateral portfolio investment continued to grow (in nominal terms), while other private flows dried up and net DAC portfolio investment in developing countries was a negative $4.7 billion.

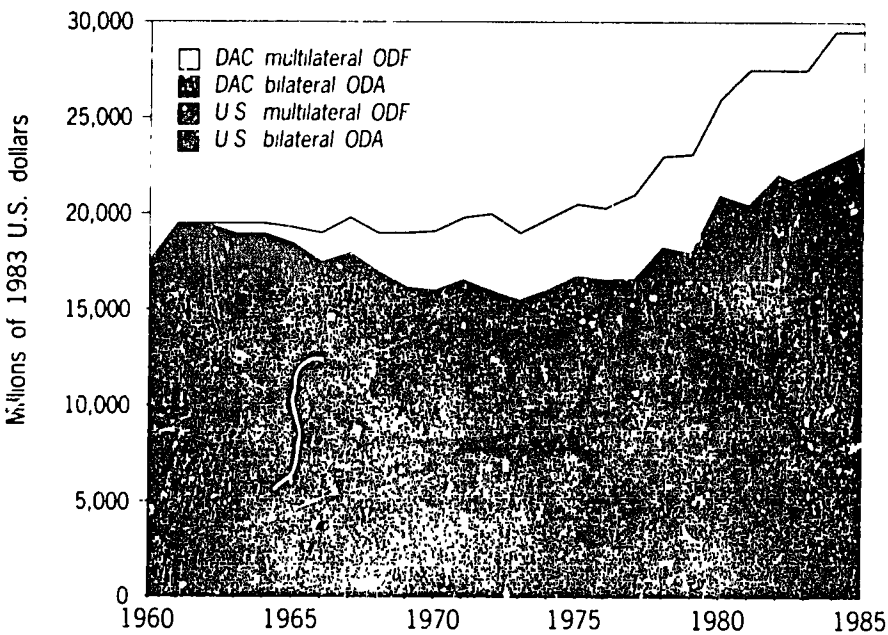
The changing importance of the United States. The share of aid funds contributed by the United States has declined almost continuously since the mid-1960s, from about one-half to about one-third of official development finance (ODF).[6] This is shown in Figures 13.3a and 13.3b in constant dollar terms and as percentages of official DAC bilateral aid, contributions to multilaterals, and combined total ODF. Most non-U.S. flows come from five other major donors (Canada, France, Germany, Japan, and the United Kingdom), but there are also a large number of small individual donors, including non-OECD countries.

It is notable that the United States, relative to other donors, generally provides a smaller proportion of total DAC official development assistance (ODA) through multilaterals than through bilaterals. This was briefly reversed in the late 1970s, when there had been a long increase in the U.S. share of multilateral funding, but that increase was completely erased in the 1980s. U.S. contributions to multilaterals as a share of U.S. ODA have increased from below the DAC average (7.6 percent in 1960–61 and 11.4 percent in 1970–71) to above it (34 percent in 1980–81) and then declined far below it again (19 percent in 1984–85).

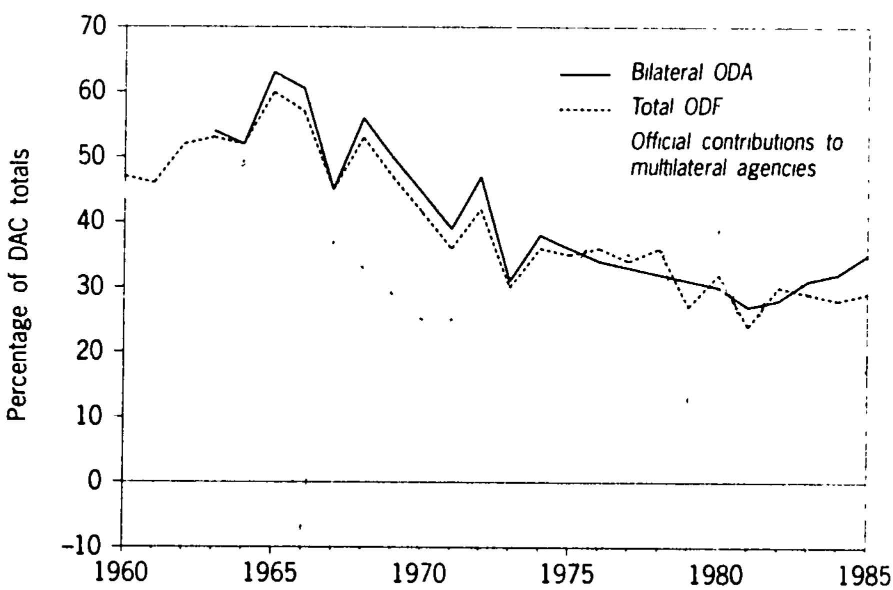
The U.S. role in private flows has also changed considerably over the 1970–85 period, as shown in Figures 13.4a, 13.4b, and 13.4c. While private voluntary flows from the United States have been fairly constant, other countries' PVOs have recently expanded (Figure 13.4a). Consequently, the U.S. share of PVO grants has fallen, from over 60 percent in the early 1970s to just over 50 percent in 1985. The U.S. share of private investment in multilaterals (Figure 13.4b) and in developing countries (Figure 13.4c) remains smaller than this, and is quite unstable.

FIGURE 13.3 U.S. Contributions to ODF and ODA, 1960–85

a. Cumulative official contributions to bilateral and multilateral agencies from the United States and from other DAC countries



b. Official U.S. contributions to bilateral and multilateral agencies and to total official development finance

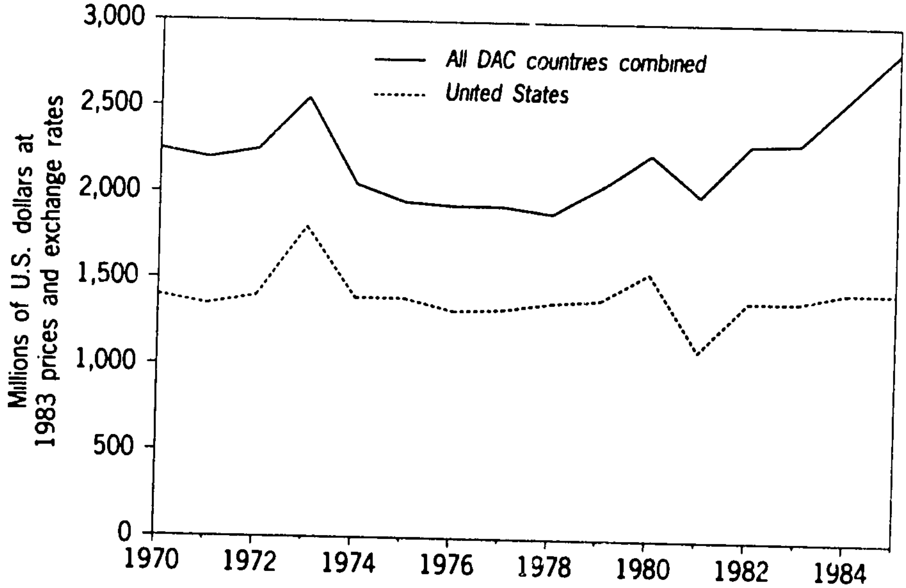


NOTE Multilateral official development finance (ODF) includes all official development-oriented funds, both concessional and nonconcessional

