House of Commons

International Development Committee

FINANCING FOR DEVELOPMENT: FINDING THE MONEY TO ELIMINATE WORLD POVERTY

Fifth Report of Session 2001–02

Volume I

HC 785–I

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Footnotes
In the footnotes of this Report, references to oral evidence are indicated by 'Q' followed by the question number. References to written evidence are indicated by the page number as in 'Ev 12'. The oral and written evidence is published separately in Volume II (HC 785-II)

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FIFTH REPORT

The International Development Committee has agreed to the following Report:

FINANCING FOR DEVELOPMENT: FINDING THE MONEY TO ELIMINATE WORLD POVERTY

SUMMARY

Meeting the Millennium Development Goals (MDGs) will require an additional US$50 billion in aid per year, a doubling of current aid levels. The United Nations Conference on Financing for Development—the "Monterrey Summit"—took place from March 18–22. The aim of the Monterrey Summit was not solely to increase aid; rather it was to mobilise, and increase the effective use of financial resources in order to meet the MDG targets.

The most dramatic outcomes of the summit process were the aid increases announced by the EU and the USA which total an extra US$12 billion per year. This is less than a quarter of the funds needed to meet the MDG targets. Nevertheless, we welcome these increases as steps in the right direction.

This report examines financing for development as part of an emerging global new deal, looking at the conference preparations and outcomes, and at a range of issues which were discussed, including innovative sources of finance, aid, trade and debt relief.

Our conclusions and recommendations include:

- Trade-related policies including the EU's Common Agricultural Policy must be reformed, and debt-relief processes improved, so that developing countries are able to earn and retain the resources they need to meet the MDG targets;

- Proposals for innovative sources of finance—including currency transactions taxes, special drawing rights, and an international development trust fund—merit further consideration. But they must not distract attention from the need for Governments to finance development directly;

- Aid is the only resource that can be focussed exclusively on poverty reduction. We warmly welcome the recently announced increase in UK aid, which by 2006 will take the UK's aid contributions to 0.4 percent of Gross National Income. Nevertheless, we call on the Government to set a timetable for meeting its longstanding 0.7 percent commitment;

- Aid donors and recipients must work together to improve the effectiveness of aid. Recipients must commit themselves to poverty reduction and good governance. Donors must provide sufficient, timely and quality aid, invested carefully and sensitively so as to encourage local ownership;

- The UK Government must do its utmost to ensure that the emerging global development partnership is a balanced partnership characterised by transparency, fairness, mutual accountability, and the equitable sharing of financial burdens. Continuing efforts should be made also to ensure that the USA focuses its Millennium Challenge Accounts on poverty reduction and meeting the MDG targets.

The Chancellor told us that his aim was to ensure that "no country genuinely committed to good governance, economic development and poverty reduction, and to the opening up of trade and investment, is denied the chance to achieve the 2015 goals through lack of resources". This is a fine aim. It implies that significantly more aid will go to those

countries which use it effectively to reduce poverty. The Government should make the case for aid and international development even more strongly than it already does, in international fora, to its EU partners, and to the electorate. Now is the time for action to implement the agreements reached and reiterated at Monterrey, and to make the global new deal a reality.

Background and Acknowledgements

The UN Conference on Financing for Development was held in Monterrey, Mexico, from 18 to 22 March 2002. On 6 February the Committee announced an inquiry to take place at the conclusion of the conference, in order to examine the conference process and outcomes, and to investigate issues on the Financing for Development agenda. We received twenty-two written memoranda from a range of organisations with interests, expertise, and experience in this area, and held three evidence sessions at Westminster.

We are grateful to all the people and organisations who gave evidence to the inquiry, and to those who assisted us in other ways. We would like to thank especially the following people who gave oral evidence: the Rt Hon Gordon Brown, Chancellor of the Exchequer; the Rt Hon Clare Short, Secretary of State for International Development; Barrie Ireton, Department for International Development; Gus O'Donnell, HM Treasury; Belen Vazquez of Action Aid; Jenny Ross of British Overseas NGOs for Development; Tony German and Judith Randel of Development Initiatives; Simon Maxwell and John Roberts of the Overseas Development Institute; Professor Paul Mosley of the University of Sheffield; Steve Tibbett of War on Want; and Professor Paul Bernd Spahn of Goethe University, Frankfurt.

I. INTRODUCTION: TOWARDS A GLOBAL NEW DEAL?

1. One in five of the world's population live in extreme poverty, surviving on less than US$1 per day; nearly half of the world lives on less than US$2 per day.[1] At the United Nations (UN) Millennium Summit in September 2000, the international community—represented by the largest ever gathering of heads of state and government—committed itself to achieving the Millennium Development Goals (MDGs), promising that, "we will spare no effort to free our fellow men, women, and children from the abject and dehumanizing conditions of extreme poverty to which more than a billion of them are currently subjected".[2] The Prime Minister has made international development, especially in Africa, the poorest continent, a foreign policy priority for the Parliament. He described the state of Africa as "a scar on the conscience of the world" and, supporting the New Partnership for Africa's Development (NEPAD), pledged, "on our side: provide more aid, untied to trade; write off debt; help with good governance and infrastructure; training to the soldiers, with UN blessing, in conflict resolution; encouraging investment; and access to our markets so that we practice the free trade we are so fond of preaching."[3] There is indeed a cross-party consensus on these issues. The Chancellor of the Exchequer, Gordon Brown, reiterated the UK's commitment to the MDGs, stating that the aim was to "build a virtuous circle of debt relief, poverty reduction and sustainable development, in order that no country genuinely committed to good governance, economic development and poverty reduction, and to the opening up of trade and investment, is denied the chance to achieve the 2015 goals through lack of resources".[4] It is vital that the Chancellor, the Government, and the international community, translate these fine words into action, and soon.

2. The MDGs crystallise commitments made at a series of UN conferences, and encompass specific time-bound targets—for instance, to halve, between 1990 and 2015, the proportion of people whose income is less than US$1 per day—and measurable indicators to assess progress.[5] The MDGs provide the focus for concerted international efforts to eliminate poverty and facilitate development, a focus around which a consensus has been built, a consensus which is unprecedented and vital if there is to be any chance of reaching the MDG targets.

3. In contrast to promises made at many global summits, the Millennium Declaration recognised financing for development as a key component of achieving the development targets, and highlighted the need to mobilise substantial financial resources. The cost of achieving the MDG targets—an achievement which would still leave nearly a billion people living on under US$1 per day—has been estimated at around US$50 billion of additional development assistance per year every year from 2001 to 2015, a figure which takes no account of the pressing needs for humanitarian assistance (US$3–4 billion extra per year), or for global public goods such as peacekeeping, action to combat HIV/AIDS, agricultural research, measures to reduce greenhouse gases and to preserve biodiversity (US$15 billion extra per year).[6] An additional US$50 billion per year equates to a doubling of current aid[7] levels, an increase in the aid given by the OECD donor countries from 0.22 percent to 0.44 percent of their Gross National Income (GNI).[8] The African Development

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[1] These World Bank measures are based on 1993 Purchasing Power Parity terms. This allows cross-country comparisons to be made, and progress to be charted over time.

[2] United Nations Millennium Declaration, September 2000.

[3] Prime Minister's speech to the Labour Party Conference, September 2001.

[4] Q99

[5] See—http://www.developmentgoals.org/

[6] These are the estimates cited in the Zedillo Report, a report of the UN high-level panel on Financing for Development. See—http://www.un.org/esa/ffd/a55–1000.pdf. The World Bank's estimate of the cost of meeting the MDG targets is US$40–60 billion; Oxfam's estimate is US$100 billion.

[7] "Aid" refers to Official Development Assistance (ODA) to developing countries as defined by the OECD donors' Development Assistance Committee (DAC).

[8] If the OECD/ DAC donors had, in 2000, reached the 32 year-old UN-endorsed target of contributing 0.7 percent of their gross national income to aid, official development assistance would have been US$168.6 billion.

Bank estimates that an extra US$20–25 billion per year would be needed to enable those African countries which it judges to be in a position to use aid effectively, to reach the MDGs.[9] Most of the MDG targets have deadlines of 2015, a mere 13 years away. On current trends, there will be a massive shortfall of resources and, especially in Africa,[10] the targets will not be met. Avoidable poverty, ill-health, and death will be the consequences for hundreds of millions of the world's poor.[11] More resources, and more effective use of resources, must be priorities. If the international community does not act now, it will be too late.

4. The UN Conference on Financing for Development—the "Monterrey Summit"—took place from 18 to 22 March 2002, in Monterrey, Mexico. The aim of the conference, as expressed in the Monterrey Consensus, was to mobilise, and to increase the effective use of financial resources in order to meet the MDG targets.[12] These dual aims—more resources and more effective use of resources—reflect the emerging framework for international cooperation to eliminate poverty. This framework is one of global partnership, or, as the Chancellor described it, a "global new deal" establishing a new relationship between developed and developing countries.[13] The deal is that, "in return for developing countries pursuing corruption-free, pro-stability, pro-investment and pro-trade policies, developed countries should substantially increase the development aid they are prepared to offer in the run-up to 2015".[14] As the United Nations Development Programme (UNDP) put it in their written evidence, the "MDGs provide a benchmark against which the performance of development partners can be measured, and progress towards the achievement of internationally agreed targets of development cooperation assessed".[15]

5. This report examines Financing for Development—the conference process, the conference outcomes, and a range of issues and proposals which came up during the Financing for Development process—as a key component of an emerging global new deal. In chapter two we examine the Financing for Development conference itself, from the preparatory processes to the Monterrey Consensus and the conference outcomes. In chapter three we describe the big picture of international resource flows, setting the scene for subsequent chapters with their specific foci. In chapter four our attention turns to proposals for innovative sources of finance, including Currency Transactions Taxes, Special Drawing Rights, and the Chancellor's proposal for an International Development Trust Fund, before we examine aid—a more traditional source of development finance—in chapters five and six. Our focus is on aid volumes in chapter five, and on aid effectiveness in chapter six. International development partnerships and burden-sharing are addressed in chapter seven. In conclusion, we emphasise the importance of political leadership in making the case for aid and for international development both domestically and internationally.

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[9] Achieving the MDGs in Africa: Progress, prospects, and policy implications, African Development Bank, June 2002. See http://www.afdb.org/knowledge/publications/pdf/global_poverty_report_jun2002.pdf

[10] The MDGs in Africa: Promises and progress, UNDP and UNICEF, June 2002. See—http://www.undp.org/mdg/mdgreportinafrica.pdf

[11] Last chance in Monterrey: Meeting the challenge of poverty reduction, Oxfam Briefing Paper no. 17, 13 March 2002. See—http://www.oxfam.org.uk/policy/papers/monterrey/monterrey.pdf

[12] UN Conference on Financing for Development, Monterrey Consensus Document. See-—http://www.un.org/esa/ffd/0302finalMonterreyConsensus.pdf

[13] Q130; and, Tackling poverty: A global new deal—A modern Marshall plan for the developing world, HM Treasury, February 2002. See—http://www.hm-treasury.gov.uk/mediastore/otherfiles/ACF711.pdf

[14] Q99

[15] Ev 109

Figure 1: The Millennium Development Goals, including targets and indicators

Goals and Targets	Indicators
Goal 1: Eradicate extreme poverty and hunger	
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day	**1.** Proportion of population below $1 per day **2.** Poverty gap ratio **3.** Share of poorest quintile in national consumption
Target 2: Halve, between 1990 and 2015, the proportion of people who suffer from hunger	**4.** Prevalence of underweight children (under-five years of age) **5.** Proportion of population below minimum level of dietary energy consumption
Goal 2: Achieve universal primary education	
Target 3: Ensure that, by 2015, children everywhere will be able to complete a full course of primary schooling	**6.** Net enrolment ratio in primary education **7.** Proportion of pupils starting grade 1 who reach grade 5 **8.** Literacy rate of 15–24 year olds
Goal 3: Promote gender equality and empower women	
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education no later than 2015	**9.** Ratio of girls to boys in primary, secondary and tertiary education **10.** Ratio of literate females to males of 15–24 year olds **11.** Share of women in wage employment in the nonagricultural sector **12.** Proportion of seats held by women in national parliament
Goal 4: Reduce child mortality	
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate	**13.** Under-five mortality rate **14.** Infant mortality rate **15.** Proportion of 1 year olds immunised against measles
Goal 5: Improve maternal health	
Target 6: Reduce by 75%, between 1990 and 2015, the maternal mortality ratio	**16.** Maternal mortality ratio **17.** Proportion of births attended by skilled health personnel
Goal 6: Combat HIV/AIDS, malaria and other diseases	
Target 7: Have halted by 2015, and begun to reverse, the spread of HIV/AIDS	**18.** HIV prevalence among 15–24 year old pregnant women **19.** Contraceptive prevalence rate **20.** Number of children orphaned by HIV/AIDS
Target 8: Have halted by 2015, and begun to reverse, the incidence of malaria and other major diseases	**21.** Prevalence and death rates associated with malaria **22.** Proportion of population in malaria risk areas using effective malaria prevention and treatment measures **23.** Prevalence and death rates associated with tuberculosis **24.** Proportion of TB cases detected and cured under DOTS (Directly Observed Treatment Short Course)

