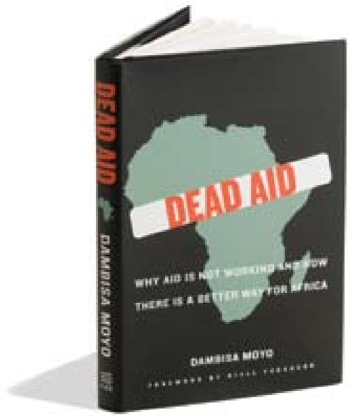
Thesis of a rigid revivalist



Dambisa Moyo

Dead Aid

Why Aid Is Not Working and How There Is a Better Way for Africa

Farrar, Straus and Giroux, New York, 2009, 188 pp., $24.00 (paper).

DAMBISA Moyo's widely discussed attack on the aid system—contrary to what you may have heard—never says that all aid should end in five years. Moyo does pose a rhetorical question about the consequences of quickly cutting off all aid, but page 76 makes it clear what she actually recommends: much more focus on using aid to encourage non-aid mechanisms of finance, so that aid declines over time with the ultimate goal of "an aid-free world."

To assess whether the book is convincing, we need to understand that it is not about how Africa should develop; it is about which mechanisms of *financing* lead to better development outcomes in Africa. Moyo defines aid as systematic cash transfers to governments, via grants or concessional loans—omitting humanitarian, emergency, and charity-based assistance directly to the needy. Her task is to show that aid thus defined cannot greatly expand economic opportunity for ordinary Africans, and that only a set of alternative development finance mechanisms would greatly expand economic opportunity for ordinary Africans.

I take three things away as I finish the book: its indictment of the aid system is its most convincing and least original contribution; its proposed alternative to the aid system is the most original and least convincing. For these two reasons the book's principal importance derives—appropriately—not from what is written therein, but from who wrote it. I will explain each of these points.

First, the book executes a stinging airstrike on several myths and profound flaws of the aid system. These accusations are generally accurate in some measure, well supported, and valuable. I'll list just a few. Donors never had much basis for applying lessons from the Marshall Plan's successes in reconstructing rich Europe to transforming a poor continent. Donors have frequently failed to contrive aid mechanisms that accurately and credibly punish failure in effective delivery, or reliably limit aid to corrupt regimes. The latest debt crisis was less a sign of donors' lack of the altruistic mettle to forgive debt than it was a sign that earlier rounds of debt forgiveness failed to touch the fundamental problem. Motivating aid through guilt and glamour is incompatible with fostering rigorous accountability for results. The aid industry has a clear incentive to portray Africa as helpless and needy, an image directly deleterious to efforts to attract private investment.

These missiles are, unfortunately, on target. They are not original, of course: these points have been made before and very well in widely read books, as Moyo points out, by the likes of Peter Bauer, William Easterly, Nicolas van de Walle, Eberhard Reusse, David Sogge, and many others. So their value here lies in loudly reminding the world that many issues often left out of polite conversation remain unresolved—and deserve fresh urgency.

Second, the book proposes four alternative ways to finance development in Africa. Here it becomes a fresh and provocative brainstorm. But the book stumbles as a policy blueprint because it does not come close to offering sufficient evidence that the sweeping changes it recommends in finance mechanisms will greatly improve development outcomes. If it is right, it does not show that it is.

- Moyo suggests that more African countries and businesses should acquire bond ratings and tap private bond markets. Readers don't hear that many small and poor African countries—including Benin, Mali, and Malawi—already have sovereign ratings from Fitch or Standard & Poor's (ratings that were paid for by, ahem, donor agencies, as Todd Moss has observed). Furthermore, it is not well established that large waves of private capital are unleashed simply by the advent of a bond rating. Dilip Ratha's research has suggested that most of the variance in ratings for unrated countries can be easily predicted with existing, freely available information about those countries, so it is unclear that a rating itself tells investors a great deal that they don't already know. And one of the two successes the book showcases for successfully attracting large-scale bond finance—Gabon (p. 93)—unfortunately ranks at the bottom 12 percent of earth's nations for "control of corruption" according to the World Bank's *Governance Matters* project. This just doesn't fit the book's rigid thesis that "aid *is* the problem" and that other forms of finance solve "the problem."
- *Dead Aid* praises the Chinese government for its promotion of foreign direct investment (FDI) in Africa, suggesting that other donors should follow suit but that their aid deters FDI. Readers would be right to reflect on Moyo's evidence that 78 percent of Tanzanians see China's influence as beneficial while just 36 percent see the United States this way. But all the laurels for China distract us by raising other questions: Why won't the large aid flows from China accompanying Chinese FDI do the same ostensible harm of other aid? And if Western aid has deterred Western FDI, why hasn't it deterred Chinese FDI? A better discussion would have focused on

what limited successes and major challenges have been met in the long experience of attempts to encourage FDI, such as those of the Multilateral Investment Guarantee Agency or the U.S. Overseas Private Investment Corporation.