SOURCE See Figure 13 1

FIGURE 13.4 Private Flows from DAC Countries and the United States, 1970–85

a. Grants by private voluntary agencies



b. Private portfolio investment in multilateral agencies

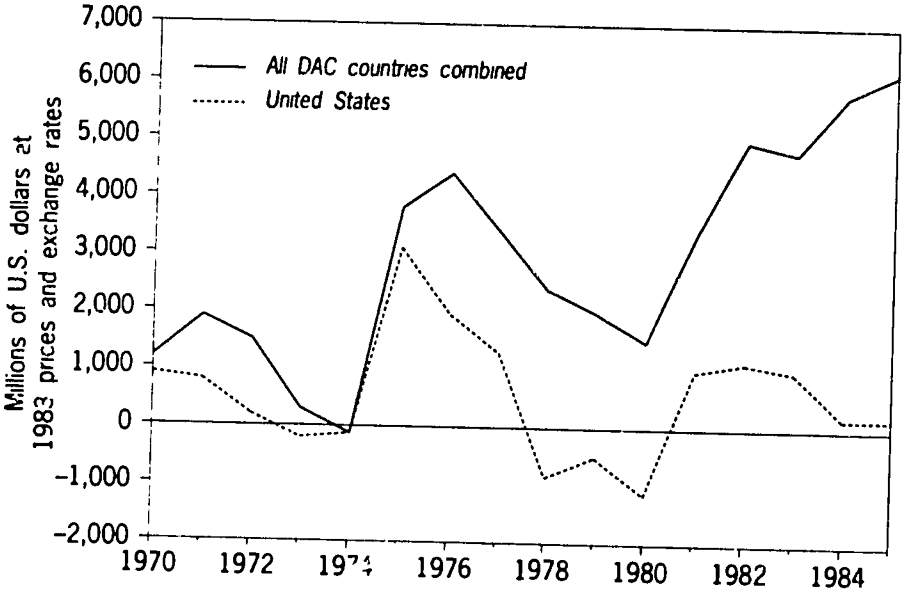


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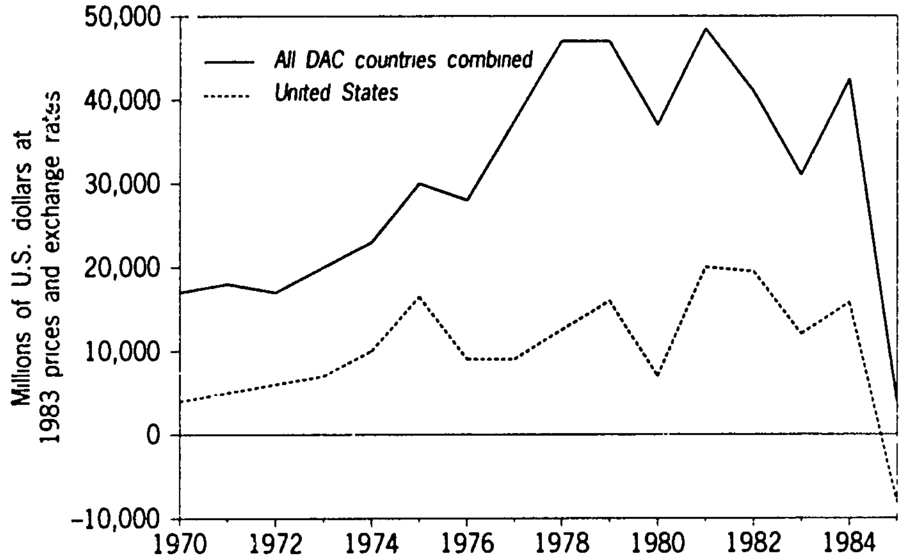
FIGURE 13.4 (continued)

c. Private flows not including investment in multilateral agencies



SOURCE See Figure 13 1

The proliferation of multilaterals. The problems of aid coordination engendered by the growth in aid flows and in the number of donors are compounded by the rising number of multilateral agencies. In 1960, only seven major multilateral aid channels were operating;[7] by 1975 there were eight more.[8] The ages and relative sizes of the largest agencies are listed in Table 13.1.

The changing geographic concentration of aid flows. The relative decline of the U.S. share in aid flows has become more marked in recent years because of the increased concentration of U.S. aid on a few major recipients. In 1960–61 the top two recipients of U.S. ODA were India and Brazil; together they received 19.3 percent of all U.S. bilateral aid. In 1970–71 the top two were India and Vietnam; they received 27.5 percent. By 1980–81 the top two were Israel and Egypt, who received 34.6 percent; by 1983–84, their share had increased to 37 percent. This increasing concentration was largely due to the growing use of U.S. foreign aid to pursue narrowly defined military and national security interests, combined with shifts in the definition of those interests.

Other donors also concentrate their bilateral assistance, but to a lesser degree than does the United States. Table 13.2 illustrates the geographic concentrations of most major donors and agencies. Clearly, each bilateral donor allocates aid differently, and in the aggregate, bilateral aid is highly

TABLE 13.1 Age and Net Disbursements of Major Multilateral Agencies, 1964–85 (selected two-year averages)

	Year established/year of first commitment	Millions of current U.S. dollars					Percentage of multilateral total				
		1964–65	1970–71	1975–76	1980–81	1984–85	1964–65	1970–71	1975–76	1980–81	1984–85
World Bank total		474	872	3,154	5,615	8,029	56.4	43.5	48.7	42.7	49.8
IBRD	1947/48	279	585	1,776	3,482	5,372	33.2	29.2	27.4	26.5	33.3
IDA	1960/61	184	225	1,198	1,731	2,546	21.9	11.2	18.5	13.2	15.8
IFC	1956/57	11	62	180	403	111	1.3	3.1	2.8	3.1	0.7
United Nations total		221	529	1,354	2,668	2,908	26.3	26.4	20.9	20.3	18.0
WFP	1962		125	350	541	729		6.2	5.4	4.1	4.5
UNDP	1965		219	378	725	616		10.9	5.8	5.5	3.8
UNHCR	1949		8	81	451	408		0.4	1.2	3.4	2.5
UNRWA	1946		45	99	164	191		2.2	1.5	1.2	1.2
UNICEF	1949		47	114	231	262		2.3	1.8	1.8	1.6
UNFPA	1967				140	123				1.1	0.3
Other UN			85	332	418	579		4.2	5.1	3.2	3.6
Regionals total			359	914	1,670	3,007		17.9	14.1	12.7	18.6
AfDB/AfDF	1964/67 (AfDF 1972)		4	51	177	333		0.2	0.8	1.3	2.1
ADB/ADF	1966/68 (ADF 1974)		32	317	507	805		1.6	4.9	3.9	5.0
IDB	1959/61	44	323	546	987	1,869	5.2	16.1	8.4	7.5	11.6
Special constituency agencies											
EDF/EIB	1957	104	242	653	1,500	1,406	12.4	12.1	10.1	11.4	8.7
Arab/OPEC agencies	various			384	532	377			5.9	4.0	2.3
IFAD	1977/78				65	220				0.5	1.4
Others			1	23	1,091	179		0.0	0.4	8.3	1.1
Total multilateral		841	2,003	6,482	13,140	16,126	100.0	100.0	100.0	100.0	100.0

NOTE Blanks indicate unavailable data

SOURCE Flows calculated from OECD, *Development Cooperation 1986*, p 239; *Development Cooperation 1977*, p. 197, and *Development Cooperation 1974*, p 261 Dates for the establishment of and the first commitment from each agency are from *Development Cooperation 1980*, p 138

dispersed. However, some of the recipients favored by large donors are relatively small and rich, and they almost certainly receive aid flows far in excess of their absorptive capacity or their relative need. These flows are often targeted by critics as wasteful and inequitable. In contrast, while multilaterals also concentrate their aid on certain countries, their focus is on larger, poorer countries (see Table 13.4 for per capita figures).

To examine changes in geographic concentration over time, it is most convenient to use concentration ratios.[9] In Table 13.3 we show the percentage of the nine major donors' geographically allocated bilateral ODA going to the top one, two, and four bilateral recipients. It is particularly important that all donors, except France and the United States, have been tending toward

TABLE 13.2 Geographic Concentration of ODA, 1980–81 Average

Percentage of geographically allocated bilateral ODA, with total bilateral ODA in parentheses			
Australia (US$0.5 billion)		Netherlands (US$1.1 billion)	
Papua New Guinea	57 6	India	13 9
Indonesia	9 4	Surinam	9 7
Bangladesh	4.0	Indonesia	7 5
Philippines	2.6	Neth. Antilles	7.4
Pakistan	2.4	Tanzania	7.3
Canada (US$0.5 billion)		Sweden (US$0.5 billion)	
Bangladesh	11.2	Vietnam	15.6
India	9.4	Tanzania	14.8
Pakistan	8.3	India	11.1
Sri Lanka	6.1	Mozambique	6.5
Tanzania	4.6	Zambia	5.7
France (US$3.4 billion)		United Kingdom (US$1.3 billion)	
Reunion (DOM)	16.6	India	20 6
Martinique (DOM)	14.9	Bangladesh	8.4
New Caledonia (TOM)	5.4	Tanzania	4.9
Fr. Polynesia (TOM)	4.7	Sri Lanka	4.9
Morocco	4.2	Kenya	4.7
Germany (US$2.9 billion)		United States (US$4.1 billion)	
Turkey	12.5	Egypt	21 4
Bangladesh	10.1	Israel	19.4
India	6.0	India	5.6
Sudan	4.8	Turkey	4.8
Indonesia	4.7	Bangladesh	3 6
Japan (US$1.8 billion)		Total DAC (US$18.2 billion)	
Indonesia	17.0	Egypt	6.7
Korea, Rep.	10.5	India	6.3
Thailand	8.9	Bangladesh	5.4
Bangladesh	7 5	Indonesia	5.4
Philippines	7.1	Israel	4.8

Percentage of total geographically allocated ODA, with total ODA in parentheses			
IDA (US$1.8 billion)		Total multilateral (US$7 billion)[a]	
India	39 2	India	18.6
Bangladesh	8 9	Pakistan	5.5
Pakistan	4.7	Bangladesh	5.0
Egypt	3.6	China	3.4
Tanzania	3.2	Egypt	2.8
WFP (US$0.5 billion)		OPEC (US$5.4 billion)	
Pakistan	8.9	Syria	23 8
Kampuchea	7.3	Jordan	17.4
India	6.5	Morocco	6.8
Somalia	5.5	Lebanon	5.3
Egypt	5.4	Yemen	5.2