Goal 7: Ensure environmental sustainability	
Target 9: Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources	**25.** Proportion of land area covered by forest **26.** Land area protected to maintain biological diversity **27.** GDP per unit of energy use (as proxy for energy efficiency) **28.** Carbon dioxide emissions (per capita)
Target 10: Halve, by 2015, the proportion of people without sustainable access to safe drinking water	**29.** Proportion of population with sustainable access to an improved water source
Target 11: By 2020, to have achieved a significant improvement in the lives of at least 100 million slum dwellers	**30.** Proportion of people with access to improved sanitation **31.** Proportion of people with access to secure tenure
Goal 8: Develop a Global Partnership for Development	
Target 12: Develop further an open, rule-based, predictable, non-discriminatory trading and financial system **Target 13:** Address the Special Needs of the Least Developed Countries Includes: tariff and quota free access for LDC exports; enhanced programme of debt relief for HIPC and cancellation of official bilateral debt; and more generous ODA for countries committed to poverty reduction **Target 14:** Address the Special Needs of landlocked countries and small island developing states (through Barbados Programme and 22nd General Assembly provisions) **Target 15:** Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term	*Official Development Assistance* **32.** Net ODA as percentage of DAC donors' GNI [targets of 0.7% in total and 0.15% for LDCs] **33.** Proportion of ODA to basic social services **34.** Proportion of ODA that is untied **35.** Proportion of ODA for environment in small island developing states **36.** Proportion of ODA for transport sector in land-locked countries *Market Access* **37.** Proportion of exports (by value and excluding arms) admitted free of duties and quotas **38.** Average tariffs and quotas on agricultural products and textiles and clothing **39.** Domestic & export agricultural subsidies in OECD countries **40.** Proportion of ODA provided to help build trade capacity *Debt Sustainability* **41.** Proportion of official bilateral HIPC debt cancelled **42.** Debt service as a % of exports of goods and services **43.** Proportion of ODA provided as debt relief **44.** Number of countries reaching HIPC decision and completion points
Target 16: In co-operation with developing countries, develop and implement strategies for decent and productive work for youth	**45.** Unemployment rate of 15–24 year olds
Target 17: Cooperating with pharmaceutical companies, provide access to affordable, essential drugs in developing countries	**46.** Proportion of population with access to affordable essential drugs on a sustainable basis
Target 18: In co-operation with the private sector, make available the benefits of new technologies, especially information and communications	**47.** Telephone lines per 1000 people **48.** Personal computers per 1000 people

Source: United Nations Development Programme.

II. THE UN CONFERENCE ON FINANCING FOR DEVELOPMENT

The Preparatory Process

6. In response to demands from the G77 group of developing countries, the UN General Assembly agreed in June 1997 to consider holding an intergovernmental dialogue on the financing of development. The first substantive session of the Preparatory Committee—a "Prepcom" in the language of international conferences—took place in May/June 2000, and the fourth and final Prepcom was held in New York from 14 to 27 January 2002. There were in addition numerous regional meetings, and discussions between the various international organisations and other key stakeholders such as civil society and business interests. The final Prepcom completed the Monterrey Consensus Document for heads of state to endorse two months later at the Monterrey Summit.

7. One feature of the preparatory process, highlighted particularly in the memoranda received from UNDP,[16] and jointly from the Department for International Development (DFID) and HM Treasury,[17] was the participation of business interests and civil society organisations throughout the process. In contrast, other witnesses including British Overseas NGOs for Development (BOND) reported that civil society organisations had not been able to participate effectively either in the preparatory process or in the "roundtables" at Monterrey when they were given very little time and were unable to influence a pre-decided outcome.[18] As we discovered, NGOs had, in part, ruled themselves out of the Financing for Development (FfD) process having decided that they would not be able to exert much influence. As BOND wrote, "NGO involvement in [the] FfD preparatory process was modest. The broad nature of the agenda was often beyond the remit of individual NGOs and coordination of efforts took place both at the UK and the EU level to maximise impact. Many heavyweight NGOs and NGO networks decided early not to invest in the FfD process assuming their views would have little chance of influencing the official proceedings; furthermore, the usual lack of resources hampered southern NGOs involvement".[19]

8. The Secretary of State for International Development, Clare Short, told us that "the preparatory process was very good and went well",[20] and in their joint memorandum DFID and HM Treasury claimed that "the significant participation of the IMF [International Monetary Fund] and the World Bank meant that this was a good example of the UN and the Bretton Woods institutions collaborating effectively towards shared objectives".[21] Improved coordination between the UN, the International Financial Institutions and the World Trade Organisation (WTO) was similarly applauded by UNDP[22] and the Overseas Development Institute (ODI),[23] although the World Development Movement (WDM) was more critical, arguing that "the FfD process clearly asserts the primacy of the international economic institutions over the UN system".[24] We understand these concerns about the relative weight and influence of the International Financial Institutions as opposed to the more democratic UN, but **we welcome the improved coordination between the various international organisations and feel that such efforts are crucial if there is to be policy coherence as regards international development. The appropriate response to greater coordination between the International Financial Institutions and the UN is to strengthen the voice of developing countries in all fora, rather than to decry such coordination.** Policy

[16] Ev 109
[17] Ev 78, para 1
[18] Ev 7 and Ev 8
[19] Ev 7; see also Q5 and Q13.
[20] Q99
[21] Ev 78, para 1
[22] Ev 109
[23] Ev 42
[24] Ev 111, para 4

coherence and the grounding of international cooperation in national-level politics would be improved too by the participation of parliamentarians in international conferences, something which—as seems to be the norm at international meetings—was lacking at Monterrey.

From the Zedillo Report to the Monterrey Consensus

9. In December 2000, as part of the conference preparations, the UN Secretary General appointed a panel to recommend strategies for the mobilisation of resources to finance development. This panel was headed by Ernesto Zedillo, the former President of Mexico, and published its report—the Zedillo Report[25]—on 26 June 2001. The Zedillo Report provided a basis for subsequent negotiations, and ultimately led to the Monterrey Consensus. The Zedillo report was wide-ranging, discussing issues including domestic resources, private capital flows, trade, aid, and the architecture of global governance. It was widely welcomed by NGOs and the wider international development community for imparting a sense of urgency to proceedings and for making it clear that the MDG targets would not be achieved if a "business as usual" approach were adopted. In addition to calling for a doubling of aid to US$100 billion, the report made a series of recommendations about: establishing attractive economic and business environments in developing countries; the need for the WTO to pursue a "development round" and to implement fully previous agreements; the need for donors to honour their commitments to provide aid amounting to 0.7 percent of their national income and to harmonise their development assistance; the importance of reforming the architecture of global governance; the desirability of international taxes and a new allocation of Special Drawing Rights to finance the provision of global public goods; and a proposal to establish an international tax organisation. For many NGOs including BOND[26] and WDM,[27] the Zedillo report was an exciting document full of innovative proposals, a document which provided a benchmark against which the Monterrey Consensus could be judged.

10. Given the political realities of relationships between developed and developing countries, and the need to ensure the continued participation of the USA in the process, it is not surprising that the Monterrey Consensus emphasises the responsibility of developing countries for their own development, and has a somewhat narrower agenda than the Zedillo report, expressed in less forthright language. Developed and developing countries insisted that some issues were best dealt with in other fora—trade in the WTO, and debt relief in the Heavily Indebted Poor Countries (HIPC) initiative—with the result that more attention was focussed on aid volumes, and most especially aid effectiveness. BOND criticised the role of the USA in diluting the Zedillo report's recommendations, highlighting in particular its intransigent negotiating stance and obstructive negotiating tactics, and its efforts to exclude mention of either the 0.7 percent of GNI target, or the MDGs in the Monterrey Consensus.[28] We were also told that the EU reduced its ambitions for the process when at the third Prepcom its primary objective became that of keeping the USA on-board.[29]

11. The UK played an active role in the Financing for Development process. UK objectives were: to focus FfD on poverty elimination; to promote developing countries' efforts to create the right policy environment for poverty reduction; to press for significant increases in aid; to press for measures to increase aid effectiveness; and, to strengthen the voice of developing countries in the international financial architecture.[30] Speeches by the Chancellor of the Exchequer in November and December 2001 pushed international

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[25] Zedillo Report—see footnote 6 for web-site.
[26] Ev 5
[27] Ev 110, para 1
[28] Ev 7
[29] Q12
[30] Ev 78, para 2

development issues further up the international political agenda and highlighted the need for more and better use of finance for development. The UK was a key player in developing the common EU position and making the case for aid; as BOND put it, 'the UK appeared to be one of the more progressive voices' in the process.[31] Indeed, the UK has increased its ODA/GNI percentage contribution from 0.26 in 1997, to 0.32 in 2000, and is firmly committed to reaching 0.4 percent by 2006. Such progress is very welcome, and puts the UK in a stronger position to persuade other states to increase their contributions. If the UK were to set a timetable for reaching its 0.7 percent commitment, its position would be strengthened further. Despite the arguments made by the UK and other states at the conference, it is disappointing that the Monterrey Consensus lacks the sense of urgency of the Zedillo report, a sense of urgency which must be revived if there is to be any hope of meeting the MDG targets. **We commend the Government on its active role during the FfD process, and trust that it will endeavour to inject international discussions and actions to meet the MDGs with a sense of urgency.**

Aid Increases, Assessment, and Implementation

12. Whilst not part of the Monterrey Consensus, the most dramatic outcomes of the conference were the announcements by the EU and the USA of substantial increases in ODA. (ODA volumes are discussed in more detail in chapter five of this report). The EU announced on 15 March that—as an intermediate target en-route to meeting the 0.7 percent of GNI target—all member states would seek by 2006 to meet or exceed the current EU average of 0.33 percent of GNI. Assuming that the currently more generous donors maintain their current generosity, this would have the effect of pushing the EU average to 0.39 percent of GNI, providing an extra US$7 billion of aid per year from 2006 and raising an additional US$20 billion between now and 2006. On 14 March the USA announced that it would provide—through its Millennium Challenge Accounts (see also paragraphs 61 and 94–99)—an extra US$5 billion of aid per year from 2006, and an extra US$10 billion between now and 2006. Assuming that the announced increases in aid from the EU and the USA materialise, they would amount to an extra US$12 billion per year from 2006, a long way short of Zedillo's costing of an extra US$50 billion per year from 2001 for the MDG targets, but a step in the right direction. Made in the week before the conference commenced, the ODA announcements were clearly precipitated by the Monterrey process and the debate it generated about aid and international development. In our view this was one of the most important outcomes of Monterrey, pushing international development right to the top of the international political agenda, perhaps for the first time ever.

13. **But, being briefly on top of the international political agenda is not the same as being adequately resourced.** As the Chancellor of the Exchequer acknowledged in the Budget Report or "Red Book", the commitments to increase ODA fall short of raising the resources needed to meet the MDG targets.[32] Critics of the FfD process point out too: that Monterrey merely produced a reaffirmation of existing commitments;[33] that no binding commitments were made, or timetables set for reaching 0.7 percent;[34] that little progress was made on untying aid; that the Consensus entrenched a one-size fits all development model and failed to challenge the inequitable system of global governance;[35] and, perhaps most strongly, that in sacrificing the message of the Zedillo report in order to keep the USA on board Monterrey was a "failure of multilateralism".[36] **We share some of this disappointment, but are keen to maintain the momentum gained at Monterrey rather than dwell on what might have been.**

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[31] Ev 6
[32] Budget Report "Red Book", 2002, p.107.
[33] Ev 1
[34] Ev 8
[35] Ev 113, para 20, Ev 110, para 3 and Ev 111, para 4
[36] Ev 68

14. Whilst developing countries and many NGOs were understandably disappointed with the Monterrey outcomes,[37] and regarded the process as excessively donor-driven,[38] the achievement of a consensus was no mean feat. As ODI put it:

> "A now obvious but important point about the long process of preparing for Monterrey is that a consensus was achieved. At the outset this was far from a foregone conclusion. There could, until the end, have been an unresolved confrontation between exaggerated expectations of developing countries for higher resource flows, more debt relief, a preponderant role for themselves in the international financial architecture and the construction of new institutions of world economic governance with authority over macroeconomic policy and international investment on the one hand, and defensive and negative attitudes on the part of developed countries on all these issues on the other".[39]

Clare Short too told us that "Monterrey was very important, in that the developing world and the OECD countries agreed on what the reform agenda is to deliver to the poor of the world; that is unprecedented in human history, and very post cold war".[40] In addition—whilst conforming to the USA's demands and referring to "internationally agreed development goals" rather than to the MDGs—the Monterrey Consensus strengthened international commitment to the MDGs, and "became the first UN conference to achieve concrete and specific increases in ODA".[41] In summary, the UK Government's assessment was that, "The UN Conference on Financing for Development was a major success and potentially represents a turning point in the global fight against world poverty".[42]

15. **We warmly welcome the aid increases announced by the EU and the USA. But, the success of the summit must ultimately be assessed in terms of its contribution to meeting the MDG targets. As such, it is too early to judge the summit's success. Thus far, little has been achieved and nothing has been implemented. If the Monterrey Summit is to be seen as a turning point rather than a talking shop, the international community must implement quickly the agreements reached, and use them as a starting point for a concerted international effort to eliminate poverty.**

16. The next step is to make the forthcoming World Summit on Sustainable Development (WSSD) a success. Unfortunately, as WWF-UK made clear in its memorandum, the FfD process and the Monterrey Consensus lacked substantive links to the environmental and resource dimensions of sustainable development.[43] There is much work to do to bring the anti-poverty and pro-environment agendas together beneath the banner of sustainable development. Indeed, the failure of the Bali preparatory conference to agree on a clear agenda for Johannesburg, suggests to us that WSSD will be hard-pressed to make much progress in terms of promoting sustainable development and poverty elimination. DFID and HM Treasury wrote that: "It is now a matter of taking forward the agenda from Monterrey, at the UN and the Bretton Woods institutions, through the G7 Meetings in Halifax and G8 in Kananaskis, at the World Summit on Sustainable Development in Johannesburg and the Commonwealth Finance Ministers' Meeting in London".[44] We agree, and share with Clare Short the view that, "now, we have got to get WSSD right and then

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[37] Ev 48

[38] In its memorandum too, ODI described the Monterrey Consensus as reflecting "the mainstream of donor thinking on how to make development policy and development assistance effective in reducing poverty and achieving the Millennium Development Goals". However, for ODI this was a statement of fact rather than a criticism. See Ev 40.

