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How Will Greater Foreign Aid Help the Poor This Time?

William Easterly, Ph.D.

What are the two tragedies of the world's poor? The first tragedy has already been well covered by Jeffrey Sachs in his book *The End of Poverty*. He notes that 30,000 children die every day from the diseases and malnutrition that go along with extreme poverty. For example, there are nearly 2 million annual child deaths from diarrhea, which could be easily prevented with 10-cent doses of oral rehydration therapy. It's really a tragedy that people are so poor that they cannot afford 10-cent doses of oral rehydration therapy.

But there's a second tragedy, which Jeff doesn't spend any time in his book talking about, and the second tragedy is that the West already spent \$2.3 trillion on foreign aid over five decades, and babies with diarrhea are still not getting the 10-cent doses of oral rehydration therapy. There are still 2 million deaths, and even in what the World Bank calls an aid success story like Ghana, 50 percent of babies with diarrhea never receive oral rehydration care.

This is really the scandal of our generation, that all this money has been spent on foreign aid and yet, in any meaningful sense, this money never reached the desperate poor. What is the response to this failure? It's to ask for more aid money, which has been the same answer as in the previous five decades of foreign aid, which does nothing whatsoever to address the second tragedy: that money is spent and yet does not reach the poor.

A Grandiose Global Plan

So Jeff Sachs, the U.N., the World Bank, and the International Monetary Fund have come up with a big

Talking Points

- Aid agencies as an industry should be reorganized and drastically restructured to specialize more in individual monitorable tasks for which they can be held accountable.
- A truly independent evaluation of aid to see what piecemeal interventions are working would give agency staff incentives to search for what works.
- Aid vouchers could be given to the poor to promote competition among aid agencies to deliver what the poor want to get these vouchers.
- Social entrepreneurs could meet potential philanthropists and official aid donors in a marketplace setting in which there is transparency and accountability for how both parties have done in delivering results.
- Philanthropists or official aid agencies could put up large amounts of money for prizes to reward finding things that actually work to achieve benefits at a reasonable cost for poor people.

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plan to solve all the problems of the poor by the year 2015. It's a pretty modest plan: There are only 449 separate interventions, and there's a very doable agenda of 54 different Millennium Development Goal target indicators, which represent 18 targets, which represent 8 millennium goals, and the plan is all nicely laid out very clearly and concisely in a 451-page main report with 3,300 pages of technical annexes.

How exactly would this plan be implemented? Jeff says in his book that the U.N. Secretary General should personally run the plan. He would not have to do much: He would just have to coordinate the actions of thousands of officials in six U.N. agencies, the U.N. country teams, the World Bank, the International Monetary Fund, all consistent with the World Bank and IMF Poverty Reduction Strategy Papers, which have their own 1,246-page "PRSP sourcebook."

Just think about the incentives that are created by this grandiose global plan. You have all the aid donors and recipients collectively responsible. They all share responsibility for implementing all of these actions, for meeting 54 different goals, which also depend on lots of other things besides what the donors and recipient governments do. If anything goes wrong, you can blame the other aid donors, you can blame the other factors that affected whether the goals were achieved or not, or you could even just say, "The reason I didn't achieve that goal was that I was working on this other goal."

That's what happens when you have multiple goals, collective responsibility, and goals depending on things besides what the aid agents themselves do. This is the worst possible incentive system of all time. When you really read the fine print of the very long documents that set out the goals, you reach this conclusion: In this great, grandiose campaign to end world poverty and achieve the Millennium Development Goals, nobody is individually responsible for any one result.

Accountability and Incentives Through "CIAO"

To join the media war over foreign aid, I came up with this acronym called "CIAO." What does "CIAO" stand for? The reason the aid plans go so

wrong is because they lack the "C," which is customer feedback; they lack the "I," which is incentives; they lack the "A," which is accountability; and as a result, they lack the "O," which is the good outcome that would come from any intelligent effort to end world poverty.

Of course, you could set all this in reverse if you did have true accountability and incentives. Then aid agents would want to get customer feedback and try to figure out what works, and then you could get some specific good outcomes from some aid efforts.

Just think about the U.N. Millennium Development Goals. How, possibly, could you get customer feedback on which of the 449 interventions are working? Where are the incentives for those implementing the 449 interventions? Who can be held accountable if some of the 449 interventions don't work? And why doesn't somebody just get held accountable for getting 10-cent medicine to babies?

The planners' favorite answer is to double foreign aid. An interesting iron law of aid advocacy is that whenever anyone starts campaigning for more foreign aid, they always ask for an exact doubling of foreign aid. It's never an 83 percent increase or 117 percent; when in doubt, double foreign aid. Not long ago we had the G-8 summit, in July 2005, where they agreed to double aid to Africa. They've also agreed to double foreign aid as a whole by the year 2010, and the aid campaigners will then ask for doubling aid again after 2010.