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TABLE 13.2 (continued)

UNDP (US$0.6 billion)		CMEA (US$2.6 billion)	
India	4.1	Vietnam	34.8
Bangladesh	3.5	Cuba	22.8
Sudan	3.0	Afghanistan	10.5
Ethiopia	2.9	Kampuchea	5.3
Indonesia	2.4	Lao PDR	3.5
All sources combined (US$33.1 billion)			
India	7.8		
Egypt	4.4		
Syria	4.4		
Bangladesh	4.3		
Vietnam	3.4		

a. ODA contributions to multilateral agencies from DAC member countries
SOURCE Calculated from *Development Cooperation 1983*, pp. 208–213.

less geographic concentration over time. This trend seems to be related to program size: smaller programs tend to be more concentrated, and to become less so as they grow. As exceptions to this rule, France has maintained a roughly constant degree of concentration on a few overseas territories, while the United States has actually increased concentration in its shift to security-based lending. A notable feature of geographic concentration is that it

TABLE 13.3 Concentration Ratios for Major DAC Donors, 1960–81 (selected two-year averages)

	Percentage of geographically allocated bilateral ODA									Percentage of total ODA to multilateral agencies		
	Top recipient			Top 2 recipients			Top 4 recipients					
	60–61	70–71	80–81	60–61	70–71	80–81	60–61	70–71	80–81	60–61	70–71	80–81
Australia		75.8	57.6		85.1	67.0		89.8	73.6		10.9	22.2
Canada	54.0	42.0	11.2	83.5	58.0	20.6		64.6	35.0	24.9	22.6	45.7
France	94.2	13.3	16.6		25.2	31.5		42.7	41.6	7.3	10.2	16.3
Germany	34.1	14.6	12.5	64.2	24.6	22.6	91.7	38.4	33.4	22.6	22.0	27.5
Japan	26.6	26.9	17.0	48.2	50.2	27.5	83.1	71.4	43.9	18.5	14.9	32.3
Netherlands	74.9	33.3	13.9	96.4	51.2	23.6		77.9	38.5	36.3	25.3	25.6
Sweden	38.9	18.6	15.6	66.0	36.2	30.4		66.8	48.0	83.8	52.6	35.1
United Kingdom	17.3	27.8	20.6	33.8	33.2	29.0	51.7	42.9	38.8	15.2	17.9	34.6
United States	11.6	18.0	21.4	20.6	31.6	40.8	34.8	48.1	51.2	7.6	11.4	34.0
Simple average of 9 largest DAC donors	44.0	30.0	20.7	59.0	43.6	32.6	63.4	58.5	44.9	27.0	20.9	30.4
All DAC countries combined	15.0	14.8	6.7	24.7	24.4	8.9	36.9	36.7	16.3	11.0	12.5	31.3

NOTE Blanks indicate unavailable data.
SOURCE Calculated from *Development Cooperation 1985*, pp. 123, 306–314; *Development Cooperation 1983*, pp 208–213

increases the vulnerability of aid recipients to sudden changes in the objectives and perceptions of their principal donors. This is particularly evident among recipients of U.S. aid, which is large, concentrated, and unstable. Virtually all of the country studies in this volume call attention to the seriousness of this problem.

The changing poverty emphases of aid flows. In the early 1970s, both bilateral and multilateral donors dramatically increased the share of funds going to the least developed countries (LLDCs).[10] This occurred during a period of rapidly growing total aid, resulting in very rapid growth of LLDC receipts, as shown in Figures 13.5a, 13.5b, and 13.5c.

DAC bilateral aid flows shifted *away* from the LLDCs in the late 1970s, however, and then shifted back toward them a few years later. Funding of LLDCs has been heavily influenced by the 1970s' emphasis on helping the poorest of the poor (reinforced by famines in Asia and Africa) and by the 1980s' emphasis on structural adjustment in distorted economies (reinforced by famines in the Sahel). Unfortunately, these bursts of funding were probably far in excess of the LLDCs' real absorptive capacity.

Multilateral aid to LLDCs, however, has been growing in a somewhat more stable fashion. This is particularly important for those countries with high ratios of aid to gross national product (GNP), for whom the predictability of aid is essential to its productive investment

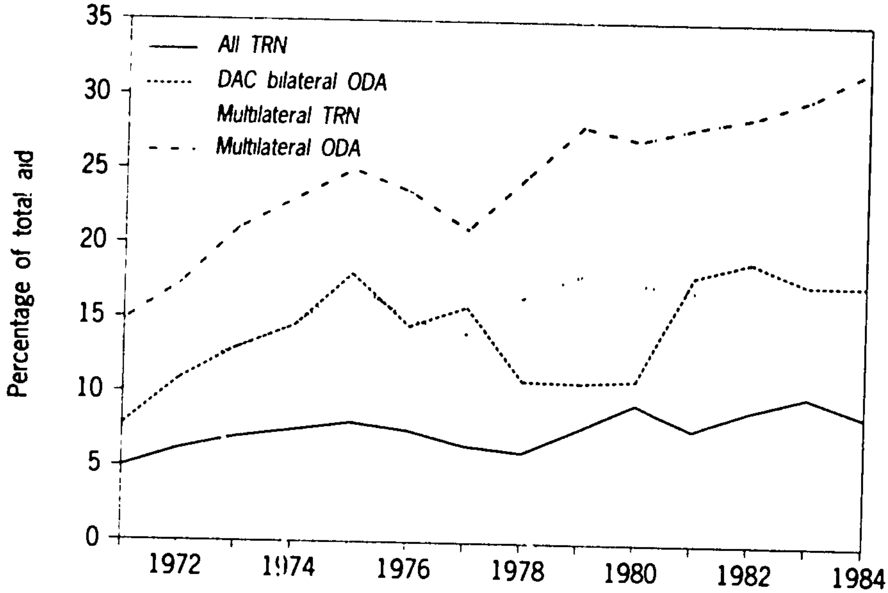
These data clearly show the special importance of the multilateral agencies in providing aid to the poorest countries. Very poor countries may be of little strategic or political importance to bilateral donors, but they have great economic needs and potential for development.

The changing regional emphases of aid flows. Table 13.4 shows bilateral and multilateral aid allocations by region and selected country. It is notable that bilateral allocations have changed considerably over time, recently shifting toward the Middle East, North Africa, and sub-Saharan Africa at the expense of Asia. In contrast, multilaterals have maintained a more consistent pattern, with aid generally targeted to the very poor countries of South Asia and Africa. These trends are closely related to those discussed in the section above.

Differences in the geographic allocations of bilaterals and multilaterals are particularly evident in their per capita levels of ODA. The dramatic extremes and apparent misallocations allowed by bilaterals are rarely seen among multilaterals. In 1983–84, bilaterals gave over five times their world average ODA per capita to countries in the Middle East, and over three times the average to North Africa, largely reflecting U.S. support for Israel and Egypt. This left relatively little bilateral aid for poorer, more populous countries, particularly in South Asia, where over half of the world's poorest people live, and where bilaterals actually gave less per capita than multilaterals.