[39] Ev 41

[40] Q99

[41] Ev 78, para 1

[42] *Ibid.*

[43] Ev 114. WWF is now the brand-name for organisations previously called either the World Wildlife Fund or the Worldwide Fund for Nature.

[44] Ev 79, para 11

drive the world into implementation and stop having so many conferences, and, if we have conferences, let us just check on delivery, rather than have any more grand declarations”.[45]

17. We welcome the Monterrey commitment to agree on a follow up conference by 2005, and trust that this will be about checking on delivery rather than merely re-affirming old commitments. In the remainder of this report our attention shifts to mechanisms—existing and proposed—for financing development, something which is crucial if the MDG targets are to be met.

[45] Q99

III. RESOURCE FLOWS: THE BIG PICTURE

18. Meeting the MDG targets will require substantial resource transfers from developed to developing countries; of this there can be no doubt. The real question is, which method of generating and transferring financial resources is most effective at reducing poverty? [46] The Financing for Development agenda ranged from domestic resource mobilisation, to foreign direct investment, debt relief, trade earnings, and aid. A single inquiry cannot deal comprehensively with all these issues, but, it is important that, in focussing on aid and the potential of innovative sources of development finance, we do not forget the bigger picture.

19. The ultimate aim of the FfD process was not to increase aid levels. It aimed, in line with the Millennium Declaration, to eradicate poverty, achieve sustained economic growth, and promote sustainable development. Aid is extremely important, but achieving the MDG targets will require progress on several fronts. Looking at the big picture of financial resource flows, we can distinguish between domestic resource mobilisation within developing countries, inflows into developing countries, and outflows from developing countries (see figure 2). It is the combination of these three elements which determines the resources which a country has to work with in its development.

Figure 2—Inflows, outflows and domestic resource mobilisation: A schematic diagram of financing for development

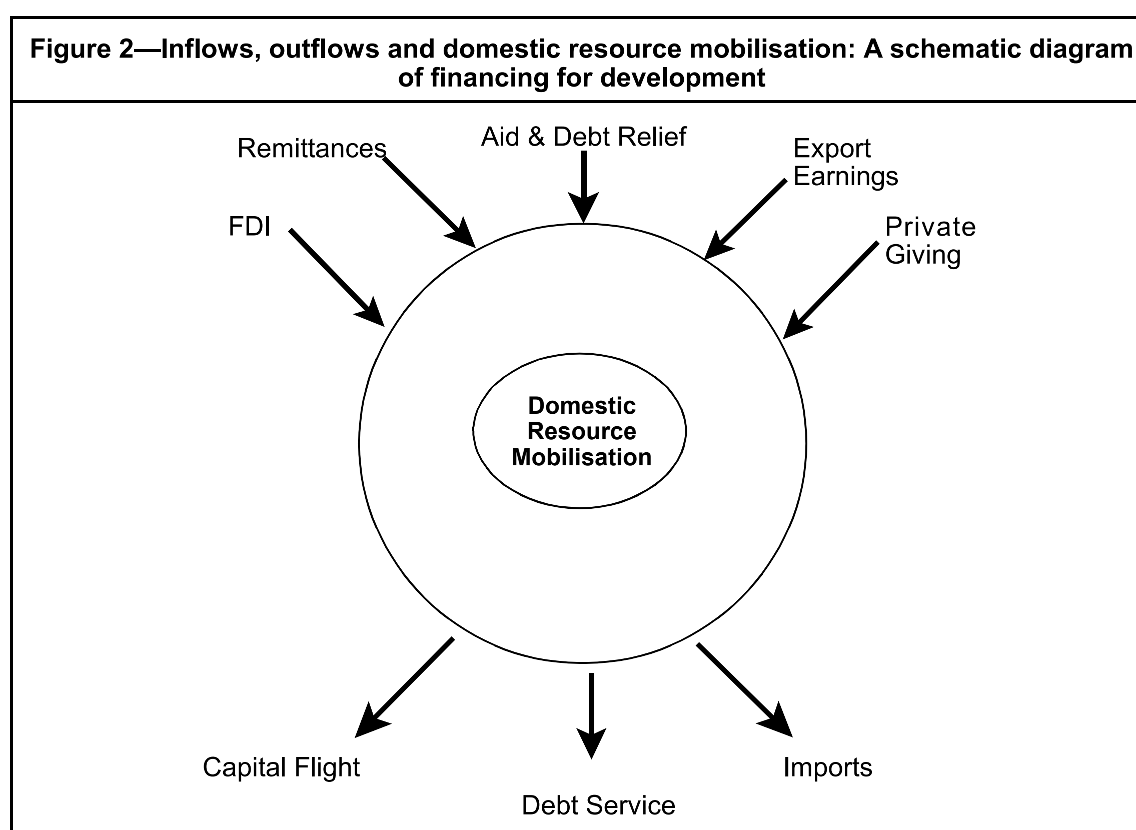

Diagram Source: Committee's own.

Domestic Resources and Responsibilities

20. The starting point of the Monterrey Consensus is the responsibility of countries for their own development, and the importance of domestic resource mobilisation. Domestic resource mobilisation refers primarily to public and private savings, taxation, and investment. As the Zedillo report put it "The domestic economy is virtually always the dominant *source* of savings for investment, and the domestic policy environment is a

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[46] Clearly the answer to this question will vary depending on a particular country's circumstances, but nonetheless the question's value remains. We acknowledge gratefully the help of Simon Maxwell, the Director of ODI, in formulating this question.

decisive determinant of the *desire* to invest. Furthermore, the equally crucial question of the *efficiency* with which resources are invested is determined overwhelmingly by national decisions and the domestic policy environment".[47] Such sentiments were strengthened in the Monterrey Consensus, with particular attention given to the importance of "good governance", "sound economic policies" and "solid democratic institutions" in mobilising and attracting resources.[48] We concur fully with these views; **if developing countries are to escape poverty they must take responsibility for their own development. Developing countries will need to establish policy environments, and local banking and financial systems, to both retain and mobilise domestic resources, and to attract and retain international resources.**[49]

21. As we noted in our report on Corruption,[50] and saw during our recent visit to Nigeria, corruption is the enemy of development. It will not be possible to reduce the present levels of poverty in developing countries unless corruption is controlled. For instance, Nigeria's growing poverty has coincided with the generation of huge wealth from oil and gas. In Angola too, many millions of people live in abject poverty whilst millions of pounds of oil and diamond revenues have been used to finance wars. In paragraph 27, we refer to the "staggering 39 percent" of African private wealth that is held abroad. **Developing countries must show that they are taking strong measures to tackle corruption and money laundering so that countries' resources benefit all the people rather than corrupt elites. Developed countries must rigorously enforce their own anti-corruption laws and insist that financial transactions by firms with developing countries are open and transparent.**

22. Getting the local institutional and policy environment right is likely to have significant multiplier effects in terms of mobilising both domestic and international capital. However, important as the national policy environment is, reliance on domestic resources will not enable developing countries to meet the MDG targets. DFID and HM Treasury told us that "It is only likely to be possible for developing countries to generate domestically a small share of the additional $50 billion of funds required to meet the MDG targets. The World Bank estimate that if poorly-performing countries raised their savings rates and efficiency of investment to the average levels achieved in countries with good policies, then this would reduce their funding requirements by some $7 billion (from $22 billion to $15 billion)".[51] Therefore, we must consider other resource flows too.

Inflows into Developing Countries: Trade, Investment, Remittances, Aid and Philanthropy

23. A quick look at the data reveals the magnitude and type of North-South flows of financial resources (see figure 3). On average, from 1996–2000, the total net flow of long-term financial resources from DAC donors[52] to developing countries and multilateral organisations was more than US$170 billion per year. The components of this total annual flow were: private flows at US$106.6 billion (62 percent); ODA at US$50.6 billion (30 percent); other official flows at US$7.6 billion (5 percent); and, net grants by NGOs at US$5.9 billion (3 percent).[53] The volume of private flows has been quite volatile, peaking within the 1996–2000 period at US$127 billion in 1997 and reaching a low of US$75 billion

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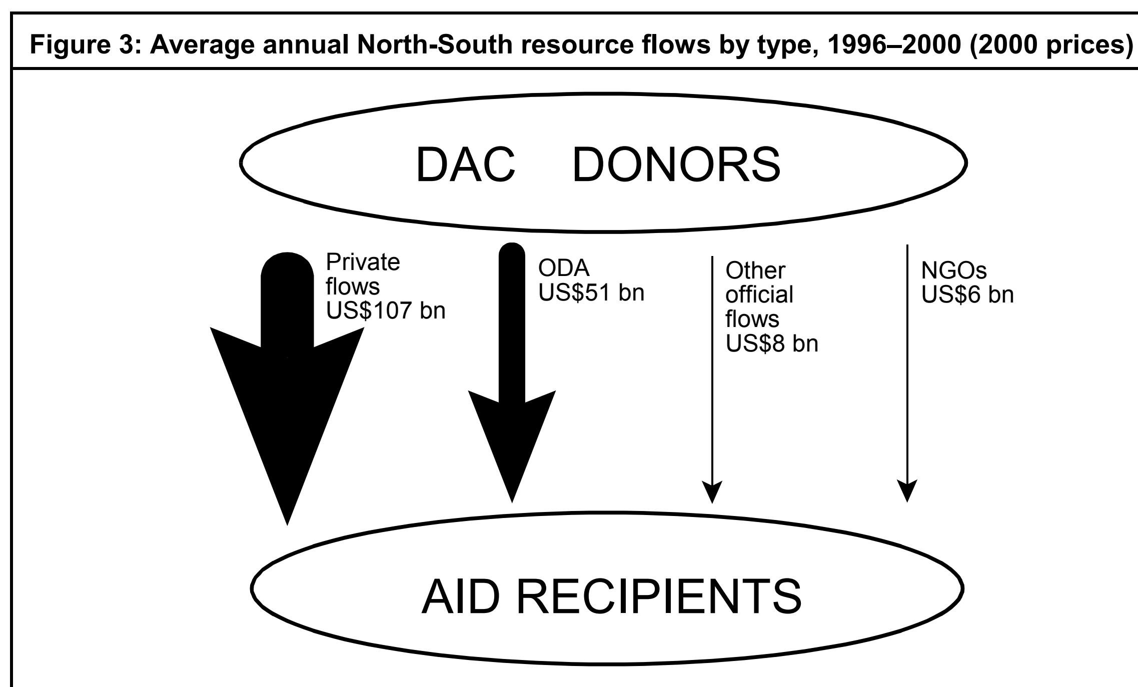
[47] Zedillo Report, pp.36–37.
[48] Monterrey Consensus, paragraph 11. See footnote 12 for web-site.
[49] The New Economics Foundation's report on "Chasing shadows" offers an interesting perspective on domestic resource mobilisation, suggesting that domestic saving is a key driver of growth.
See—http://www.neweconomics.org/uploadstore/pubs/Chasing%20shadows%20final.pdf
[50] Fourth Report from the International Development Committee, Session 2000–2001, *Corruption*, HC39-I .
[51] Ev 83, para 25
[52] The DAC donors are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, UK, USA.
[53] Data from OECD/DAC Development Cooperation Report 2001.

in 2000. The volume of ODA has been steady at around US$50 billion. Whilst aid is important, clearly, any consideration of financing for development must not exclude other flows of financial resources; the Monterrey Consensus reflects this point in its enthusiasm for trade and foreign direct investment as engines for development.