Unfortunately, the obsession with the amount spent substitutes for customer feedback, incentives, and accountability. It substitutes for focus on whether the money actually reaches the poor, so the second tragedy continues unabated. And it also creates the perverse incentives in aid agencies just to spend money, because if money is the indicator of success, then all the incentives are just to spend aid money and not to try to have the money get results.

The World Bank and IMF have their own plans, which they call the Poverty Reduction Strategy Papers. This planning approach is really just a misguided way to approach the problems of world poverty.

F. A. Hayek said that "the success of action in society depends on more particular facts than anyone can

possibly know.” How can you possibly know enough to implement a big plan? Economics is all about teaching people how little we really know, how little economists really know, about what they imagine they can design. Karl Popper has this great quote, which is really applicable in a lot of circumstances, that any sort of comprehensive plan to remake society in a way that eliminates poverty is just completely unworkable because “it’s not reasonable to assume that a complete reconstruction of our social system would lead at once to a workable system.”

Searchers vs. Planners

The alternative to planners is “searchers.” There are private entrepreneurs who get customer feedback to meet essential needs, like your need for Harry Potter books. They have incentives to get them to you, so there were 9 million copies of the Harry Potter book distributed on the first day of its publication because everyone along the supply chain had the right incentive to get 9 million copies out there. The publisher is held accountable if you’re dissatisfied. If you get your Harry Potter book and the words are upside down, you can take it back and get a new one; and if the firm doesn’t give you a new one, then the firm is eventually going to go out of business for mistreating the customers.

The other great feedback system that we’re all familiar with is democracy. Politicians are subject to voter feedback, so they have the incentives to meet your needs for public services, and they’re accountable if they do too lousy a job on delivering public services.

Now, we know none of these solutions works perfectly all the time, and they’re certainly not an overnight panacea because, as Karl Popper has told us, there’s no way that you could transform a whole society overnight from what it is now to a free-market democracy. It’s just not within the realm of economists to be able to engineer that. But we know from overwhelming empirical evidence that markets and democracy are the ultimate home-grown source of prosperity. This is how you eliminate world poverty: through markets and democracy. This is what works.

I think markets and democracy can be a great model. Since they are such a successful system,

they can be a great model to try to make aid more like a successful system, to try to inspire aid efforts to do less planning and more searching, to try to get aid agents thinking in market-like terms, thinking in democracy-like terms of getting CIAO: getting customer feedback, having incentives for aid agents to deliver the medicines to the babies, and having accountability if they don’t.

We’re lucky enough in rich countries to get most of our needs met. And how do we get them met? We get them met from the efforts of political, economic, and social searchers with CIAO. But on the other side of the aid wall, the poor are stuck with unaccountable planners. It seems that the only part of the world in which people still believe in central planning is those who are unlucky enough to be the intended beneficiaries of aid plans. On our side of the aid wall, we get our needs met with searchers, but for the poor on the wrong side of the aid wall, the second tragedy continues.

So we have to ask the question: Why is it that planners are so popular? Why are these big plans more popular than searchers in the whole foreign aid business? There’s a fairly clear political economy explanation that the planners offer appealing dreams of ending poverty, which is really good for sound bites and media frenzies, without anyone in the rich countries actually being held responsible for doing anything very costly. All that has to be done is to spend a little more aid money, and then everyone is satisfied, and then you promise grandiose things like the end of poverty for which you will never be held accountable. Politically, it’s great to be able to promise big things for which you’ll never be held accountable.

Searchers don’t offer big promises like the end of poverty, which aid cannot possibly achieve. Nothing outsiders do can possibly achieve the end of poverty; again, that has to be done by relying on home-grown markets and democracy. So aid right away has a huge rhetorical disadvantage: It’s not offering the big promise, and the searchers are insisting on politically risky accountability. Everybody likes accountability for other people, but nobody likes being held accountable themselves, and rich country politicians certainly don’t want to be held accountable for taking responsibility for

whether their aid dollars accomplish something in helping poor people.

Why the Planners Have Failed

The dream of planners is that foreign aid could finance economic growth, and the only reason to think that that can't happen is that it has never happened and every effort to make aid achieve economic growth has failed. The data show that there is a correlation between aid and growth, but, unfortunately, it's negative. Sophisticated econometric analysis finds no evidence that aid raises growth. What *does* raise growth is markets, so the citizens of India and China, by shifting to more market-oriented economic systems and creating new opportunities for millions of local entrepreneurs to get rich by their own efforts, increased their own incomes by \$715 billion last year while we were agonizing about whether to give \$10 billion more here or there for foreign aid.