FIGURE 13.5 Flows to Least Developed Countries (LLDCs), 1971–84

a. Percentage of total aid allocated to LLDCs



b. Real aid flows to LLDCs

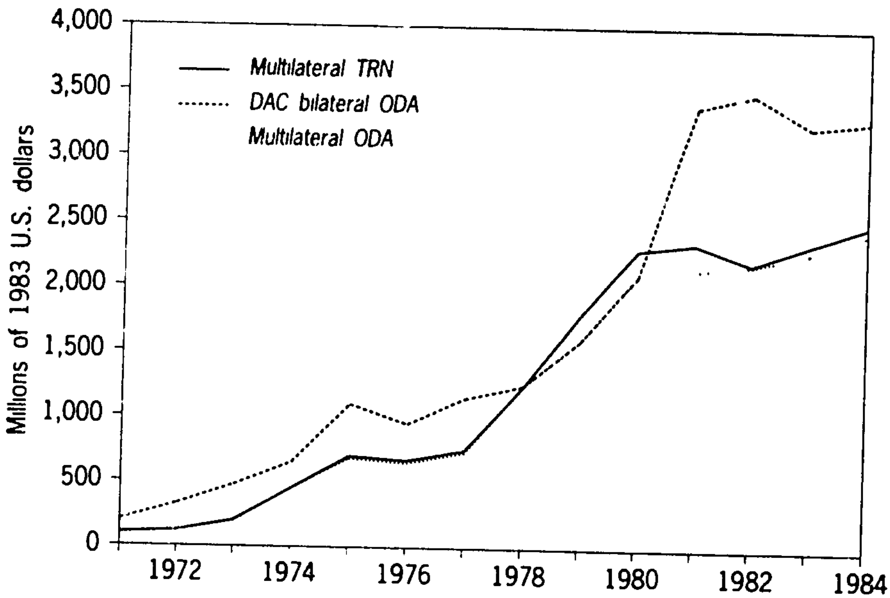


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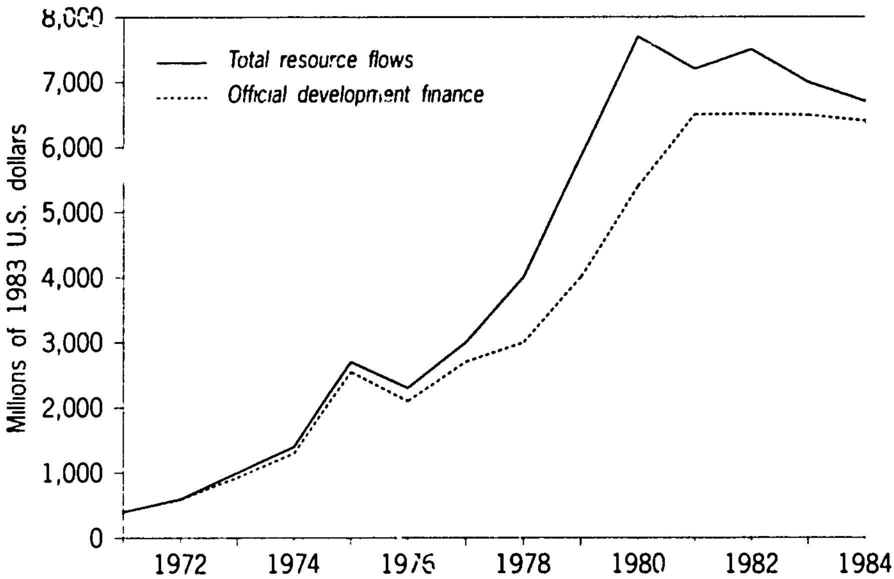
FIGURE 13.5 (continued)

c. Real official development finance and total resource flows to LLDCs



NOTE Deflated by DAC GNP deflators
SOURCE Calculated from *Geographical Distribution of Financial Flows to Developing Countries*, 1978 (for 1971-77), 1981 (for 1977-80), and 1986 (for 1981-84) and *Development Cooperation 1985*

Comparative Advantage in Theory

To explain the facts and trends outlined above, it is appropriate to turn to the economics and political science literature on foreign aid. In this section we briefly summarize a few themes from this literature and then use those insights to compare the abilities of donors and agencies to raise and spend money.

The quantity of aid. Support for aid typically follows patterns of international trade and investment. These links generate donor country constituencies for aid (people pursuing humanitarian, religious, commercial, financial, industrial, military, political, and ideological interests) and help create the skills and institutions necessary for its provision.[11] The various constituencies for aid receive substantial real benefits from aid programs, but there are often significant spillovers between constituencies. For example, in the United States, food aid serves both humanitarian and agricultural interests. Support for aid is therefore typically in the form of coalitions of more or less diffuse interest groups. Some groups do provide foreign aid independently of their governments and have done so for centuries. These represent only a

TABLE 13.4 Regional Distribution of Aid Flows, 1970–84 (selected two-year averages)

	Percentage of flows to all developing countries						Value of aid flows (current U.S. dollars)					
	Bilateral ODA			Multilateral ODA			Bilateral ODA per capita			Multilateral ODA per capita		
	1970–71	1980–81	1983–84	1970–71	1980–81	1983–84	1970–71	1980–81	1983–84	1970–71	1980–81	1983[–84]
Sub-Saharan Africa	17.6	21.0	23.8	36.3	35.4	36.5	3.93	14.80	13.08	1.23	7.69	6.9
Americas	13.9	8.5	11.8	11.1	11.5	11.1	2.98	6.09	6.75	0.36	2.54	2.2
Middle East	2.2	18.4	16.1	7.5	5.3	3.4	2.03	50.69	34.19	1.05	4.55	2.5
Israel	1.1	3.3	5.9	0.0	0.0	0.0	22.30	214.56	311.71	0.03	0.06	0.0
North Africa	5.3	9.5	8.9	7.0	4.1	4.1	4.95	26.89	19.95	0.99	3.61	3.16
Egypt	0.4	4.5	6.3	2.4	2.6	2.7	0.65	26.92	30.10	0.65	4.75	4.50
South Asia	21.9	10.8	9.6	19.2	29.3	30.1	1.77	2.92	2.08	0.24	2.46	2.25
India	13.2	2.9	2.5	11.9	16.4	14.0	1.45	1.08	0.75	0.20	1.87	1.43
Bangladesh	0.2	3.2	3.1	0.7	4.7	5.9	0.13	9.25	7.00	0.09	4.17	4.59
Pakistan	6.1	2.1	1.2	4.7	4.8	5.5	6.01	6.62	2.80	0.70	4.62	4.60
Far East Asia	25.2	8.0	10.1	7.6	10.7	7.2	1.56	1.48	1.53	0.07	0.61	0.37
China	0.0	0.0	2.4	0.0	3.0	2.5	0.00	0.00	0.52	0.00	0.24	0.19
Indonesia	8.2	3.3	2.7	3.1	1.6	1.5	4.05	[illegible].72	3.80	0.23	0.86	0.74
Total to all LDCs (millions of current U.S. dollars)	6,064	25,456	22,212	921	7,858	7,672	2.20	7.69	6.19	0.33	2.37	2.14

SOURCE Calculated from *Geographic Distribution of Financial Flows to Developing Countries 1981/84* (for 1980–81 and 1983–84). For 1970–71, aid data are from *Development Cooperation 1973*, pp 202–205, and population data are from *United Nations Demographic Yearbook 1980*

fraction of aid flows, however, because it is generally more efficient to fund aid out of national tax receipts, like other national collective goods.

Of course, different interest groups benefit differently from each activity, and the degree to which various constituencies and coalitions should be tapped for any given aid enterprise is often the subject of intense debate. Feasible coalitions may or may not correspond to national boundaries, and organizations at the subnational and multinational level may have to be formed. Indeed, one of the earliest arguments for multilateral activity, and one of the most important, is that much foreign assistance has global public good qualities. It provides a shared infrastructure for international trade and finance, and helps maintain peace and political stability.[12]

After World War II, the United States dominated the world economy; it was the only country able to fund aid efforts and was arguably their most significant beneficiary. Initially, its greatest concern was the economic recovery of Europe. The United States took the lead in extending assistance in reconstruction, bilaterally through the Marshall Plan and multilaterally through the Bretton Woods institutions.[13]

Soon non-European countries came into greater prominence as potential recipients of economic assistance, and the United States developed the Point

Four program to extend assistance throughout the world. As the postwar economy grew, however, a concern with "burden-sharing" arose (Pincus 1965). Growth in other industrialized countries, increasing their stake in a politically stable and economically growing world, implied that they too were benefiting (or would benefit) from the effects of U.S. aid, and the United States sought to lead other donors into matching-funds arrangements, both formal and informal. In such arrangements, each donor pledges to fund some fixed fraction of a program's cost, usually through a multilateral agency. This helps overcome the public goods problem. In theory, such arrangements can even induce full Pareto efficiency when each donor's share of funding is equal to its share of the benefits.[14]

Throughout the 1960s and 1970s, the United States took the lead in establishing and strengthening multilaterals. In the initial stages, the United States dominated a number of these organizations, but as other countries grew economically, they took increasingly large shares of each funding cycle.

The recognition of public goods qualities in aid activities is not, however, always an argument for global multilateral activity. It is only an argument for matching donors with those agencies capable of providing the services they need, and vice versa. Many services belong at the national level, because they serve national interests. But other services might belong at the regional or subregional level. The variety of types of agencies that are needed is manifest in the variety of agencies that have arisen, as discussed below.

The quality of aid. A longstanding feature of most bilateral programs is that much of their aid is tied to procurement in the donor country. A newer but similar arrangement is to offer aid as subsidized credit for the purchase of donor country exports. Either form of tying substantially reduces the real value of aid to recipients (Bhagwati 1967) and may significantly distort their economies over the long run. In donor countries, aid tying helps preserve high-cost, noncompetitive industries and creates a policy-induced market failure similar to the effects of protectionism in trade.

Attempts to untie existing aid programs have made some progress, despite the political strength of the beneficiaries of aid tying.[15] One way to address this problem is to support multilateral agencies, whose aid is difficult to tie. Furthermore, the size and global contacts of multilaterals allow them to establish effective systems for international competitive bidding and recruitment.

The other side of this coin is that tied aid and export credits allow producers to subsidize their exports for economic and political reasons. This can be beneficial to aid recipients; subsidized goods represent real resources to be used in the development effort. If the donor provides such goods consistently, and the recipient buys no more than it really wants, this can be an effective form of assistance. (The chapter by T. N. Srinivasan in this volume provides valuable insight into this issue.)