Figure 3: Average annual North-South resource flows by type, 1996–2000 (2000 prices)



Data Source: OECD International Development Statistics Online. Diagram Source: Committee's own.

24. The mix of resource flows differs, both by recipient and by donor country. (See figure 4 for a comparison of selected OECD/DAC countries). At Monterrey, Andrew Natsios, head of the United States Agency for International Development (USAID), emphasised that 80 percent of flows from the USA to developing countries are private, including investment, philanthropy, and remittances: the Gates Foundation spends more money in terms of health care in the developing world than any other donor country; remittances from the USA to developing countries amount to US$30 billion per year ;[54] and, private giving through US NGOs amounts to some US$4 billon per year.[55] Alan Larson, US Under Secretary of State for Economic, Business and Agricultural Affairs, reported that US imports from developing countries amount to some US$450 billion per year, and applauded the fact that US imports from sub-Saharan Africa increased by 17 percent in 2001 under the African Growth and Opportunity Act.[56] As the USA seems keen to emphasise, perhaps to deflect attention from its modest aid contribution, the apparent generosity of donor countries does differ depending on whether generosity is defined in terms of ODA as a percentage of GNI, or in terms of total resource flows as a percentage of GNI. Yet, the adoption of a broader definition of generosity only succeeds in lifting the USA from being the least generous of the DAC countries to a place fifth from bottom of the donor table, providing total resource flows which amount to 0.25 percent of GNI. Nevertheless the point remains: non-aid resource flows are important.

25. **Financing for development must be considered in the round; the focus should not be solely on aid. Non-aid flows of resources are crucial for developing countries' prospects of meeting the MDG targets.** In 2001, of the developing countries' total GNI

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[54] ODA: A key to global stability. Forum hosted by BOND/Interaction/Norwegian Forum/Action Aid during the Financing for Development Conference—copy placed in library.

[55] Ev 26

[56] Transcript of press conference given by Alan P. Larson, US Under Secretary of State for economic, business and agricultural affairs at the UN Conference on Financing for Development—copy placed in library.

of US$6389 billion, US$2176 billion or some 34 percent came from the export of goods and services. For sub-Saharan African countries, the figure was 40 percent—US$117 billion out of a total GNI of US$294 billion.[57] Clearly, trade earnings are a major inflow into developing countries, and could—particularly if we as developed countries were to practice what we preach, reducing subsidies and opening our markets to developing country exports—be a very powerful engine for development. Clare Short emphasised that making the Doha round of WTO negotiations a "development round" was part of the consensus reached at Monterrey, and lamented the fact that agricultural subsidies in OECD countries amount to US$360 billion per year. As she said: "if we do not give countries better trading opportunities they will not have the chance to grow their economy".[58]

Figure 4: North-South resource flows by type, selected country comparisons for 2000 (US$ billions, 2000 prices, except where stated otherwise)

	DAC	France	Nether-lands	Sweden	UK	USA
Official Development Assistance	53.737	4.105	3.135	1.799	4.501	9.955
ODA as % of GNI	0.22	0.32	0.84	0.8	0.32	0.1
Other Official Flows including Export Credits	-4.537[59]	0.014	0.038	NA	-0.072	0.562
Grants by Private Voluntary Agencies	6.935	NA	0.306	0.026	0.536	4.069
Private Flows at Market Terms (including FDI)	74.537	1.439	3.469	2.127	2.093	10.666
Total Long Term Resource Flows	130.673	5.557	6.947	3.952	7.058	25.252
Total Resource Flows as % of GNI	0.54	0.43	1.85	1.76	0.5	0.25

Data Source: OECD Development Co-operation Report 2001, Table 13.

26. The WTO calculates that abolishing OECD agricultural subsidies would provide developing countries with three times their current ODA receipts. Such issues are of particular importance at a time when the USA has passed legislation to increase its agricultural subsidies by some 80 percent, providing nearly US$200 billion of subsidies to its farmers over the next ten years under the new Farm Act, a move which will rob developing countries of export opportunities and potential trade earnings. Whilst this US policy initiative is without doubt detrimental to the goal of poverty reduction, it in no way relieves EU governments of the responsibility for removing their own export subsidies, subsidies which Oxfam estimates are twice as high as those in the USA.[60] The WTO claims too that the elimination of all tariff and non-tariff barriers—barriers which cost poor people in rich countries too—could result in gains for developing countries of around US$182 billion in the services sector, US$162 billion in manufactured goods, and US$32 billion in agriculture.[61] **The current situation in which Northern governments advocate trade liberalisation whilst themselves engaging in agricultural protectionism is a disgrace,**

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[57] Global Development Finance, World Bank, 2002, p.200. See—http://www.worldbank.org/prospects/gdf2002/
[58] Q129
[59] This reverse flow is made up primarily of US$5 billion of repayments made by developing countries to Japan on loans extended during the Asian financial crisis.
[60] Europe's double standards: How the EU should reform its trade policies with the developing world, Oxfam Briefing Paper no. 22, June 2002. See—http://www.oxfam.org.uk/policy/papers/22europe/22europe.html
[61] Doha: A Trade round for development. Speech given by Mike Moore, Director-General of the WTO at the Third Annual Conference of the Parliamentary Network on the World Bank, Berne, 10 May 2002.

and puts at risk not only the Doha trade round, but also the MDGs. The developed countries must act now to eliminate agricultural subsidies and to enable developing countries to sell their products in Northern markets. We urge the Government to do its utmost to bring such changes about. We will be monitoring progress very closely.

Outflows from Developing Countries: 'Capital Flight', Debt and Debt Service Repayments

27. Outflows from developing countries complete the picture. A first strand of resource outflows is 'capital flight' or investment overseas by developing countries. Over the course of the 1980s and 1990s such resource outflows amounted to around US$1200 billion, or nearly 20 percent of the GDP of developing countries.[62] This average hides significant regional variations; in South Asia 3 percent of private wealth is held abroad; in Africa the figure is a staggering 39 percent.[63] Such flows are of course difficult to identify, measure or control, but if developing countries are to retain more of the resources they need to meet the MDG targets, steps must be taken both to improve in-country conditions and remove the incentive for capital flight, and—through improved surveillance and regulation of the international banking system—to discourage illegal outflows.

28. Debt and debt service repayments are the second major resource outflow from developing countries. As we noted in our first report on debt relief, in 1995 the total debt service paid by developing countries was US$194 billion, or, more than three times the volume of aid then provided to developing countries by DAC donors.[64] Since then, the HIPC initiative has been established, and subsequently enhanced, with the aim of providing eligible countries with a sustainable exit from the burden of debt so that they are able to retain more of their resources for poverty reduction. In conjunction with the provision of debt relief, the HIPC process has entailed encouraging countries to adopt policies of macroeconomic adjustment, and structural and social policy reforms.

29. Under HIPC, the IMF and World Bank have approved debt-reduction packages for 26 countries, amounting to a total of US$40 billion or about half what these countries owe. Alongside the impact of other debt reduction, the HIPC process will reduce these countries' debts by about two thirds, and make their actual debt service payments for 2001–05 some 30 percent lower than they were in 1998–9. The debt service payments of HIPC countries in 2001–05 will average 9 percent of exports—or less than half what the typical developing country pays—and 14 percent of government revenue, which is around half the 1998–9 share. Prior to the HIPC initiative eligible countries were spending more on debt service than health and education combined; this is no longer the case. Now, HIPC countries' spending on social services is three times that spent on debt service, and takes up an increasingly large proportion of the countries' budgets.[65] (See figure 5 for additional measures of the impact of debt relief).

30. We welcomed the HIPC initiative, and applauded the role of the UK Government in pushing for debt relief,[66] but, we are very concerned that it is not delivering sufficient debt relief and is in many cases failing in its stated aim of providing a sustainable exit from debt for the poorest countries. Jubilee Research, the successor to Jubilee 2000, now takes the

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[62] Global Development Finance, World Bank, 2002, p.69—for web-site see footnote 57.

[63] Flight capital as a portfolio choice, World Bank, 2000, p.5. See—http://www.worldbank.org/html/dec/Publications/Workpapers/wps2000series/wps2066/wps2066.pdf

[64] Third Report from the International Development Committee, Session 1997–1998, *Debt relief*, HC563, paragraph 20.

[65] HIPC Initiative—Status of Implementation, IMF/World Bank, April 12 2002. See—http://www.imf.org/external/np/hipc/2002/status/041202.htm

[66] Third Report from the International Development Committee, Session 1997–1998, *Debt relief*, HC563; Fourth Report from the International Development Committee, Session 1998–1999, *Debt relief and the Cologne G8 summit*, HC470; Fourth Report from the International Development Committee, Session 1999–2000, *Debt relief—further developments*, HC251.

view that HIPC is little more than an accounting exercise which has succeeded in replenishing the books of the international financial institutions, whilst providing little debt relief to developing countries. This is a view shared by some US parliamentarians, albeit with different conclusions drawn. For Jubilee Research, the failure of HIPC ought to lead to the development of a fair, independent and transparent process for sovereign debt cancellation, in which debtors and creditors share the responsibility for the situation that many poor countries find themselves in. For some US parliamentarians, the likely implication is that the USA ought not to provide more funds for debt relief.

Figure 5: Debt Service and Social Expenditure for 26 HIPCs that have reached their Decision Points (in US$ billions, unless otherwise stated)

	1999	2000	2001	2002
Debt service paid[67]	3.082	3.144	2.431	
Debt service due after HIPC relief				2.372
Social expenditure	5.330	5.930	6.898	7.637
Debt service/exports (percent)	15	15	11	11
Debt service/fiscal revenue (percent)	21	23	17	15
Social expenditure/debt service (percent)	173	189	284	322

Data source: IMF/World Bank, HIPC Initiative—Status of implementation report, March 2002.

31. In evidence, the Chancellor defended HIPC but acknowledged that there are some problems with the initiative, particularly as a result of falling commodity prices and the use of over-optimistic projections in calculating what debt relief would be required.[68] He told us that, "there is no complacency on our part about both what has been achieved and what has yet still to be done",[69] and accepted that countries would need a "systematic topping-up at completion point to ensure that no country exits the HIPC process with an unsustainable debt burden".[70] Towards the end of our inquiry, at the G8 Summit in Kananaskis, it was announced that the HIPC trust fund would be topped up to the tune of US$1 billion. We welcome this announcement, and applaud the Chancellor for his continuing efforts in pushing for debt relief.

32. There must not be any complacency about the HIPC process and the prospects of the HIPC countries' debt being reduced to sustainable levels. Our assessment, whilst supportive of HIPC and the debt relief process overall, is that there are a range of serious problems. Firstly, the process is too slow. After six years of the HIPC process only six countries—Uganda, Bolivia, Mozambique, Tanzania, Burkina Faso and Mauritania—have passed fully through the initiative to completion point. The rate of countries' progression through the process has clearly meant that less debt relief than promised has been delivered, and that fewer countries than expected have received debt relief. Secondly, the definition of debt sustainability used is rather arbitrary and takes little account of the developmental needs of poor countries or the resources needed to meet the MDG targets; debt relief should be more closely linked with an assessment of the resources countries need to meet the MDG targets. Thirdly, at least ten of the 26 HIPC countries are likely to exit the process with unsustainable debt burdens, even using the IMF and World Bank's measures of sustainability. This is due, in part to the fact that decisions about the amount of debt relief to be granted were made on the basis of unknown future levels of exports and over-

[67] Debt service figures for 2000 largely reflect debt service for countries that reached their decision points at end-2000 or later. The full impact of debt relief therefore does not appear until 2001 and thereafter.
[68] Q99
[69] Q128
[70] Q99

optimistic projections of economic growth, and in part to the fact that developing countries have—unsurprisingly—suffered a series of economic shocks which have knocked them off course. In this, we are in agreement with the Chancellor; additional debt relief will be required.

33. In sum, **we remain supportive of the HIPC process, but recognise that there are serious problems which require addressing, particularly as regards the speed of the process, the linking of debt relief to development needs, and the likelihood of countries exiting HIPC with sustainable debt burdens. The HIPC process must also be flexible enough to cope with the diversity of circumstances which developing countries face, including those which are emerging from conflict.**

34. We are also concerned to ensure that debt relief calls forth additional resources, rather than simply diverting the flow of aid from non-HIPC to HIPC developing countries. Our concerns were heightened by the realisation that debt relief counts towards a country's ODA contribution, something which we imagine may come as a surprise to others too. So, for instance, in 2000, 3.4 percent of UK ODA was in the form of debt relief.[71]

35. We sought clarification about this from the Chancellor and the Secretary of State, and were told that whilst debt relief is counted as part of a country's ODA contribution, if the UK were to grant additional debt relief, this would not be at the expense of DFID's aid budget.[72] We accept this explanation, but do have some lingering concerns which stem in part from the fact that debtors were rarely servicing their debt in full anyway. In such cases debt relief is to some extent a virtual transfer of resources, rather than something which actually provides a country's government with additional resources for development. This is in marked contrast to other forms of ODA which—notwithstanding the fungibility of aid—do provide developing countries with additional real resources. Pound for pound, debt-relief ODA may well provide less resources for poverty reduction than ODA which is not in the form of debt relief.