- Moyo recommends that donor countries stop hurting African exports by, among other things, reducing their lavish subsidies on agricultural products like cotton and sugar. This is commendable, but the evidence is very weak that reducing remaining trade barriers will have a big bang in Africa. Nancy Birdsall, Dani Rodrik, and Arvind Subramanian have pointed out that the 1994 currency devaluation in 14 African countries—which immediately doubled the domestic value of all exports—accomplished little sustainable poverty reduction for West African cotton farmers.
- Finally, Moyo recommends mobilizing Africans' own capital—such as by expanding microcredit and by making international workers' remittances cheaper to send. These plausibly good financing ideas deserve more attention, but again it is unclear how much they can improve development outcomes. Jonathan Morduch and David Roodman have rigorously shown that despite the rock-star status of microcredit in development circles, evidence on the magnitude of its antipoverty effects remains oddly scarce. And shaving some percentage points off the cost of sending remittances will have limited effect on remittance flows until countries let more Africans move—such as if the Economic Community of West African States actually implements its *de jure* protocols for free labor mobility, or if rich donor countries expand opportunities for Africans to work there temporarily.

There are nevertheless bright spots in the book's recommendations: more "collective bond" issues could raise capital for multiple small countries, while pooling risk and lowering transaction barriers, following South Africa's new Pan-African Infrastructure Development Fund. Much more attention should go to providing the basic infrastructure Africa requires for international integration, such as the construction and maintenance of key roads and power lines.

What these bright spots have in common is that they speak directly to sub-Saharan Africa's fundamental development challenge: that an economy much smaller in dollar terms than that of the American city of Chicago has been shattered into 48 separate countries. Chicago's economy would never overcome such a fate without bold financial and other mechanisms for its neighborhoods to work together. Collective bonds, roads, and migration work in this direction for Africa.

"The book is weakened substantially by several statements much too strong for the evidence to justify."

The book is weakened substantially by several statements much too strong for the evidence to justify. Its steely insistence that aid "guarantees economic failure" is difficult to reconcile with the fact that many African countries with well over 10 percent of GDP in aid have shown strong real growth over the past decade, including Ghana, Tanzania, Mali, Burkina Faso, Mozambique, and Uganda. As many reviewers have noted, the book needed a better fact checker and contains numerous unfortunate mistakes: It claims for example that "donors' African aid purse is slowly shrinking," whereas the Organization for Economic Cooperation and Development reports that aid flows to sub-Saharan Africa nearly doubled between 1997 and 2007, from $32 billion to $58 billion.

Third, despite its substantial limitations, one reason for which the book deserves attention is that it was written by an African. This observation is hard to debate—indeed, it is trumpeted in the first sentence of the book's own foreword by academic heavyweight Niall Ferguson. Like Kwame Nkrumah's *Africa Must Unite* a half-century ago, *Dead Aid* profoundly and effectively indicts the failures of the current international system to promote development in Africa. Also like Nkrumah, Moyo channels a very real and widely held frustration among Africans about their treatment by the West even if she stumbles on the specific alternatives she proposes to the troubled policies of the past. But most important, Nkrumah's and Moyo's books remain valuable because they get the biggest picture right: African development is mostly in the hands of Africans, outsiders' attempts to foster it face inherent limitations, and these observations are most persuasive when made by an African.

One of the most interesting issues the book raises, then, must be one that stands apart from how to finance African development: Why does the West see so few thoughtful, critical analyses of aid and development written and spoken by Africans? These most certainly exist—including work by Benno Ndulu, Agustin Fosu, Ngozi Okonjo-Iweala, Andrew Mwenda, and many others—but they are too few and they are not widely heard in the West. Perhaps demand is limited: Western agencies and editors prefer Western authors. Perhaps supply is limited: sharp Africans seeking the best careers hesitate to criticize donor agencies that will be their funders or clients. Perhaps there are many other reasons.