This is the true source of long-run development, not foreign aid. The good news about this is that, once you acknowledge that growth is mostly home-grown and comes from home-grown markets and democracy, you could free up aid so that it could maybe accomplish some useful things for poor people to give them new opportunities. You could free aid to do some more specialized tasks that are not so grandiose as ending poverty or achieving economic growth. You could hold aid agencies accountable for achieving specialized tasks.

Let me just give you one example of the wrong approach of planners. There's a Canadian/World Bank project in Lesotho that tried to promote farming in a mountainous region of Lesotho, which didn't work because, according to the project managers, the local people were defeatists and didn't think of themselves as farmers. That was really silly of the local people—except for the fact that they were not farmers; they were migrant workers in South African mines. The only result of the project was that they built a new road on which South African lorries brought grain into the region, which drove the few existing farmers out of business. This is the kind of mess-up on the ground that happens when you try to plan from the top down.

Unaccountable planners also keep repeating or even intensifying the same failed approaches. The aid business has been stuck for a long time on trying to work with local governments, which usually means they wind up chasing unachievable goals of transforming poor country governments, which outside aid cannot possibly do. So you have the unaccountable chasing the unchangeable.

In the 1960s and '70s, there was project aid, which assumed that governments had good institutions and policies. And, of course, the aid didn't work then because the governments didn't have good institutions and policies.

In the 1980s, there was some dawning realization that part of the problem was bad economic policies, so then there was the invention of structural adjustment by the World Bank and IMF, which made aid conditional on the bad governments adopting good policies. The only problem with structural adjustment phase one was that it didn't work. Aid was not a strong enough incentive to change policies, and the aid donors were not sufficiently selective; they kept giving money to bad governments even when they didn't reform.

So the response to the failure of structural adjustment phase one was structural adjustment phase two, where you continue the same failed program but now you add even more objectives, even more things that you're trying to change in the bad government on the receiving end. Conditionality in the 1990s expanded to include conditions on corruption and democracy, which was also ineffective; and the meddling of the aid community, combined with very unstable local domestic situations, sometimes led to failed states. Now, in the new millennium, we're talking about trying to use armies to try to take over some government functions—that U.N. peacekeepers could go into the country and start administering the country directly.

At every stage, there's been an escalation from trying ever more intensively to change bad government into good government; and that, like fostering the end of poverty, is not something that can be achieved by outside foreign aid. So the outcome of structural adjustment is that of the 13 African countries that receive the most structural adjust-

ment funds, there were two relative success stories that the World Bank and IMF talk about over and over again: Ghana and Uganda. All the other 11 countries had zero or negative growth, and a lot of countries under IMF programs actually wound up becoming failed states altogether.

The World Bank and IMF, in response to the failure of structural adjustment loans, did acknowledge some of the criticisms of outside critics, and what they did was change the name: The name of the loans was changed to “Poverty Reduction Support Credits” and “Poverty Reduction and Growth Facilities,” which is still trying to do the same thing as the old structural adjustment loans, but now with nicer-sounding names.

How the U.N. Has Failed

And what about the U.N.’s accountability? The fascinating thing about the U.N. is that it is the main sponsor of the U.N. Millennium Development Goals Campaign to End World Poverty, and then, at the same time, the U.N. issues these incredibly gloomy reports about how badly everything is going. In September 2005, they issued a report that talked about how everything is failing: Millions more fell into deep poverty, decline of hunger is slowing, measles immunization is lagging despite a safe and inexpensive vaccine that’s been available for 40 years, there is no change in maternal mortality, forests are disappearing, slum dwellers are growing. The U.N. is talking about the failure of its own plan.

So what is the response to failure of the aid plans? Let me give you three possible choices for the way the U.N. could have responded, and then I’ll ask you, with your knowledge of current events and your knowledge of economics, to tell me which ones of these choices were actually selected by the U.N.

- Possible response (a): The U.N. could hold somebody in the U.N. accountable for the failure and create incentives in the future to get results through such accountability.
- Possible response (b): Ask donors for more money to follow the same plan over again—to do the exact same thing that just failed over again.

- And response (c): Just have Jeff Sachs make an MTV video with Angelina Jolie.

Of course, I don’t have to tell you. What actually happened was (b) and (c); (a) still has never happened. In fact, it never even seemed to occur to the U.N. that (a) was a possible response when they were writing their gloomy reports about how the aid plan was failing. They never seemed to notice the irony of writing about the failure of their own program. For them, it’s just a fund-raising vehicle to talk about failure.