36. Therefore, we wish to emphasise three points: first, the granting of additional debt relief by donor countries, perhaps to top-up countries as they exit the HIPC process, must never be at the expense of other ODA flows; second, donors must make every effort to be as transparent as possible when they are reporting on the debt relief components of their ODA; and third, the international community must consider carefully for each developing country on a case-by-case basis whether development resources are best provided through debt relief, or through other ODA instruments. **Debt relief must provide additional real resources, and must never be provided at the expense of other ODA flows.**

Aid for Poverty Reduction

37. The map of globalisation reveals an uneven landscape of opportunity and exclusion. The world is criss-crossed by huge flows of trade and investment, but developing countries are largely bypassed. Lacking the capacity to trade, or the ability to attract investment, developing countries are marginalised and the least developed countries are almost totally excluded. In 1998, the least developed countries attracted less than 4 percent of long term capital investment headed for developing countries. In consequence, 84 percent of the total resource flow to the 48 least developed countries was aid.[73] Developing countries will not meet the MDG targets through attracting inward investment and generating export revenues. Both the pattern and purpose of non-aid resource flows explain

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[71] OECD/DAC Development Cooperation Report 2001, p.91.
[72] Ev 101 to Ev 103
[73] Briefing on International Conference on Financing for Development, UN Department of Public Information, February 2002.

why aid—more aid, used more effectively—is crucial. As the joint DFID/HM Treasury memorandum explained:

> "Globalisation is changing the context in which governments interact with private investors. Although foreign private investment in developing countries has risen significantly over the last couple of decades or so, much of this investment is concentrated in a small number of large countries. Many of the poorest countries including those in sub-Saharan Africa have not succeeded in attracting significant amounts of foreign or local private savings and investment sufficient to sustain high rates of economic growth".[74]

38. Poverty reduction is not what motivates private capital. Given the appropriate pro-poor policy environment, inward investment may lead to a reduction of poverty in the long term through increased growth and trickle-down, but there are no guarantees. In addition, it is unlikely to have a speedy impact on people's ability to meet their basic needs for food, water, shelter, education and health services. As the Chancellor told us: "there is absolutely no doubt that, when we are talking about health and education and anti-poverty programmes, these cannot be done properly without the richest countries being prepared to devote a higher share of income to the poorest countries".[75] **There are various flows of financial resources, any of which might be tapped by developing countries, but only aid can be truly focussed on poverty reduction. We are glad that DFID, the Treasury and the Government are so supportive of aid, and encourage them to continue to push the case for aid in both domestic and international fora.** As Development Initiatives told us, "you have to remember that most private finance which is invested in developing countries is not targeted on poverty reduction. It may be welcome, it may contribute to growth, but if you look at the people who are chronically poor, then they are the people who most need the aid which is the only international resource which can be specifically targeted on poverty and the goals".[76] We return to issues of aid volume and aid effectiveness in chapters five and six.

[74] Ev 83, para 26
[75] Q104
[76] Q39

IV. INNOVATIVE SOURCES OF FINANCE FOR DEVELOPMENT

39. Global public goods such as peacekeeping, agricultural research, the prevention of contagious diseases, global financial stability, and biodiversity conservation, are likely to be under-provided by national governments because the benefits of their provision extend across borders.[77] The Zedillo Panel reported an annual shortfall of US$15 billion for the provision of global public goods, in addition to the extra US$50 billion per year needed to meet the MDG targets. Global public goods are non-rival; one person's consumption of the good does not reduce another's ability to enjoy it. They are also non-excludable; one person cannot prevent another's consumption. Such characteristics give rise to free-riding, market failure and under-provision, leading many commentators to conclude that what is needed is a new multilateral mechanism for funding the provision of global public goods.[78]

40. The Zedillo report examined a range of proposed mechanisms including a carbon tax, a currency transactions tax, and a new allocation of Special Drawing Rights (SDRs), concluding that "new sources of finance should be considered without prejudice by all parties involved".[79] The more conservative Monterrey Consensus "recognize[s] the value of exploring innovative sources of finance".[80] In the UK, DFID and the Treasury accept the "need to raise a very significant amount of additional finance for development to achieve the Millennium Development Goals" and acknowledge the importance of looking at proposals openly and carefully.[81]

Currency Transactions Taxes

41. We examined the proposal to establish a currency transactions tax (CTT) in some detail, seeking in particular to assess its feasibility. More commonly known as the "Tobin Tax", this proposal originated in a suggestion made by Nobel-prize winning economist James Tobin in the early 1970s to impose a small tax, most commonly of between 0.01 and 0.1 percent, on foreign exchange or currency transactions. For Tobin, the purpose of the tax was to reduce short-term capital flows in order to restore the autonomy of national monetary policy. Imposed on currency transactions, the tax would automatically fall most heavily on short term capital flows, discouraging them, but having little impact on long-term investment and trade-related flows.

42. For current advocates of the tax such as War on Want and members of the Tobin Tax Network,[82] the tax has two developmental purposes. Firstly, in reducing speculation the tax would give developing countries—which are particularly affected by exchange rate fluctuations and financial crises—"more room for manoeuvre in terms of their domestic policy" and make them less vulnerable to the fluctuations of currency markets.[83] This would provide developing countries with a more stable environment in which to marshal their resources to meet the MDG targets. Secondly, the tax could provide a major source of revenue which could be earmarked for developmental purposes, including the provision of global public goods. Estimates of possible revenue yields vary depending on the tax rate proposed, the expected impacts on the currency markets, and assumptions about evasion and

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[77] Financing and providing global public goods: Expectations and Prospects, Institute of Development Studies, for the Swedish Ministry for Foreign Affairs, November 2001.
[78] Q66
[79] Zedillo report, p.6.
[80] Monterrey Consensus, paragraph 44. See footnote 12 for web-site.
[81] Ev 82, para 21; and, Tackling poverty: A global new deal—A modern Marshall plan for the developing world, HM Treasury, February 2002. See footnote 13 for web-site.
[82] The Tobin Tax Network includes 48 organisations including ActionAid, Christian Aid, Friends of the Earth, Oxfam, Save the Children Fund and World Vision from the charity sector; the GMB, TGWU, TUC and UNISON from the trade union sector; and, a range of faith-based organisations.
[83] Q82

collection, but tend to range from around US$50 billion to US$300 billion for a 0.1 percent tax.[84]

43. There are a variety of objections to CTT proposals. A first set of objections suggests that CTTs are an unnecessary and unhelpful interference in the currency markets, and that exchange rate fluctuations reflect economic fundamentals and the competence of governments in managing their economies. We accept that CTTs and capital controls are no substitute for good governance, but we do not share this view in full; volatile markets may need to be regulated to curb their harmful excesses and to prevent contagion effects. A second set of objections is that whilst CTTs would reduce the liquidity of currency markets, they may actually increase volatility rather than reduce it, and hinder the efficient workings of the markets. This is a highly technical, and also, an empirical matter. We do not pretend to have the technical expertise to assess such objections, or to adjudicate between the different views of experts who do, and as such are not qualified to judge the validity of such a critique. A third set of objections suggests that CTTs would not deter speculation as the tax is too small; a fourth argues that CTTs would cause currency markets to migrate to different tax regimes including offshore tax havens and/or into other products such as derivatives. These are serious objections, to varying degrees.

44. We agree that the Tobin Tax as initially proposed would not sufficiently deter speculators at times of exchange rate instability; and that a tax set at a rate which would deter speculators would be likely to lead to market migration. However, these problems might be reduced by more sophisticated variants of the Tobin Tax such as Professor Spahn's proposed two-tier CTT.[85] In this proposal, a low rate tax imposed at all times would generate revenues from the currency markets, and at times of exchange rate instability an additional tax would be triggered which would be at a level high enough to discourage speculation and restore stability.

45. But, despite Professor Spahn's assessment that a CTT could be imposed by the EU-plus-Switzerland without pushing the currency markets either offshore or into derivatives trading, we are not convinced that the Spahn proposal addresses adequately the problems of collection and feasibility. It might also accentuate the problems of a two-speed Europe. Such matters are highly technical, and in this we defer to the assessments made by the Zedillo panel and the European Commission's report on Responses to the Challenges of Globalisation. The Zedillo report described the merits of a CTT as "highly controversial" and concluded that "further rigorous study would be needed to resolve the doubts about the feasibility of such a tax".[86] The EU reported that a CTT would "most likely require a multilateral approach".[87] We are aware of the suggestion—made by Rodney Schmidt of the North-South Institute and acknowledged as useful by DFID and HM Treasury[88]—that the tax could be collected through the Continuous Linked Settlement Bank system.[89] Schmidt argues that levying the tax on currencies rather than countries, and collecting it through the settlement system, would reduce the risk of both geographical migration of markets, and migration into derivatives. Nonetheless, in our view it would be very difficult for the UK or the EU to impose the tax unilaterally.

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[84] Ev 69—corroborated by: Zedillo report; UN Technical note on existing proposals for innovative sources of finance; and, European Commission report on Responses to the challenges of globalisation. See— http://europa.eu.int/comm/economy_finance/publications/globalisation/r2002_185en.pdf

[85] This two-tier CTT was outlined most recently in a paper produced by Professor Spahn for the Germany Ministry of Development Cooperation. See—http://www.wiwi.uni-frankfurt.de/professoren/spahn/tobintax/Chapter0.pdf

[86] Zedillo report, p.9—see footnote 6 for web-site.

[87] Responses to the challenges of globalisation, European Commission, February 2002, p.13. See footnote 84 for web-site.

[88] Ev 82, para 23

[89] Ev 99. See http://www.waronwant.org/tobin/TobinTax1.pdf for Schmidt's proposal.

46. We recognise that there is considerable support for CTTs both in the UK and in other countries including, in the North, France, Canada and Belgium. We too are sympathetic to the motivations behind CTT proposals. **We share with many advocates of CTTs the view that exchange rate volatility contributes to poverty and hinders development, and we too wish to see more financial resources available for development. Many taxes—taxes on smoking, motoring, pollution—have two apparently contradictory purposes. This is not a significant criticism of CTTs, but the question remains as to whether a CTT is the best way, either of reducing speculation or of raising revenue. If we are to be persuaded fully, further investigation into issues of feasibility and practicality will be needed.** The Spahn proposal—in separating but linking the two aims of generating revenue and reducing speculation—is an interesting one, which, in conjunction with technological developments in the banking system, is worthy of further consideration. Nevertheless, **in our view it is imperative that generating the political will to finance development remains the central focus, and that the choice of methods by which to collect funds remains a secondary consideration.** As Clare Short argued: "You do not have to invent a new tax to find the money, you have to decide whether you should find the money, and then, if new taxes are good for the international system, let us have them. But I think it is slightly dangerous to the development argument if you get boxed into thinking you can only get more money for development if you can find a new tax".[90] The possibility of a currency transactions tax merits further consideration. Detailed feasibility studies and cost benefit analyses are required to look into CTT proposals in greater depth before they can be recommended.

Special Drawing Rights

47. Created by the IMF in 1969 as an international reserve asset to supplement Fund members' reserve holdings, SDRs are in themselves neither new nor innovative. The primary motive for creating SDRs was to promote international financial stability by providing a permanent increase in the world stock of reserves and hence preventing general shortages of international liquidity from occurring. There have only ever been two allocations of SDRs. The most recent, in 1981, brought total SDR allocations to about 1.5 percent of global reserves. New allocations can be made. A general allocation, in line with existing IMF quotas, requires the agreement of 85 percent of the IMF's membership in terms of voting power. A special allocation, directed towards developing countries for instance, would require unanimity. In practice, general and special allocations can be vetoed by the USA. A special allocation to new IMF members which were not beneficiaries of earlier general allocations was agreed by the IMF Board in 1997, but is being held up by US opposition, in part because it is feared that discussion of SDRs in Congress might re-open wider issues about the role of the IMF.

48. There are a variety of interlinked proposals for using SDRs to finance development. One is that a new allocation of SDRs should be used to fund an emergency financing facility to deal with financial crises. A second is that SDRs should be made available to poorer countries so that they can build up sufficient reserves without having to borrow at market rates. A third proposal, associated particularly with George Soros, is that periodic general allocations of SDRs should be made, and that developed countries should put their allocations into an international development trust fund, which would be used to finance development. ODI estimates that this proposal could raise perhaps US$4 billion per year.[91]

49. Whilst not considering any proposal in much depth, both the Zedillo Report and the Monterrey Consensus did consider SDR allocations as a means of financing development. The Zedillo Report described SDRs as a "promising approach to easing financial constraints on developing countries", and drew attention in particular to the

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[90] Q122
[91] Ev 46

possibility that a new SDR allocation might reduce the flow of "reverse aid" which developing countries pay to borrow sufficient reserves to protect themselves from crises.[92] The UK supports a new general allocation—the Fourth amendment—on equity grounds, to boost liquidity and to provide finance for development, but is opposed by, amongst others, the USA, Germany and Canada. HM Treasury reports that the UK is "open to the arguments for another possible general SDR allocation".[93]

50. There are a variety of objections to SDR proposals. A first set of objections concern liquidity and inflationary pressures: there is no reliable means of calculating the liquidity requirements of the global economy; no way of assessing whether these needs can be met by the capital markets; and, no way of telling what volume of SDRs would contribute to inflationary pressures.[94] A second objection, although clearly this would be seen as a plus from some viewpoints, is that SDR allocations would reduce the power of the IMF to—through the attachment of conditions to its lending—encourage developing countries to adopt particular policies. A third objection is that new regular allocations, particularly specific allocations, would contravene the principles and procedures which govern IMF allocations of SDRs.