Many aid activities offer important economies of scale. Some economies will be administrative or managerial in nature, but these are rapidly exhausted even among the smallest foreign aid agencies. Other economies will arise through overcoming market failures (Krueger 1981). Still others will be acquired through learning-by-doing and will depend on the depth and breadth of an agency's experience in a particular activity. Some of this knowledge can be shared with other agencies, resulting in familiar patterns of institutional leadership.

USAID, a bilateral agency, has been such a leader since its inception. Because of its size and broad responsibilities, it has had to develop systems for project and program design, appraisal, monitoring, and evaluation that can be widely applied and that take into account many aspects of development processes. In particular, a long and large concentration on agriculture has given USAID a leadership role in that area. While numerous valid criticisms of USAID's operations can and have been made—many from within USAID—it is unlikely that the development field would have progressed as rapidly as it has if the work of USAID had been diffused through a dozen different national agencies working in different languages and organizational styles.

USAID's learning process, however, has been limited by its close ties to the localized, short-term interests of the U.S. government. By the 1970s, the expansion of the World Bank Group had brought a broader and longer-term perspective and a somewhat more geopolitically disinterested player onto the development scene. Its comparative research is widely credited with a number of important advances in development thinking, and the intellectual impact of World Bank missions in developing countries has been noted in a number of the country studies in this volume. Research in the Bank and its application to the lending process are both driven and facilitated by the magnitude and extent of the Bank's responsibilities.

All economies of scale, of course, are eventually exhausted. Most activities do not need to be global, and some aid activities may be so distinct that they warrant functionally specialized agencies. This is clearly shown by the relative success of the geographically focused regional development banks and of the functionally specialized Consultative Group on International Agricultural Research (CGIAR).[16] In these cases, it has been effective to match an agency of appropriate size with a coalition of constituencies willing to fund its work.

Relatively small bilateral agencies and PVOs may well reach efficient sizes in some activities. This is most likely to happen if the activity is important in their home economy, because bilaterals have direct access to the individuals and institutions that support them, giving bilaterals in general a special advantage in helping to transfer and adapt national skills for institution-building efforts elsewhere. USAID, for example, offers good technical assistance to national agricultural research institutions largely because it can facilitate the transfer of skills accumulated in the U.S. land-grant college system.[17] Similarly, British and French assistance in export crop marketing or Scandinavian aid in forestry are successful because they match the institutional resource endowments of their countries with the needs of others. (For an in-depth analysis of these and other sources of comparative advantage, see the recent research of the World Bank's project Managing Agricultural Development in Africa [MADIA], comparing eight major agencies working in six countries.[18])

The adaptation and transfer of skills and institutions is further facilitated by strong cultural, linguistic, and economic ties between countries. These ties generate the necessary skills for effective communication across national boundaries and also ensure the long-term contact needed for successful institution building (Lele and Goldsmith 1989). The fact that many such ties originate in exploitative colonial enterprises should not now prevent their application to more equitable activities.

Some multilaterals have substantial "indigenous" institutional skills of their own, and they may also have strong links with developing countries. The World Bank is an important example, having frequently used its unique position to help build macro and sectoral analytical capacities in member governments. The Bank, however, is an exception; in general, bilaterals have the advantage in institution-building technical assistance.

Multilaterals may have fewer indigenous skills and weaker links with specific countries, but they benefit from internationally competitive recruitment. In particular, multilaterals can recruit the nationals of third-party developing countries. Bilaterals almost never do this, although they frequently employ nationals of recipient countries. This gives multilaterals a relative advantage in enclave-type technical assistance (such as the agricultural research centers supported by the CGIAR) and technical assistance elated to turn-key projects (such as the construction of ports, roads, and so forth), which are increasingly important as the older generation of technicians trained during colonial administrations moves into retirement. Global recruitment also provides a positive externality when those more widely experienced personnel move on to other jobs.[19]

The geopolitically partisan quality of bilateral agencies helps them to tap a major constituency for aid. But it also limits their effectiveness, because it affects the nature of their aid, its allocation among recipients, and its stability. These limitations were an important cause of the rise of multilaterals in the 1960s.

The relatively large number and the partisan nature of bilaterals particularly affect their ability to influence the economic policy of recipients.[20] Several agencies, each with a small stake in an individual recipient country, usually have little incentive to engage in policy dialogue, aid coordination, and conditional aid, but even if they wish to do so their divergent styles and interests make such work very difficult. And when a single donor dominates the scene, its attempts to influence recipient policies will be suspect because of its independent geopolitical agenda and lack of local political accountability. Examples of these problems will be found in all the country studies of this volume.

The potential for multilateral agencies to help solve this problem was well put in the 1969 Pearson report:

> If international organizations take the initiative in assessing country performance and in coordinating aid strategy at the country level, many bilateral aid givers could find it easier to ensure that their aid forms part of an integrated whole. In short, if bilateral donors wish to ensure that bilateral aid is effective, they should try to strengthen the multilateral framework (Pearson 1969: 214).

Coordination is particularly important for policy-based aid (which in practice subsumes program aid and structural adjustment aid), because policies must be stable (but flexible) and national in scope, whereas projects can be locally oriented and relatively short-lived. Multilaterals have, indeed, taken the lead in these policy-based activities. National aid coordination efforts are led by the World Bank's consultative groups and the UN Development Program's Roundtables, while policy-based aid has been led by the World Bank's structural adjustment loans. This work has not been free of ideological content and political conflict, if only because multilaterals are inevitably governed by their donors' point of view and may even be disproportionately influenced by their few largest donors. The agencies' administrative structures, however, demand that donors make compromises among themselves and with recipient-country members, thus diluting and smoothing out fluctuations in each member's short-term interests.

The structure of multilaterals also has a significant impact on their allocations across recipients. (For relatively recent empirical work on this issue, see Maizels and Nissanke 1984; Mosley 1982; McKinlay and Mugham 1984.) While it is difficult to test meaningful hypotheses in this area, it does seem clear that multilaterals have been able, to a greater extent than bilaterals, to allocate their aid following the long-term resource needs of recipients rather than the short-term interests of donors.

Multilateral aid also seems to be more stable than bilateral aid. While formal studies of this issue are rare, clear patterns do emerge from most data series. Johnston et al. (1987: 13) noted about USAID in sub-Saharan Africa: "One of the most striking characteristics of this assistance has been its instability." Aid from most multilaterals has been more stable, contributing significantly to its effectiveness (Cassen 1986).

Finally, while PVOs are not formally within the scope of this chapter, they do have considerable significance as channels for certain aid activities, and often provide additional resources as well.[21]

First, because they are private, PVOs have clear advantages in mobilizing human resources inspired by humanitarian and religious interests, in both donor and recipient countries. They can appeal to constituencies that are alienated by or simply do not correspond to the formal structures of government, and organize those constituencies on their own terms.

Second, because they are small, they tend to have low administrative overheads. Consequently, they are often relatively flexible and willing to take risks, although they generally have poor institutional memories and may also have poor interagency communication and coordination. Nevertheless, as long as PVOs can use the research, information dissemination, and aid coordination activities of larger agencies, their contribution to overall productivity can remain very high.

Third, because they are voluntary (as opposed to being funded through compulsory taxation by governments as is "official" aid), PVOs are often highly motivated to educate the public in both donor and recipient countries.[22] The education of voters, legislators, and government officials can have important spillover effects on the funding of official agencies as well.

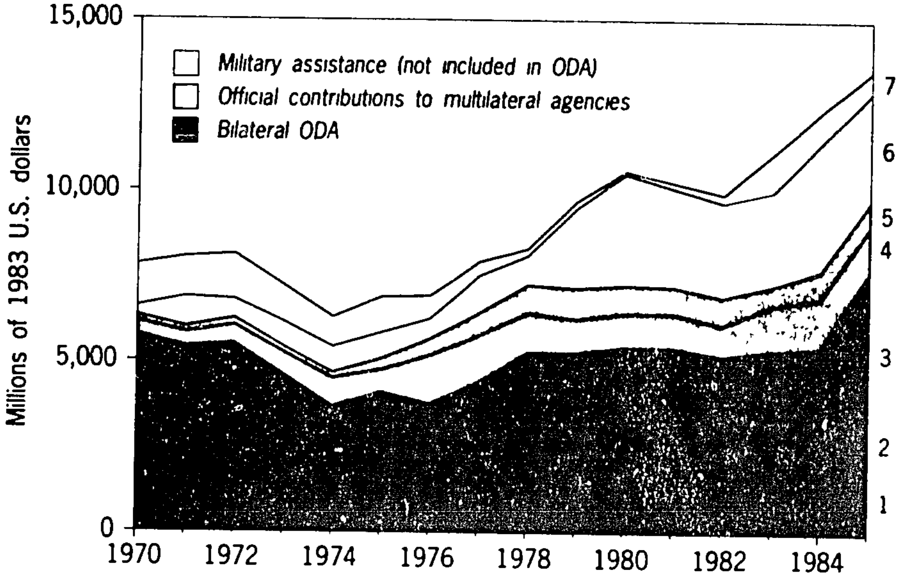
Having enumerated some of the theoretical comparative advantages that donors and agencies could exploit to raise resource productivity, we will now survey the development field, asking to what degree selected donors and their aid channels have actually employed them.