Let me just give you one example of the searchers who find good things that work. This is an example that I’ve seen with my own eyes, and I know the person responsible personally. There’s a Ghanaian named Patrick Awuah who is the son of a market-trading mother, grew up under Ghana’s brutal military regimes in poverty. He somehow got an escape route where some benefactor financed a scholarship for him at Swarthmore, and then he got rich working for Microsoft.

Then he decided to do something for Ghana. He came back to Accra, Ghana, and started a private university to compete with the state-run university, where professors and students operate under heroic conditions but it’s just a state-mismanaged mess. He started his own private university in Accra, which was an immediate success, attracting lots of students. Fifty percent of his students are on scholarship, out of poverty. The curriculum is business, computers, and critical thinking. And Patrick Awuah says one of his proudest moments came when one of his students e-mailed him, saying, “Mr. Awuah, I am thinking now.”

The only sad part about this story is that he was naive enough to think that he could increase the scale of his efforts by approaching some of the official aid donors for supplementary financing, and he was totally turned down by the official aid donors. It seems as if the great “Save Africa” campaign has room for everyone except Africans.

Finding What Works

So what do we wind up with as a policy recommendation? I discovered this really amazing princi-

ple: When something doesn't work, you should discontinue it.

What are some of the things we could discontinue? We could discontinue structural adjustment loans for poor countries under whatever name, because these have been an attempt at Utopian social engineering by the IMF and the World Bank that have not worked. Get rid of all the Utopian goals and plans. Let's just call an end to this whole charade of the Millennium Development Goals. It's not causing anyone to do anything constructive except write very large reports that nobody wants to read. Let's get rid of the Poverty Reduction Strategy Plans. That's not how you get out of poverty. George Washington did not have to fill out a Poverty Reduction Strategy Plan; that's just not the answer.

For long-run development, most of the hope is not from aid at all; it's from home-grown, private entrepreneurs, social entrepreneurs, reformist politicians, and political activists who campaign for democracy, all of whom have good CIAO: They get good customer feedback, they have incentives, they have accountability, and they get good outcomes. Aid at best could play a supporting role, fixing specific problems that are fixable by outsiders.

The good news for aid agencies is, they could be set free from all the planning nonsense that absorbs most of their energies now to concentrate on piecemeal improvements for the poor rather than try to develop whole societies. So how do we try to get them motivated to do that?

Number one, we should have truly independent evaluation of aid to see what piecemeal interventions are working. That will give incentives for aid agencies' staff to search for what works when they know that they're facing independent evaluation. And once they have those incentives, the aid agencies as an industry will be reorganized and drastically restructured. Instead of these grandiose schemes to end poverty, you would have aid agencies that specialized much more in individual monitorable tasks for which they can be held accountable.

To get more and more incentives for searchers to work in development, we could do aid vouchers where we just give vouchers to the poor and say, "Here are vouchers you can turn in for any devel-

opment service you want from any aid agency." The aid agency then can turn in the voucher for their own budget, so there will be competition among aid agencies to deliver what the poor want to get these vouchers.

We can think of aid marketplaces where we have venture capital funds, where social entrepreneurs can meet potential philanthropists and official aid donors in a marketplace-type setting where there's a lot of transparency and a lot of accountability for how both parties have done in the past in delivering results. We could also think about having philanthropists or official aid agencies put up large amounts of money for prizes to reward finding things that actually work to achieve benefits at a reasonable cost for poor people—at the very least, just have someone, somewhere responsible for delivering 10-cent rehydration therapy doses to infants.

The only people who can be planners are those elite officials at the IMF and U.N. and World Bank who come up with the grandiose plan, but everyone else—all of us—can join an army of searchers for solutions to the poorest's problems, giving increasingly vociferous feedback to aid agencies and rich country politicians to say that a half-century of the second tragedy of the world's poor has just been too long. A half-century of glamorous but unaccountable aid spending has been way too long, and a half-century of aid spending without getting 10-cent medicines to sick babies is way, way too long.

Conclusion

The advocates of aid usually close with some inspirational rhetoric to motivate you to action. I also believe very much in inspiration, so I'll close with a quote from Robert F. Kennedy on how we can all be searchers:

Each of us can work to change a small portion of events and the total of all those acts will be written in the history of this generation. Each time a man stands up for an ideal, or acts to improve the lot of others, he sends forth a tiny ripple of hope and crossing each other from a million different centers of energy and daring, those ripples

build a current which can sweep down the mightiest walls of resistance.

Let's combine to sweep down the aid wall. Let's change foreign aid.

—*William Easterly, Ph.D., is a professor of economics at New York University (Joint with Africa House) and co-director of NYU's Development*

Research Institute. He also serves as a non-resident fellow of the Center for Global Development in Washington, D.C.; and spent 16 years as a research economist at the World Bank; and is the author of The White Man's Burden: Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good (Penguin Press, 2006).