51. **We are supportive of the Government's position on SDRs. If the fourth amendment were ratified it would provide a welcome one-off increase in global liquidity, and might provide some resources for development. We encourage the Government to continue to press this case.** However, given the strong objections and veto power of the USA, and SDRs' limited realistic potential to raise new resources, SDRs cannot be expected to provide much in the way of financing for development. The EU, in its report, questioned whether it is appropriate to use monetary creation—which is what an SDR allocation is—to finance development.[95] **We tend to share these concerns, but consider that there might be a limited role for SDRs, perhaps as part of an International Development Trust Fund.**

The International Development Trust Fund

52. In a series of speeches and publications made since November 2001, the Chancellor has proposed the establishment of an International Development Trust Fund—or perhaps more precisely a financing mechanism or "facility"[96]—to generate quickly the step-change in aid flows which is needed if the MDG targets are to be met. The suggestion is that donor countries should commit substantial aid resources to 2015 and beyond, and that these resources should be used as collateral to leverage additional funds through borrowing in international capital markets. This borrowing would be guaranteed by donor governments. In this way, additional flows of US$15–20 billion per year could be leveraged up to US$50 billion per year. The amount of borrowing required to meet a given target would depend on initial donor contributions, interest rates, the total amount of resources disbursed by the fund, and the proportions and terms of any grants and loans made by the fund. The fund could be overseen by a new joint implementation committee of the IMF, World Bank, and perhaps other donors, and the resources distributed through existing institutions.[97]

53. Beyond this, we know very little. Indeed, the caution of the Treasury in fleshing out this proposal, indicates to us that the Government is engaged in the delicate business of trying to win international support for this proposal. This does however make any

[92] Zedillo report, p.58.
[93] Ev 104, para 5
[94] Ev 46
[95] Responses to the challenges of globalisation, European Commission, February 2002, p.109. See footnote 84 for web-site.
[96] Q101
[97] Ev 101

assessment of the proposed Trust Fund rather difficult and perhaps somewhat premature.[98]

54. That said, it is our duty to raise some issues which might usefully be addressed. Our main concerns are about how the large debts incurred by guarantor donor countries would eventually be paid off, and about the possible negative impact of such debts on donors' willingness to extend aid beyond 2015. In evidence, the Chancellor wondered aloud as to whether making substantial sums of aid available now might reduce the amount of aid needed after 2015.[99] We, and the Chancellor, may hope that investing substantial amounts of aid now may produce returns in terms of poverty reduction by 2015. We may hope too that as developing countries grow economically and the global market expands, the ability of donor countries to repay their borrowing will grow too. We may also hope that by 2015 tax-payers will appreciate the wisdom of providing increased aid to developing countries. But, it would not be prudent to base our plans entirely on such optimistic hopes. In addition, it remains unclear to us what an international development trust fund could do, which a similarly-funded World Bank could not.

55. Like the Chancellor, we are not dismissive of proposals for new and innovative sources of finance for development. Questions remain about some of the proposals, but there is no doubt that there is a funding gap which needs to be filled if the MDG targets are to be met. Innovative proposals may, in time, gather the international support which is needed to make them a success, and they may be a useful supplement to more traditional sources. However, it is crucial that such proposals do not obscure the real issue: **there is a funding gap which can only be filled by substantial North-South resource transfers. Such resource transfers will only be possible if sympathetic Northern governments show real political leadership, both in persuading other countries, and in securing domestic public support for the necessary resource transfers.** As the Chancellor put it: "each proposal comes back to this essential question, are the individual countries who are the donors prepared to do more, because it requires political will, whichever solution you come to".[100]

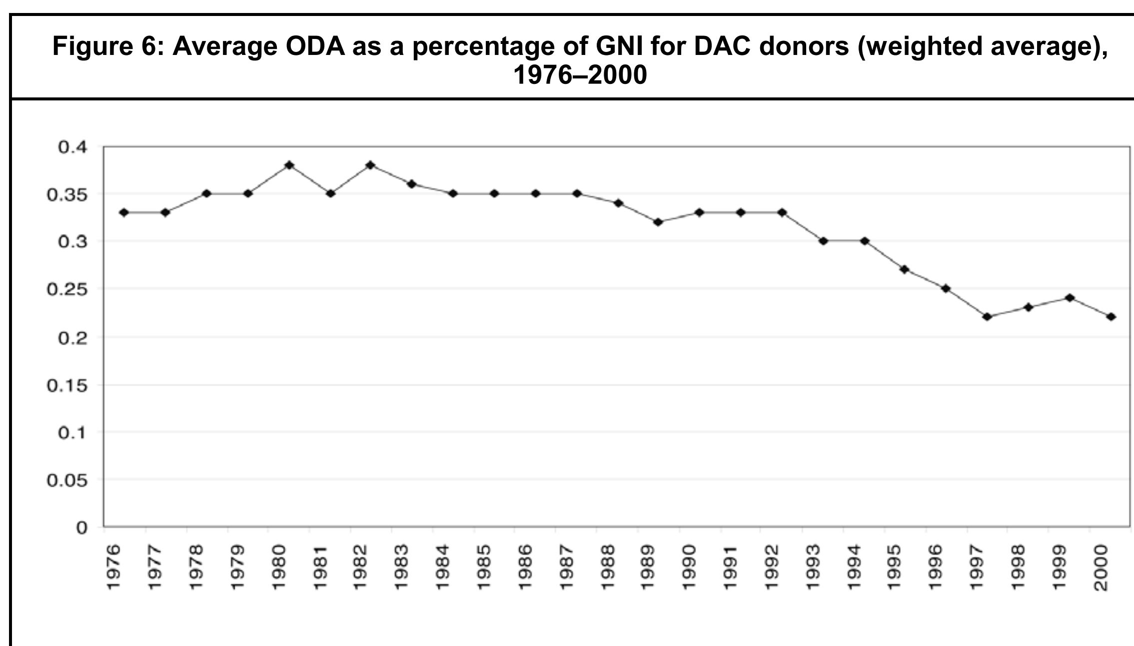
[98] However, see Ev 66 for projections concerning the proposed Trust Fund.
[99] Q101
[100] *Ibid.*

V. OFFICIAL DEVELOPMENT ASSISTANCE: VOLUMES

56. The Monterrey Consensus acknowledges the “essential role” of ODA as a complement to other sources of financing for development, especially in the poorest countries, and urges donors to make progress towards the 0.7 percent target and to allocate more of their aid to the poorest countries.[101] Unlike other financial resources, aid can be and is focussed on the provision of basic social services and the elimination of poverty (see also paragraph 38). As the Chancellor reiterated in evidence to us, “whatever we expect and hope that the developing countries are prepared to do to change the way they use money, it is going to be essential, in the next period of time, that we provide more development aid”.[102] **If the MDG targets are to be met, there must be a massive increase in aid flows to developing countries. Making aid more effective is crucial too, but there is universal agreement that aid volumes will have to increase substantially.**

57. During the 1980s and early 1990s the amount of aid given by DAC donors—measured as a percentage of national income (ODA/GNI %)—fell steadily. Since 1997, this decline has been halted somewhat, but the figure of 0.22 percent for 2000 falls well short of the 0.7 percent target (see figure 6). For DAC donors as a whole, 0.05 percent of national income was provided to the least developed countries in 2000; the UN-agreed target is to allocate 0.15 percent of GNI to the least developed countries.[103]

Figure 6: Average ODA as a percentage of GNI for DAC donors (weighted average), 1976–2000



Data source: DFID Statistics on International Development, 1996/7–2000/1.

58. In the year 2000, only five countries met or exceeded the 0.7 percent target; these countries were Denmark, the Netherlands, Sweden, Norway and Luxembourg. In absolute terms the USA was the second largest aid donor, contributing US$10 billion in ODA, with Japan leading the way at US$14 billion. Expressed as a proportion of national income however, the US Government is the least generous donor contributing 0.1 percent of GNI in ODA. (See figure 7).

59. **As far as the UK is concerned, recent years have seen welcome increases in aid contributions, from US$3.2 billion in 1997 to US$4.5 billion in 2000, raising the UK’s contribution from 0.26 to 0.32 percent of GNI (see figure 8), and bringing the UK level**

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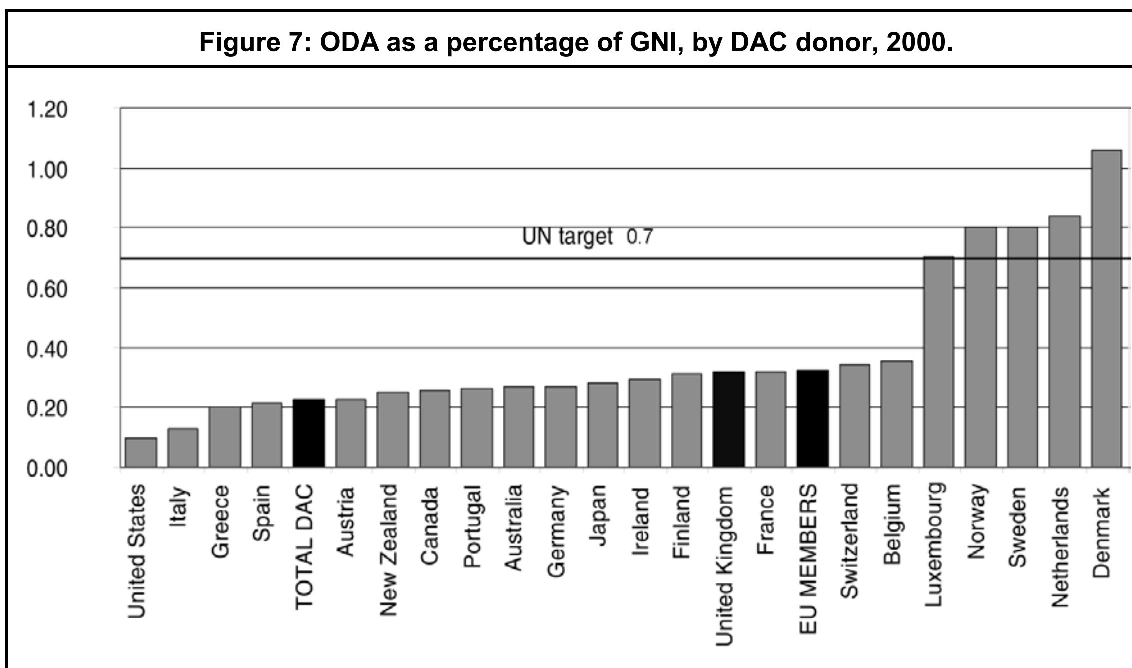
[101] Monterrey Consensus, paragraphs 39 and 42. See footnote 12 for web-site.
[102] Q124
[103] OECD/DAC Development Cooperation Report 2001, Table 7.