Comparative Advantage in Practice

Bilateral agencies. As noted above, bilateral agencies adopt functional specialties much less often than multilaterals. Nevertheless, because of differences in donor countries' resource endowments and aid constituencies, there has been some expression of comparative advantage among them.[23] The United States provided 31.2 percent of DAC bilateral ODA in 1984–85,[24] almost entirely through USAID. This amount gives the United States substantial influence in setting the agenda for all bilateral aid. But the United States has an even larger share of DAC GNP, and its ODA as a proportion of GNP is the smallest of all DAC countries (0.24 percent, given a DAC average of 0.35 percent). This low level of aid can be explained in part by the fact that the United States suffers from a large-country effect (that is, diminishing returns of various sorts) in aid as in other activities, in part because it has relatively little international trade as a proportion of GNP, and in part because it has relatively few of the close colonial ties that help motivate and support aid flows.

In addition, the United States now provides one of the smallest proportions of its aid to multilaterals (19.2 percent, while the DAC average is 23.5 percent, or 28.5 percent including the European Economic Community). This is partly due to its relative strength in the provision of bilateral aid and is partly a reaction to the fact that between 1963 and 1977 the United States gradually reduced (in real terms) its bilateral programs in order to help accelerate the buildup of multilaterals, and, with the buildup seen as complete, reverted to a larger proportion of bilateral aid.

FIGURE 13.6 Composition of U.S. Foreign Aid by Program, 1970–85



1. USAID development programs
2. PL 480
3. ESF
4. Multilateral development banks
5. Other multilaterals
6. Foreign military sales credits
7. Military assistance programs

NOTE Deflated by U.S. GDP deflator.
SOURCE Budget of the United States, various years

An exceptionally large amount of U.S. ODA is in the form of food aid through the PL 480 program, largely because domestic U.S. agricultural policy involves heavy surplus-creating subsidies. (The EEC is another major food aid donor, for the same reason.) It would be logical for the United States to build intellectual leadership in the area of food aid, but this does not seem to be taking place. In the agricultural and rural development sectors, in contrast, the United States has successfully built a leadership role commensurate with its resource flows and comparative advantage.

Finally, in recent years the United States has had an exceptionally large constituency for security-related aid. This directly affects the regional and functional distribution of aid and the scope for leadership with respect to other forms of aid, and may substitute for other forms of aid as well. The recent composition of U.S. aid is shown in Figure 13.6. Among USAID's particular advantages are large overall program size, long history, and geographic scope permitting comparative research and economies of scale in programming; large in-country missions aiding country-specific analysis and long-term relationships with governments;[25] access to subsidized U.S.

products, particularly agricultural goods; and use of U.S. institutions, including PVOs for public education and resource mobilization, and particularly research and training facilities for agriculture and other disciplines.

Japan (14.0 percent of DAC ODA in 1984–85, but rising rapidly) gives a higher proportion of its GNP in aid (0.31 percent in 1984–85) than does the United States. Japan gives a very high proportion of its aid to multilaterals (38.6 percent) and prefers to give locally (Japan leads funding of the Asian Development Bank, and its bilateral aid goes chiefly to other Asian countries). Much Japanese aid has recently gone for electrification and other public utilities (51.8 percent of sectorally allocable commitments in 1983–84, as opposed to a DAC average of 28.4 percent), and a higher proportion of its total outflows are private loans and direct investment. These preferences probably arise because of Japan's rapid and relatively recent economic expansion and the youth of its aid program. This situation is changing rapidly, however, as Japan becomes increasingly involved in a broad range of aid activities.

France (13.4 percent of 1984–85 DAC ODA, or 9.1 percent excluding aid to their Départements d'Outre Mer/Territoires d'Outre Mer [DOM/TOM]) and the United Kingdom (5.1 percent) both use their strong colonial links as channels for aid. The Commonwealth and the French DOM/TOM are key networks for strengthening a wide variety of public and private institutions. France and Britain also have particular skills in the development of export crops. Although the colonial history of agricultural export commodities has made this a politically delicate area, it is to be hoped that these skills can be exploited, especially for cotton, groundnuts, and several other crops that are in direct competition with U.S. producers and are often ineligible for U.S. assistance. The MADIA study (1987, and Lele and Hanak, forthcoming) argues this case strongly.

West German aid (9.8 percent of 1984–85 DAC ODA) is characterized by its emphasis on technical assistance (48.7 percent of bilateral ODA in 1984–85, given a DAC average of 23.5 percent). Like Japan, Germany's aid is focused on public utilities (44.7 percent of sectorally allocable commitments in 1983–84), probably because of its lack of colonial ties and the capital-intensive/capital goods orientation of its economy.

Aid from Canada (5.6 percent of 1984–85 DAC ODA), the Netherlands (4.1 percent), Italy (3.8 percent), Australia (2.6 percent), Belgium (1.5 percent), and Switzerland (1.0 percent) is relatively recent. Each of these donors exhibits different advantages in relation to its economic structure and political history. Political histories are especially important for aid from Sweden (2.7 percent of 1984–85 DAC ODA), Norway (1.9 percent), Denmark (1.5 percent), and Finland (0.7 percent), which have strong constituencies for poverty alleviation and political nonalignment. Scandinavian assistance has been given to regions and for purposes that have been politically infeasible for other donors, and has been an important complement to other programs. Scandinavian countries have also been leaders in establishing high levels of

ODA as a proportion of GNP, and in raising the proportion of ODA channeled through multilaterals. In addition, their technical assistance is strong in a number of important areas, such as forestry (especially Sweden) and livestock (Denmark). These skills must be adapted to the needs of developing countries, however, and the Scandinavian agencies sometimes suffer from their relatively small size.

Among non-OECD donors, OPEC and Arab agencies represent the largest bloc. They gave \$3.53 billion in 1985, down from a peak of \$9.64 billion in 1980. Of 1985 OPEC/Arab ODA, 10.4 percent went to non-OPEC/non-Arab multilaterals, and 36.9 percent went to countries outside of North Africa and the Middle East; 18.9 percent went to LLDCs, and 43.7 percent went to upper-middle-income countries (UMICs).

USSR net aid disbursements are estimated by the DAC to have been about \$3 billion in 1985, 70 percent of which went to Vietnam (\$1.05 billion), Mongolia (\$0.56 billion), and Cuba (\$0.51 billion).

Multilateral agencies. The World Bank Group combines the work of the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), and the International Finance Corporation (IFC), providing 49.8 percent of all flows from multilaterals in 1984 and 1985.[26] It achieves considerable economies of scale through:

1. gathering and disseminating information, and performing basic and applied research, for both particular countries and developing countries in general, in the areas of macro price and fiscal policies (relying on the IMF for monetary policy), sectoral price and investment policy, and micro behavior
2. using the above analyses to make all lending (including concessional IDA credits) conditional on satisfactory prospects for productive investment, thus ensuring its own continued creditworthiness and also providing leadership for other lenders
3. using its nongeopolitical status to lead country-level Consultative Groups for aid coordination
4. using its central treasury to make interest rate and currency swaps for maximum return on undisbursed funds and maximum efficiency in its lending operations[27]

The constituent parts of the World Bank have their own comparative advantages: the IBRD and IFC (33.3 percent and 0.7 percent of 1984–85 multilateral flows, respectively) maintain low-cost on-lending from private capital markets to developing country governments (IBRD) and private firms (IFC) through:

1. holding paid-in and callable subscriptions from member governments as collateral for their borrowings

2. making detailed analyses of projects and their political-economic context, to ensure the productivity of their loans
3. maintaining geographic and sectoral diversification in their loan portfolio, to share country and sector risks among member countries
4. cofinancing some projects with other development agencies and private investors, to share out those risks to other lenders[28]

IDA (15.8 percent of all multilateral flows in 1984–85) maintains a pool of ODA funds for on-lending to the poorest countries, which is sometimes used in conjunction with IBRD and other funds. This pool is sustained by using highly politicized replenishment rounds to ensure the participation of major donors, and by using the analytical capacity of the Bank Group to maintain high returns on extended credits.

The United Nations gave 18.1 percent of all multilateral flows in 1984–85. This sum was concentrated on technical assistance. The UN is also particularly important as a forum for international negotiation and conflict resolution, and as a provider of aid to countries and for purposes not supported by other major donors.

To sustain the services of UN system agencies, the UN collects regular, annual contributions from member governments on a matching-funds basis. The principal agencies funded in this way are the WFP (4.5 percent of 1984–85 flows), UNDP (3.8 percent), UNHCR (2.5 percent), UNICEF (1.6 percent), UNRWA (1.2 percent), and UNFPA (0.8 percent).