What is clear is that more African voices must be heard on these momentous issues. This year, the Hewlett and the Bill & Melinda Gates Foundations unveiled a large-scale program to support 24 policy think tanks throughout Africa—a major step forward in breaking down the barriers between Africans' development ideas and the world. I hope that the critical thinking they cultivate will contribute to a greatly expanded role for Africans in this vital debate.

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Low bar's tough patrons

Eduard Brau and Ian McDonald, editors

Successes of the International Monetary Fund

Untold Stories of Cooperation at Work

Palgrave Macmillan, New York, 2009, 231 pp., $34.95 (paper).

THIS is an informative and useful collection of essays by International Monetary Fund (IMF) staff and associated commentaries by interested observers. The collection provides more fodder for supporters of the IMF than for detractors either on the left, who argue that the IMF is too harsh in its policy prescriptions, or on the right, who argue that the IMF is too lenient or misguided in its policy prescriptions.

The book's six case studies of IMF financial assistance are of Korea 1998, Poland 1990–91, Turkey 2001–02, Tanzania 1995–2007, Brazil 2002, and Uruguay 2002–03. Each chapter includes a comment by someone who was either involved or a close observer of the program or activity. The commentaries add value, but they are not full-blown, objective critiques. In the interests of full disclosure, I was a participant in, or close observer of, four of the six country cases (excluding Tanzania and Uruguay) and all of the activities.

The principal value in these six essays is their focus on key decisions made by the authorities of the countries and the IMF. In five of the six cases, the episode described came at the end of an often protracted and less-than-successful sequence of programs and interactions between the country and the IMF. The authors do not fully acknowledge this fact in every case. The principal exception is the Uruguay case, though the transition program for Poland might also qualify. I was also struck by an irony in the Tanzanian case study. The IMF is credited both for advancing $400 million in financial support during 1995–2005 and for forgiving Tanzania's remaining debt to the Fund in 2006.

Three essays on other IMF activities are largely descriptive, which does not detract from their overall usefulness for those who did not live through or do not remember clearly the events of the 1990s. The essay on the IMF staff's *World Economic Outlooks* usefully provides a longer history starting in 1980. However, it is more self-congratulatory than the other essays and less convincing as a result. Taken as a group, the case studies illustrate the wide variety of economic, financial, and political issues that arise with programs that receive financial support from the IMF. A reader would be hard-pressed to sustain the view that the IMF uses a cookie cutter to design programs receiving Fund support.

The essays force the reader to think about the meaning of "success" for an IMF program. The editors define IMF success as making "a significant positive contribution," which is a relatively low bar, and also speculate about the counterfactual to IMF financial support. In the absence of such support, the immediate economic and financial consequences for the country, probably its neighbors, and possibly the world would have been more adverse. They raise the possibility that some countries alternatively might have received financial support from friends and allies, but without the policy reforms that produced overall success.

Implicit in the essays and commentaries, and occasionally explicit, is a second test of the IMF's success: could the policy advice from the IMF have been better? In almost all cases, the answer is yes, as is often noted by the authors, notably in the Uruguay case, but that is too harsh a test for judging any crisis response.

The overwhelming message of these six case studies is the importance of "ownership." The program belonged to the authorities of the country, and they fought to shape and own its content. The exception to this pattern is Korea, where public opinion still views the episode as the "IMF crisis" not Korea's crisis. However, even in this case, until the new Korean government owned its program, financial authorities in other countries were unwilling to pour more financing through the IMF into Korea and out the back door to foreign creditors.

The book's message about the IMF in the current global economic and financial crisis, drawn in particular from the Brazilian and Uruguayan cases, is the importance of an IMF that is flexible, is prepared to take risks, and is equipped financially to respond on a scale appropriate to country needs and circumstances.

On IMF reform, messages in this volume are somewhat more discouraging. The half-essay by Tom Dawson reminds readers that the country members of the Fund control IMF transparency and accountability. For example, the members ultimately determine rules governing release of Executive Board documents as well as what the IMF publishes, in large part, about their countries. Similarly, Charles Enoch, in his half-essay on country transparency, notes that since the establishment of the Special Data Dissemination Standard in 1999, members have been reluctant to raise the bar further in this area.