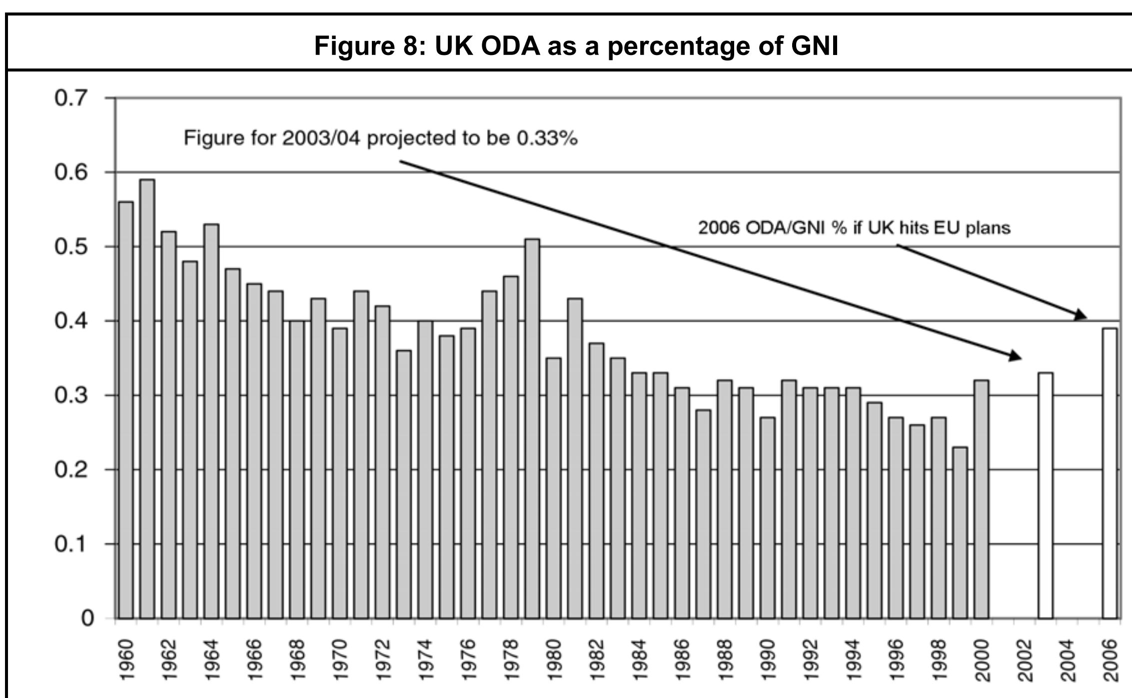
with France in these terms.[104] In the recent spending review, the Chancellor announced that UK aid will rise to 0.4 percent of GNI by 2006. This increase, whilst leaving the UK well short of its 0.7 percent commitment, will lift it well above the current OECD/DAC average of 0.22 percent, enable it to meet and exceed the EU target of 0.39 percent by 2006, and reinforce the UK's position as the most generous G7 donor in ODA/GNI terms.

Figure 7: ODA as a percentage of GNI, by DAC donor, 2000.



Data source: OECD/DAC Development Cooperation Report 2001.[105]

Figure 8: UK ODA as a percentage of GNI



Data source: Development Initiatives memorandum[106]—using OECD/DAC data.

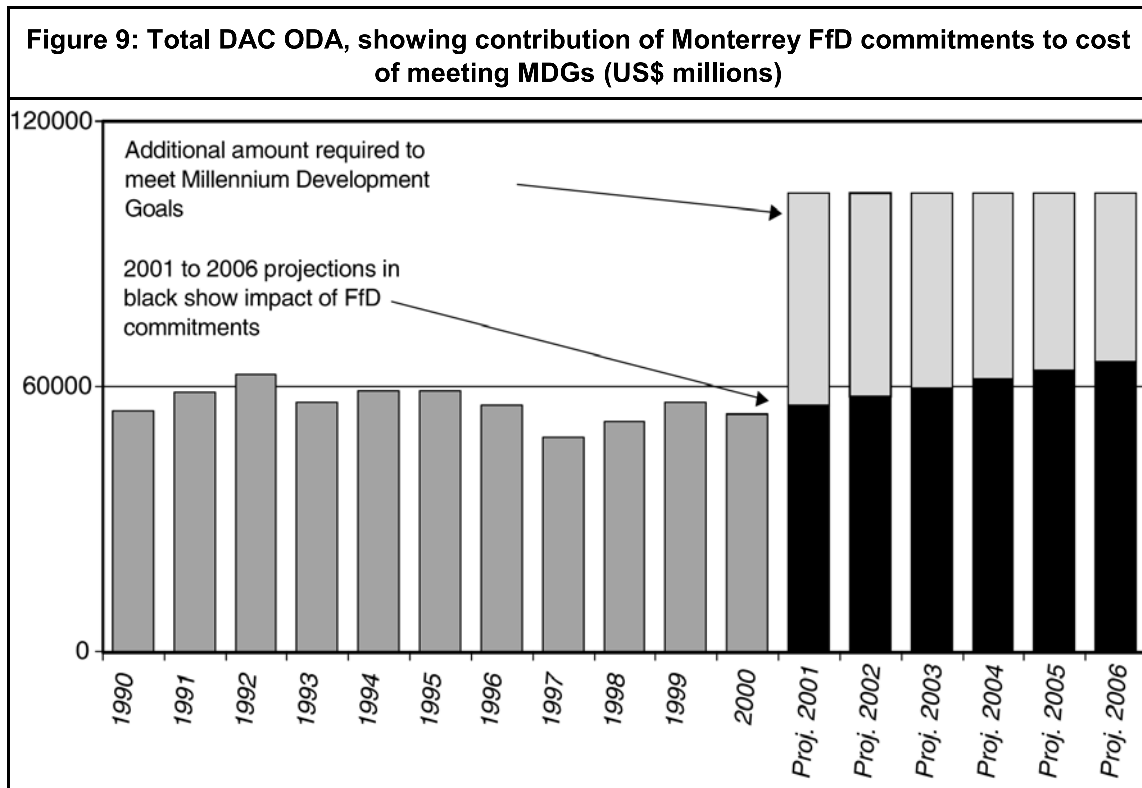
[104] Ev 81–82

[105] Although the UK and France are shown as equally generous in ODA/GNI terms, the UK's contribution is rising more sharply than that of France.

[106] Ev 12. Figure 8 does not take account of the aid increases announced recently in the spending review, increases which will put the UK at an ODA/GNI level of 0.4 percent by 2006.

60. As previously outlined (see paragraph 12), in the week before the Financing for Development Conference, both the EU and the USA announced substantial increases in aid. The EU announcement amounts to an extra US$7 billion of aid per year from 2006; the US announcement amounts to an extra US$5 billion of aid per year from 2006. We applaud these announcements and the effort which went into making them possible, not least the work of DFID and HM Treasury in making the case for aid both within the EU and in discussions with the USA. That said, the announced increases in aid still do not provide the resources needed to finance the MDG targets. (See figure 9). More recently at the G8 summit, it was agreed that up to 50 percent of the additional US$12 billion announced at Monterrey could be targeted at Africa. We are pleased that these funds were earmarked in this way, but are disappointed that little in the way of new resources was announced by the G8.

Figure 9: Total DAC ODA, showing contribution of Monterrey FfD commitments to cost of meeting MDGs (US$ millions)



Data source: Development Initiatives memorandum[107]—using OECD/DAC data.

61. Additionally, in the case of the US announcement—an increase of aid that will likely make the USA the biggest donor but still leave it as the least generous in ODA/GNI terms—there are a range of concerns. Firstly, any increase in aid will require congressional approval, something which cannot be taken for granted. Secondly, the increase has not been expressed as a percentage of national income, and hence will be eroded over time by inflation. Thirdly, the USA intends to disburse the funds through its own Millennium Challenge Accounts; this will duplicate existing frameworks and will mean that the USA will attach its own strict—and in some critics' eyes excessively political rather than developmental[108]—conditionalities to the funds (see also paragraphs 94–99). In the case of the EU announcement: it is not clear what, if anything, can be done to ensure that member states honour their commitments to reach a minimum of 0.33 percent; there are question marks about the impact which accession countries will make on EU aid levels; and, it is disappointing that the timetable extends only as far as 2006 and the attainment of an EU average of 0.39 percent.[109]

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[107] Ev 14
[108] Ev 2, para 2 and Ev 8
[109] Ev 2, para 2

62. The ability of the EU to deliver the promised increase in aid, and to make progress towards the 0.7 percent target, depends on the actions of individual member states. As one of the most respected players in international development, the UK has the responsibility to show leadership in this area, including as regards aid levels. In their written evidence, DFID and HM Treasury assured us that, "The Government is committed to significantly raising the amount of our development assistance, and its share in national income, in the current spending round".[110] We are pleased that such commitments have been kept, and that in the recent spending review, the Chancellor announced that UK aid—including debt relief—will rise to nearly £4.9 billion per year by 2005–06. However, we were disappointed that the Chancellor side-stepped our question as to when the UK would set a timetable for reaching 0.7 percent, reiterating that the UK is committed to the target, but refusing to be drawn on any timetable beyond 2006.[111] We understand the difficulties involved in committing future governments to spending, but indicative long-term commitments have been made in relation to domestic issues such as transport and health. We see no reason why similar long-term commitments can not be made as regards international development. **We recommend that the Government follow the example of Belgium and Ireland (see figure 10) in setting a date—a date which is sufficiently in advance of the 2015 MDGs' deadline—for reaching 0.7 percent, and a timetable for hitting that target.**

Figure 10: EU Member States' Current Aid levels and Future Commitments

Country	Current Aid Level	Future Commitments
Austria	0.23	0.35 by 2003
Belgium	0.36	0.4 or 0.41 by 2003, 0.7 by 2010
Denmark	1.06	To be reduced to 0.7
Finland	0.31	0.4 by 2007
France	0.32	Committed to at least EU average
Germany	0.27	0.35 or 0.36 by 2006
Greece	0.2	0.33 by 2006
Ireland	0.3	0.45 by 2002, 0.7 by 2007
Italy	0.13	0.25 by 2006
Luxembourg	0.71	1.0 by 2005
Netherlands	0.84	Current level to be maintained
Portugal	0.26	0.36 by 2006
Spain	0.22	0.3 by 2003/4
Sweden	0.8	1.0 by 2006
UK	0.32	0.4 by 2006
EU average	0.32	0.39 by 2006

Data Source: DFID/HMT memorandum[112] and Action Aid/BOND supplementary memorandum.[113]

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[110] Ev 80, para 14
[111] Q105
[112] Ev 81–82
[113] Ev 35–39

VI. OFFICIAL DEVELOPMENT ASSISTANCE: EFFECTIVENESS

63. Aid is effective and increasingly so. In countries which follow appropriate policies, a 1 percent injection of GDP can produce a 0.6 percent increase in growth, a 1.2 percent decline in poverty and a similar decline in infant mortality.[114] In 1990, a one-time aid increase of US$1 billion allocated across countries in proportion to existing ODA would have permanently lifted an estimated 105,000 people out of poverty. By 1997–98, US$1 billion would have lifted 284,000 people out of poverty. In other words, **the estimated poverty-reduction productivity of ODA nearly tripled during the 1990s.**[115]

64. Raising questions about the effectiveness of aid may deflect attention from the insufficient volumes of aid which donors provide. On occasion it may suit donors for attention to be focussed on questions of aid effectiveness.[116] That said, **we believe strongly that there need not be a tension between aid volume and aid effectiveness, and that improvements in aid effectiveness are essential if increases in aid volume are to be generated. As such, we are firmly of the view that donors and recipients of aid must work together to improve the effectiveness of aid.** As Clare Short told us:

> "More effective use of aid could produce extra resources; a greater focus on the poorest countries and better collaboration amongst donors, including the pooling of budgets, could also maximise the efficiency of aid in diminishing poverty. Overall better allocation, co-ordination and untying, by bilateral donors and by international institutions, could make aid 50 percent more effective".[117]

The stakes are high: aid can, and must, be made more effective. This will require concerted action from both the donor and the recipient ends of the aid relationship to improve the allocation, design and delivery of aid.

The Good Recipient: Committed to Poverty Reduction and Good Governance

65. The Monterrey Consensus emphasised that developing countries have the primary responsibility for their own development, stating that:

> "Good governance is essential for sustainable development. Sound economic policies, solid democratic institutions responsive to the needs of the people and improved infrastructure are the basis for sustained economic growth, poverty eradication and employment creation. Freedom, peace and security, domestic stability, respect for human rights, including the right to development, and the rule of law, gender equality, market-oriented policies, and an overall commitment to just and democratic societies are also essential and mutually reinforcing".[118]

We share these views, and believe strongly that **developing countries—their governments, but also civil society, business and the media—have the primary responsibility for ensuring that aid is used effectively. The ineffective use of aid or the diversion of aid into the pockets of elites pushes the poor deeper into poverty and robs them of the assistance provided to them.**

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[114] The case for aid for the poorest countries, DFID/HM Treasury, March 2002—copy placed in library and see http://www.hm-treasury.gov.uk/mediastore/otherfiles/case_for_aid02.pdf

[115] The role and effectiveness of development assistance, World Bank, April 2002, p.xviii. See—http://econ.worldbank.org/files/13080_Development_Effectiveness.pdf

[116] Ev 111, para 9

[117] Q99

[118] Monterrey Consensus, paragraph 11. See footnote 12 for web-site.