Regional development banks channeled 19.1 percent of multilateral funds in 1984–85 to build infrastructure for trade and promote regional integration (for detailed data and analysis see UNCTAD 1984). They operate and are funded on the same principle as the World Bank, but their regional focus allows additional resources to be raised from constituencies with purely local interests.

The Inter-American Development Bank (IDB) is the largest of the regional development banks, with 11.6 percent of all multilateral flows in 1984–85. Its funding is led by the United States. The Asian Development Bank and Fund (ADB/F) gave 5.0 percent, and the African Development Bank and Fund (AfDB/F), whose funding is led by the African states themselves and by European countries, gave 2.1 percent. There are also several subregional organizations, such as the Caribbean Development Bank (0.4 percent), but they operate on a much smaller scale. Each bank has one or more principal donors, raising resources that add significantly to those available for bilateral activities.

Special constituency agencies form another, less well-defined category of multilaterals. They lend everywhere, but on behalf of a limited constituency or group of countries; this is often called "collective bilateralism." These agencies represented 12.4 percent of multilateral activity in 1984–85, and included the European Development Fund (EDF) and the European Investment Bank (EIB) of the EEC (8.4 percent); Arab and OPEC agencies[29]

(2.3 percent); and the International Fund for Agricultural Development (IFAD, 1.4 percent), a joint OECD/OPEC venture. IFAD is an important example of the problems of funding public goods: despite widespread recognition of the importance and the innovativeness of its work, there has been great difficulty reaching agreement on matching-funds ratios between OECD and OPEC, as changing oil prices shift the relative incomes of these two groups (King 1985).

In addition to the resource-transfer agencies discussed above, some multilaterals disburse very little money directly to developing countries but may have a large impact on development. An important example is the CGIAR: its budget of about $200 million a year in 1984 and 1985 would correspond to about 1.2 percent of multilateral flows. Almost none of this was spent by developing countries, but the CGIAR's central role in coordinating international agricultural research is of great importance to them. The CGIAR-supported research centers collaborate with national research agencies, providing important technical assistance and research services to them on a predictable, ongoing basis.

Fads, Strategy, and the Exploitation of Comparative Advantage

As noted in the above discussion, there is a striking degree of scope for comparative advantage, not only between bilaterals and multilaterals in general, but also among bilaterals and among multilaterals. Yet, those comparative advantages are rarely the focus of debate, and they display themselves only modestly in donors' and agencies' explicit policies.

An important reason for this is the lack of a broad, generally agreed-upon strategy of development, which will yield common objectives and a common understanding of development processes and within which each donor can exercise its comparative advantages. Because the leadership necessary to generate consensus around such a strategy has been missing, development agencies have been buffeted by recurring fads.[30] Each fad is a development tactic, a theme. At best, it is a segment of a strategy. Each fad is the outcome of a particular debate that, in the vacuum left by the absence of a broader strategy, becomes a standard for what is acceptable everywhere.

While it may be easy to overstate the importance of fads, they do have a significant impact on most agencies. Under their influence, agencies tend to seek essentially the same instruments for development. They come to differentiate themselves by style and method, rather than by substantive specialization. There is duplication of effort, precipitating funding crises, calls for reform, and ultimately a new dominant theme.

Repeated waves of new themes have seriously affected the professionalism of foreign assistance agencies. Each thematic change turns agencies increasingly toward generalists and away from specialists, because specialists have a greater need for stable, long-term relationships with donors and recipients. This showed most dramatically in the decline of agricultural technicians at USAID in the 1970s: despite the continuing dominance of agricultural projects in the foreign assistance program—for which there continued to be strong demand—specialists were not in vogue at that time and many skills were lost in the rush to fund more explicitly poverty-oriented programs. It can be argued that poverty-oriented projects require technical expertise at least as much as specific agricultural or other projects, but in the context of faddism this need was lost sight of in favor of the appearance of technical acceptability. Of course, this helps explain the generally poor record of such projects in achieving their objectives. Each move toward generalists further reinforces the degree to which the development-assistance community is vulnerable to a new fad, as the ability to specialize according to comparative advantage and the restraints to change arising from technical specialization are eroded. This tendency can be noted more recently at the World Bank.

From the recipients' point of view, fads tend to focus attention excessively on particular elements of the development process, distracting recipient governments from building the national capacity to address the full range of problems they face. For example, during the basic human needs fad of the 1970s, resources were diverted toward providing goods and services directly to the poor, through activities at the grass roots level. National-level institutions such as those for agricultural research were raided in order to provide the people and resources for these regionally fragmented poverty-alleviation programs, but as these programs became increasingly poorly serviced by the weaker national institutions, their effectiveness was undermined.

In many areas, grass roots poverty-alleviation activities were very much needed, but the idea was extended too far, into areas where it was no longer productive. (For a detailed discussion of this process in Africa, see Lele 1975.) By the time it was fully played out, the basic human needs fad had allowed national-level physical and institutional infrastructure and macroeconomic policy to deteriorate severely in many countries. A prime example is Tanzania, where almost all microeconomic efforts were ineffective because of an extremely weak macro environment (see the chapter by Collier in this volume; MADIA 1987; Lele and Hanak 1990).

A similar problem is seen in the wake of any fad.[31] Recently, for example, the theme of structural adjustment has focused attention on macroeconomic variables, ignoring public investments and the microeconomic problems of resource allocation. Macro policy is stressed by many analysts in the current U.S. administration, the International Monetary Fund (IMF), and the World Bank, but their ideas have spread rapidly throughout other multilateral and bilateral agencies. Again, the fad is a simplification of development processes, with obsessive concern for a few tactical objectives: immediate reductions in domestic and foreign trade controls and in fiscal deficits and certain types of subsidies, and immediate increases in aid to the private sector.

These are generally necessary reforms, but they are not sufficient. The analytic capacity of developing country governments must be enhanced if they are to sustain macroeconomic balance over the long run, provide public goods in particular markets, and build the institutions that increase factor productivity through technical change. These tasks are essential if the opportunities created by the removal of major distortions in the economy are to be seized.

In the short run, fads may help raise resources by focusing public attention on very specific foreign assistance needs. In the long run, however, they undermine each agency's comparative advantage, create embarrassing inefficiencies, and reduce both the quantity and the quality of aid.

If the various comparative advantages of bilateral and multilateral agencies are to be more fully exploited, there must be a shared strategy for aid that informs each agency's work. This strategy must incorporate the needs and desires of the entire aid community—recipients, donors, and practitioners. To be sustainable, the strategy must promote growth with broad participation by the poor, and must recognize that the natural province of public assistance is the efficient provision of public goods—the institutions, physical infrastructure, technology, and government policies on which the productivity of the private sector depends.

This is a tall order, but after four decades of experience with foreign aid, the broad outlines of a strategy capable of generating a broad consensus may now be clear. The core of a consensus strategy might be the promotion of technical change and capital accumulation in agriculture, aimed at providing increases in national income to drive demand-led growth throughout the economy.[32] Agriculture is initially at the core of this strategy because it is the dominant employer, it offers continuing opportunities for cost-reducing technological change, and it has strong demand linkages. As a result, investment and technical change in agriculture generally have strong potential for not only leading growth throughout the economy but also for fostering structural transformation of the economy, while also rapidly reducing poverty through lower food costs and expanding the demand for labor.

Generating such growth requires massive investment in infrastructure and institutions promoting technological change, open domestic markets in which small firms can operate, and an open trade regime in which labor-intensive production is profitable. The key element in the strategy is building domestic demand in rural areas. This relieves (but does not eliminate) the need for growth in exports, while focusing demand on relatively labor-intensive goods and services. Increased employment in turn raises food demand, and the whole strategy results in a more dispersed and sustainable pattern of growth.

The emphasis on domestic demand is particularly important in countries where income is highly concentrated in certain groups, such as Mexico or Brazil. In such countries aggregate demand for domestic output can often grow more quickly in the large low-income bracket than in the smaller high-income group. Thus, a broader dispersion of income, driven, for example, by agricultural growth in northeastern Brazil or in the smallholder areas of central Mexico, can accelerate growth in national income as well as improve equity. Of course, in the bulk of Asia and Africa, the agricultural sector is so large and encompasses so much of the population in broadly dispersed activities that there is no choice other than to give technical change in agriculture a central place in the development strategy.

While this strategy depends most crucially on developing country governments themselves, there is obviously scope for a wide range of donor activities. In particular, foreign aid should focus on public goods, which are uniquely able to raise the productivity of resources in the small-scale and informal sectors of both agriculture and nonagriculture. It is those productivity increases, in particular, that are the sources of equity-enhancing growth.