On the whole, the authors may have pulled a few of their punches, but they provide the serious student of the evolution of the IMF with thoughtful insights into this central global institution.

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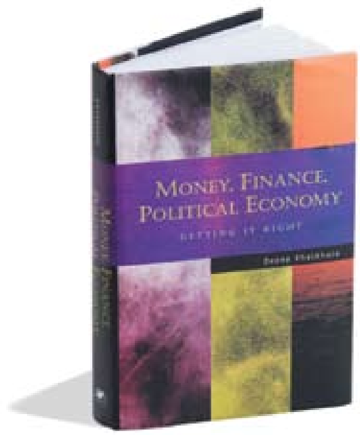
Ahead of his time



Deena Khatkhate

Money, Finance and Political Economy

Getting It Right

Academic Foundation, New Delhi, 2009, 385 pp., $39.95 (cloth).

"LIFE is lived forwards but understood backwards," wrote the philosopher Kierkegaard. This collection of a lifetime's work of the Indian economist Deena Khatkhate can be understood as an act of rebellion against much of his intellectual inheritance: socialism and central planning, Keynesian macroeconomics, and an adversarial view of North-South relationships. Instead, these essays put forward a spirited (but not uncritical) defense of capitalism and markets, espouse a macroeconomics as much Friedmanite as Keynesian, and urge a constructive approach to relationships between developing and advanced nations.

The last of these themes is illustrated in arguably the best article in the collection, which is on the brain drain—the emigration of skilled workers from developing to advanced countries. In this article, published in *F&D* in 1971, Khatkhate challenged the prevalent view of the brain drain as an evil, a form of aid from the poor to the rich. He showed that because most emigration occurred from developing countries with a clear excess supply of skilled workers, it was actually a social safety valve for the poor countries. And because it encouraged the "cross fertilization of ideas" between skilled workers from the poor nations and the richer nations, the brain drain could be "a desirable investment."

There are examples of this prediction coming to pass, such as the success of software exports from countries like India, Ireland, and Israel to more advanced nations. Ashish Arora, a professor at Carnegie Mellon University, has shown that this success is due in part to "the reserve army of underemployed engineers and scientists in these countries [that] had previously migrated to the United States and the United Kingdom." Through their work abroad, this diaspora gained experience with the business practices of their future customers—an earlier brain drain had turned into a brain gain, as Khatkhate predicted.

Other essays on North-South relationships in the book include one on "conflict and cooperation in the international monetary system." Written in 1987, it anticipates many reforms of the IMF and other international agencies—such as giving "greater voice" to the South in decision making—that have taken place or have come to the front of the agenda. To be sure, Khatkhate was one of many making similar suggestions. But, as he notes in the preface, he "received some flak" for this article since he was employed at the IMF at the time. In any event, Khatkhate soon left the IMF, after two decades of service, and went on to become editor of *World Development*, a scholarly journal.

Prior to joining the IMF, Khatkhate worked for over a decade—from 1955 to 1968—at the Reserve Bank of India, the country's central bank. Not surprisingly, therefore, a second major theme of the essays is the role of macroeconomic and financial policies in promoting economic growth. In the 1950s, the Keynesian view advocated running fiscal deficits to promote growth in developing countries. The rationale was that since there were underemployed resources in these economies, heavy government spending could lead to employment of those resources without triggering inflation. However, Khatkhate writes that

"These essays put forward a spirited (but not uncritical) defense of capitalism and markets."

the negative evidence on the actual impact of government spending convinced him that "all that happened as a result of heavy resort to fiscal deficit was inflation, decline in income, saving and investment." Khatkhate's views on monetary policy also differed from the 1960s Keynesian view, emphasizing as they did the need for rules to guide the central bank rather than give it too much discretion.

A third theme is the rhetoric vs. the reality of socialism and central planning. Khatkhate blamed socialism for trying to deliver both growth and equity and delivering neither. The real problem in developing countries, he said, was not so much the skewed income distribution but "improving the standard of the whole mass of people, which is possible only with rapid economic growth." These views were far from the mainstream when Khatkhate wrote them in 1978. He is not, however, an unvarying defender of capitalism and free markets. On the free mobility of capital, for instance, his views are close to that of his compatriot Jagdish Bhagwati in favoring a cautious approach, given the evidence that hasty liberalization can contribute to financial crises.

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