Aid plays an especially important role in raising returns to capital, or equivalently, the aggregate absorptive capacity for capital. This helps to mobilize domestic and foreign savings for local investment, particularly if accompanied by improved financial institutions. Developing countries have proven themselves capable of generating savings rates well above 15 percent and of attracting large amounts of foreign capital as well. During the late 1970s and early 1980s, capital inflows to all developing countries were about 4 percent of their aggregate GNP. Given the high mobility of capital today, however, small differences in risk or productivity will result in large capital flows, and many countries have suffered greatly from capital flight and depressed savings rates.

A development strategy led by technical change in agriculture and growth in domestic demand is broadly consistent with the needs of all developing areas in Africa, Asia, and Latin America. Each country will have to find its own path, exploiting its own endowment of institutions and resources and its own pattern of preferences. But all countries will need substantial investment in productivity-enhancing public goods, including physical infrastructure and human, social, and institutional capital. Resource transfers from outside will be needed to pay for the additional balance of payments deficits that allow such investment and to fund those internal transfer payments that are needed to facilitate policy reforms and political evolution. Over the past thirty years, expanding concessional resource flows has been an urgent priority, primarily because other resources have been used at tragically low levels of productivity. In principle, faster growth and broader participation could be achieved with readily attainable rates of domestic savings and of private capital inflows, if factor productivity were high enough to mobilize these resources.

To generate sufficiently attractive levels of resource productivity, aid agencies will have to work efficiently to help governments provide public goods, and they must pursue their own comparative advantages as vigorously as do private firms. The historical record suggests that these advantages exist, but have been eroded by successive waves of fads in development thinking. For each agency to exploit its natural advantages successfully, all agencies will have to be aware of what others can do and are doing, although explicit coordination will generally not be necessary.

The central comparative advantage of multilateral agencies is in supporting the macro environment needed for growth. This includes helping countries to open their trade regimes, minimize restrictions on their private sector (particularly on small- and medium-scale firms), and develop and maintain public goods such as physical and institutional infrastructure. Considerable financial resources will be required, as the short-run costs of switching policy regimes are substantial. The technical requirements are also large, both for managing policy-based aid and for participating in those enclave and turn-key technical assistance activities in which multilaterals find some advantage.

For most bilaterals, the key advantage is in developing appropriate institutional structures and human resources consistent with rapid economic growth. These range from the analytic skills needed to manage national price policies to subsectoral institutions such as a system of local agricultural research stations. There will inevitably be a need for close interaction between the bilateral and multilateral agencies. For example, bilateral efforts to build national agricultural research systems in agriculture should coordinate with the enclave research of the CGIAR. Similar cooperation could work in many other activities, such as between multilateral funders and bilateral technical assistance programs.

In addition to the bilateral-multilateral distinction, there could be greater recognition of the relative comparative advantages among bilaterals and among multilaterals (although this already takes place for multilaterals to some degree). Such recognition probably requires deliberate comparative research, like the recently completed MADIA project.

As we have seen, many determinants of agencies' comparative advantages cut across the bilateral-multilateral distinction. It may nevertheless be useful to summarize the broad advantages and disadvantages of these two agency types. In general, bilateral agencies have the following strengths:

1. They can apply the skills acquired in donor-country institutions to the aid process, adapting them for institution-building technical assistance in recipient countries.
2. They can use their international economic, political, linguistic, and cultural links to provide stable constituencies for aid to certain countries, and to generate the institutions and skills necessary for productive work in those areas.
3. They can respond to the needs of particular constituencies for aid and educate those constituencies as to current aid needs. When

threatened by competing national interests, bilateral aid agencies often respond by changing their aid agenda, but they can also use their influence to educate legislators and budget-makers as to the importance of their work.

In contrast, multilateral agencies have different strengths:

1. They can provide regional and global collective goods through matching-fund arrangements with member governments that help pay for benefits that spill over from one national aid constituency to another.
2. They can capture significant economies of scale in operations (particularly minimizing the cost of loan capital through bulk borrowing, risk sharing among member countries, and currency and exchange rate swaps) and in research (particularly insofar as the results of their work are disseminated internationally, providing important institutional leadership in the development community).
3. They can establish systems of international competitive bidding to purchase goods and services at the lowest possible cost and maximize the real value of aid flows.
4. They can recruit staff globally (especially from developing countries), thus expanding the worldwide pool of expertise in development processes.
5. They can undertake politically delicate tasks, such as policy-based lending, aid coordination, or refugee assistance, that bilaterals cannot do because of their geopolitically partisan nature.
6. They can complement each other better than bilaterals, because they often compete with one another for a common pool of aid funds and must specialize to justify their separate identities. In contrast, bilateral agencies all tend to do more or less the same things, once they have secured a share of their national budgets.

For aid practitioners to exploit their comparative advantages and better complement each other's work, complete agreement on tactics is not needed. What is necessary, and surely achievable, is a moderate consensus on broad strategy and a recognition of the aid community's natural diversity. As the comparative advantages of each agency are understood, those advantages can be exploited more fully. There will be more and better investment in public goods, thus increasing the productivity of all resources.

Complementarity between agencies, of course, does not have to be deliberate. Private sector firms often complement each other's work without explicit coordination. But for the invisible hand to function between governments, it is necessary to maintain an adequate base of shared knowledge and mutual understanding.

Conclusions

It is clear from the case studies in this volume that foreign assistance has contributed significantly to achieving sustainable, equitable growth in developing countries. As aid has grown in aggregate quantity, however, it may have become less efficient in meeting its objectives. This decline in efficiency has contributed to a widespread dissatisfaction with international institutions that threatens aid levels, even as polls show that a strong majority of the public supports efforts to reduce Third World poverty through economic aid (Contee 1987).

Any decline in the marginal efficiency of foreign assistance could easily be attributed simply to rapid growth and diminishing returns. However, the capacity to effectively absorb foreign aid has probably been increasing in most developing countries, as their investments in social and physical capital accumulate. Thus a declining marginal efficiency of foreign assistance is more properly attributed to the increasing fragmentation of the foreign assistance community.

The lack of leadership brings confusion and misunderstanding. As a result, passing development fads run rampant, undermining the effectiveness of all aid flows. The faddism and instability of foreign assistance is heavily associated with aid from the United States, perhaps because of the great size of U.S. flows, the strong American focus on global power politics, and the great volatility of U.S. foreign policy. Although some multilateral agencies and other bilateral donors have attempted to offset the major shifts in U.S. foreign assistance, the case studies in this volume suggest that still more efforts in that direction are needed.

Instability in foreign assistance has compounded other major external shocks, especially variations in the interest rate and in the price of oil and other primary commodities. Developing countries depend heavily on primary commodities, and the studies in this volume document the tremendous impact of shocks in these markets. For example, many of the policies targeted for reform in the 1980s were initially ways of coping with the price shocks of the 1970s. One of the objectives of development is to achieve a more diversified economy, which makes a country less vulnerable to these shocks. Diversification, however, is not achieved by artificially restricting trade in primary commodities, but by building comparative advantage in a wider range of goods and services through increased investment in human and other forms of capital. To meet these goals, development assistance policies must become more stable, with actual aid flows more responsive to the needs of recipients.

Although we emphasize that aid policies should become more stable, developing countries should probably recognize aid flows as inherently unstable, and see the income from aid as transitory rather than permanent. This recognition would place a particular emphasis on investment in fixed social and physical capital, rather than consumables. Although everyone would prefer smooth flows, they do not always occur, and careful planning can help to overcome the problem of aid instability.

The lack of leadership in the development community with respect to long-term strategy is a serious problem. We have suggested that the World Bank, as the dominant multilateral agency, is uniquely positioned to lead the aid community to a sustained consensus on an effective development strategy. Such leadership would have to be exerted far more subtly than was U.S. leadership in the early postwar period. There would have to be a broad consensus-building effort, drawing upon the analytical efforts of the whole development community and including frequent meetings and seminars with broad attendance.

Unfortunately, rather than working in this direction, the World Bank has recently been taking less interest in strategic research, thus reducing its capacity to pursue the consensus-building process. If the World Bank abrogates this responsibility, it is not clear where the leadership will come from. The United States may still have some capacity to build such a consensus, by drawing upon its intellectual resources outside of USAID, but it would require a considerable reorientation within USAID, which has until now seen the World Bank as the logical home of such an effort.

An alternative to the type of leadership discussed here, of course, would be leadership by the recipients of aid. The larger, more developed Asian countries have already built a substantial internal capacity to order their priorities and force donors more or less into conformity with their own strategies. This has worked passably well in India and China. But in smaller countries, the idea of recipient sovereignty has often turned aid into just another source of patronage for politicians and bureaucrats.

A global consensus on development strategy could draw on major economies of scale, while still providing aid that reflects the individual needs of each country. Indeed, an important goal of the strategy we present is to help make each recipient country more autonomous, by building national analytical capacities as well as by improving the level and distribution of national income. Such autonomous capacity is both a means and a goal of international development efforts, but to build it, the world's foreign aid donors and agencies must first aim to improve their own work. As the case studies in this volume show, many donors and recipients have used aid very effectively in the past, and all can be learning to use it better in the future.