66. **The pre-requisite for poverty reduction and the effective use of aid is the commitment of the recipient government to poverty reduction.**[119] Whilst emphasising the importance of country-specific factors, ODI suggested to us that the effective use of aid is built on the following foundations: effective governmental systems for public expenditure management; a tolerable degree of macroeconomic stability; political stability; physical security; and a framework of law which enables enterprise and encourages businesses to invest.[120] In addition to the various dimensions of good governance, aid effectiveness depends too on the ways in which aid resources are spent. As Judith Randel of Development Initiatives told us:

> "investment in human development is actually effective, it does deliver. Investment in public health, investment in education, are extremely effective ways of spending money but we spend a tiny, tiny amount of the aid budget on that. We [the DAC donors on average] spend 2 percent of aid on basic health and 1.5 percent of aid on basic education globally. We have not really invested that much in the things that work in the context we think they are likely to work".[121]

67. At the Copenhagen Social Summit in 1995 it was proposed that donor and recipient governments come to bilateral agreements whereby donors would allocate 20 percent of their ODA to basic social services including basic education, primary health care, reproductive health care and family planning, nutrition, safe drinking water and hygiene, if recipients agreed to allocate 20 percent of public expenditure to enable universal access to basic social services. This 20/20 Initiative offers aid donors and recipients the opportunity to take joint responsibility for a policy of social development. DFID does not have a target for the proportion of its aid spent on basic social services, but in 1997/8 18 percent of the UK's aid went to basic social services compared with a DAC average of 11 percent.[122] If the UK is serious about improving the effectiveness of aid, scarce resources must be invested in the sectors which are likely to provide the best returns in terms of poverty reduction. **We recommend first that DFID considers adopting a target for its aid allocation to basic social services, second that DFID encourages its fellow DAC members to increase their allocations in line with the 20/20 Initiative, and third that DFID continues to encourage the recipients of its aid to prioritise spending on universal access to basic social services.**

The Good Donor: Providing Sufficient, Timely and Quality Aid

68. Effective aid relationships require donors to play their part too, and to be accountable for the parts they play. As Belen Vazquez of Action Aid succinctly put it: "A good donor is a donor that accepts responsibilities in the process. The responsibilities of the donor are to provide sufficient aid, timely aid and aid of good quality".[123] ODI emphasised the importance of donors engaging seriously with the development strategy and process, the need for donors to provide flexible resources to implement the strategy, and, the importance of donors being accountable for the delivery of timely and efficient aid using simple and transparent procedures.[124] Quality aid is focussed on the elimination of poverty and the attainment of the MDG targets. Quality aid does not require the recipient to spend the aid on goods and services provided by donor country firms. Quality aid is untied aid. In this, we are in full agreement with DFID, which, having led the way in untying all its bilateral aid in April 2001, has been pushing other donors to follow suit, or at least to make progress by untying bilateral aid between EU Member States.

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[119] Q57
[120] *Ibid.*
[121] Q16. The equivalent figures for the UK—given in table 19 of the OECD/DAC Development Cooperation Report for 2001—are 2.6 percent and 4.8 percent.
[122] Peer review of UK aid, OECD/DAC Journal, 2001,Volume 2, Number 4, p. I-30, footnote 9.
[123] Q17
[124] Q62 and Q65. See Ev 61 for ODI table concerning best-practice for donors, recipients and NGOs.

69. There are various reasons why tied aid is ineffective aid. Firstly, tied aid has multiple objectives, including supporting donor-country firms; therefore its focus on poverty reduction is inevitably diluted. Secondly, tied aid cannot generate the local supply networks which would multiply the impact of an injection of aid. This was exemplified by a case we saw for ourselves in Ghana and which Clare Short mentioned in her evidence, in which the enterprise of Tema Tropical Cables, in gearing itself up to produce wire for electrification projects, was thwarted by the tying of aid, and the purchase of wires for electrification, back into Europe and North America.[125] Thirdly, tied aid can force poor countries into the ridiculous situation of having to purchase incompatible services or components—of vehicles, of hospitals, of schools—from a range of different donors. Fourthly, tied aid hinders competition between potential providers of goods and services, leading to inefficiency, and is arguably in contravention of EU internal market and free competition rules.[126] As Belen Vazquez of Action Aid put it "Development assistance should not be used as a form of subsidising home companies".[127] The OECD estimates that untying all aid would in effect provide an additional US$5 billion of resources for development every year.[128] In May 2001 the OECD DAC donors did agree to untie aid to the least developed countries, but little progress has as yet been made. **We applaud the Government's actions in untying UK aid, and encourage the Government to continue its efforts to persuade its more recalcitrant European partners to untie their aid too.**

70. As well as untying its aid, a good donor harmonises its aid procedures with those of other donors. Harmonisation and coordination reduces the bureaucratic burdens placed on recipient countries, improves the quality of aid by reducing its transactions costs, and enables poor countries to focus their resources on poverty reduction rather than complying with a range of complex and varied procedures. As Tony German of Development Initiatives told us, "what makes a good donor is not making the fragmentation even worse by everybody having their own individual little programme. ... it is better for more countries to get together to do joint programming rather than having to have their own little bit, which only makes it much more difficult for host finance ministries to track the money and then to be accountable for how the money is being spent".[129] **Ideally, and subject to an assessment of the risks involved and the requirement of accountability, aid is best provided through direct budget support.** Aid delivered in this manner can be distributed nation-wide in pursuit of poverty reduction, rather than spent on isolated projects; it is also more likely to result in sustainable ongoing development. In addition, the injection of resources directly into a government's revenue stream minimises transactions costs, and helps to build the capacity of the recipients' systems for financial management and accountability. But, as we emphasise further below, **the choice of aid instruments—as well as the allocation of aid and the selection of development interventions in general—must take account of country specifics rather than follow a preset formula.**

Aid as Investment: Targeting, Conditions and Low-Return Countries

71. As both the Secretary of State for International Development and the Chancellor of the Exchequer have been at pains to emphasise, aid ought to be conceptualised as investment in the developmental capacity of poor countries rather than as charity. Clare Short argued that, "we have got to get international development out of the charity box into the investment and economic box",[130] investing aid to enable currently poor countries to develop and ultimately to engage with the increasingly global economy. If aid is to be regarded as an investment, it should be targeted to countries where it will secure the best

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[125] Q112
[126] Ev 3, para 4
[127] Q31
[128] Ev 3, para 4
[129] Q21
[130] Q104

returns in terms of eliminating poverty, and with conditions attached to ensure that it is invested wisely. If invested aid produces good returns—in part through sensible targeting and the attachment of conditions—then it is likely to encourage further aid. We fully agree with DFID and HM Treasury; **aid should be conceptualised as investment. However, careful attention does need to be paid: first, to the allocation criteria which drive aid/investment decisions; second, to the implications for countries which are seen as offering low rates of return; and, third, to the nature of the conditions which investors might attach to aid flows.**

Figure 11: The aid relationship as investment

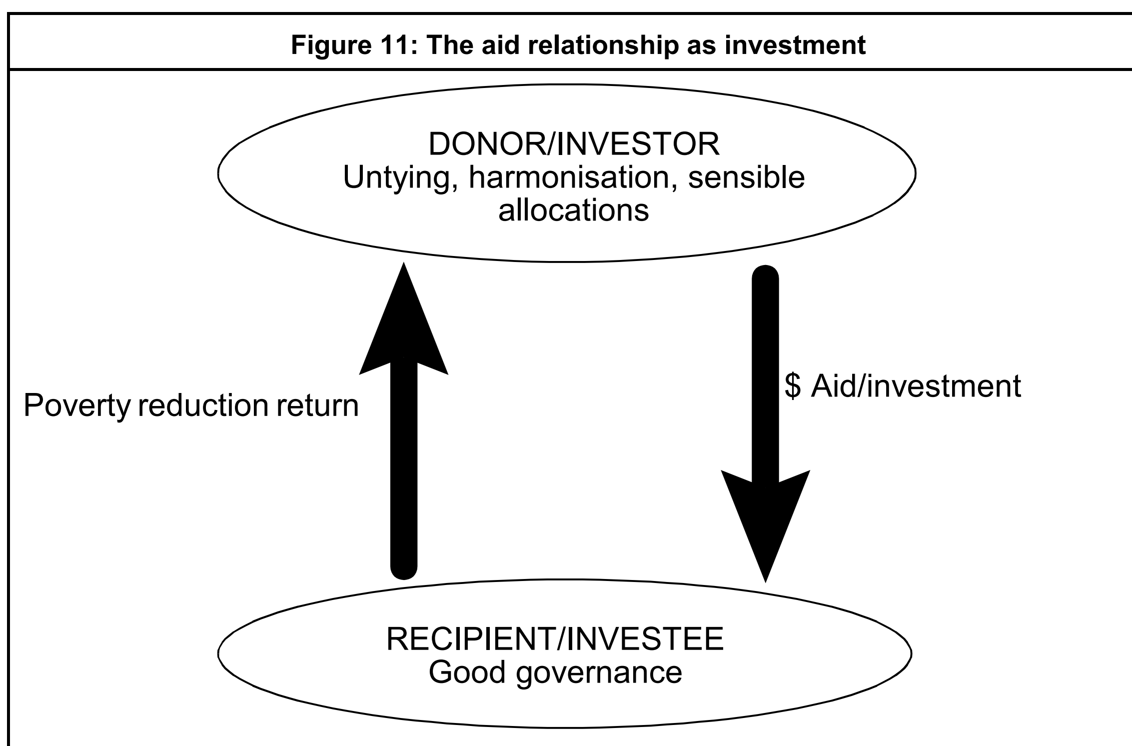

Diagram Source: Committee's own.

72. The current allocation of aid is shaped by a range of factors, including historical and cultural ties, and the realities of geo-politics. Efforts to improve the effectiveness of aid by improving its allocation are built upon conceptual models of the development process and, more specifically, of how aid contributes to poverty reduction.[131] The international community's efforts to improve the effectiveness of aid depend upon the quality of these models, and their sensible interpretation and application.

73. Particularly since the World Bank's report on "Assessing aid" was published in 1998, the widely-accepted wisdom amongst donors has become that aid should be targeted to poor countries which follow what the World Bank and the donor community deem to be sensible policies in terms of good governance, budgetary and macro-economic stability, and economic liberalisation. The simple model is that aid works by improving institutions, contributing to economic growth and raising income levels, and hence—making certain assumptions about the distribution of income gains—reducing poverty. Such mechanisms are said to work best when policies supportive of economic growth, and ideally of pro-poor economic growth, are pursued. Indeed, the World Bank's model suggests that in countries with poor policies, aid is ineffective or even harmful.[132] In short, the received wisdom has been that aid works best in, and therefore should be targeted at, poor countries which pursue World Bank-approved policies. Similarly, the model suggests that conditions should be attached to aid to encourage policy reform.

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[131] See, for instance, OECD/DAC Development Cooperation Report, 1999, p.129.
[132] Assessing aid: What works, what doesn't, and why. World Bank, 1998.

74. Over the last three or four years, however, there has been some debate about this model of aid effectiveness, specifically about the relative importance of the right policy environment in determining the effectiveness of aid. Critics of the World Bank's approach to aid allocation have suggested that aid can be effective across a range of policy environments.[133] Consequently, there are questions about the appropriate criteria for targeting aid and selecting countries, and also, about the sorts of conditions which ought to be attached to aid. DFID's position seems to be that the World Bank's advice—to target aid to poor countries with good policy—is broadly right, but that aid can also work in poor policy environments by helping recipients who are committed to poverty reduction to pursue policy reform. As we were told by Suma Chakrabarti, the DFID Permanent Secretary, in an evidence session about DFID's Annual Report, his Department's application of allocation criteria may therefore be less "mechanistic" than that of the World Bank.[134]

75. This is not the place to rehearse complex and technical debates about aid effectiveness, but the very fact that there are such debates suggests to us that donors ought continuously to re-examine their models of aid and aid effectiveness, to ensure that their aid allocations and their use of conditionalities contribute to maximising the impact of aid. **It would be helpful if DFID made explicit its underlying model of the ways in which aid is effective and its aid allocation criteria, and encouraged other donors to do the same. Such transparency is fundamental to any notion of a shared and jointly-owned development partnership, and would provide developing countries with the information necessary to—if they so wish—improve their performance in terms of the criteria.**[135]

76. Our view, as we have stated emphatically in relation to EU aid,[136] is that aid must be targeted firstly towards poor countries and countries with large numbers of poor people. A second important criterion is the nature of a country's policy environment, or more precisely the prospects of a country's policy environment changing for the better through the establishment of an aid-related policy dialogue. **Aid resources must not be squandered in countries which lack the commitment to development and poverty reduction. In addition, aid must not be used to prop up governments that are not furthering the interests of their people. This must not mean that we forget such countries, or, more specifically, the millions of poor people who live in such countries. Rather, the nature of donor engagement with such countries—countries which the World Bank labels Low-Income Countries Under Stress or LICUS—ought to be different.** As Clare Short told us: "Even where there is a lack of reform but where there are large numbers of poor people, if you can get it [aid] in effectively, it still has high effectiveness in poverty reduction".[137]

77. Donor countries need to have a range of strategies for using aid (not to mention other development interventions)—from providing direct budget support, to supporting sector-wide approaches, to financing projects, to building the capacity of civil society—so that countries can be considered on a case-by-case basis and aid can be used in the most effective way. In addition, countries should not be doubly-punished when their reforms are knocked off track by shocks such as commodity price changes or natural disasters. Just as

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[133] Ev 67. See also: OECD/DAC Development Cooperation Report, 1999, pp.130–131; Policy implications for aid allocations of recent research on aid effectiveness and selectivity: A summary, Jonathan Beynon, DFID, 2001—copy placed in library and see http://www.dfid.gov.uk/Pubs/files/beynon_paper.pdf; and, Will the new aid agenda help promote poverty reduction? Howard White, Institute of Development Studies—copy placed in library and see http://www.ids.ac.uk/ids/pvty/pdf%20files/aidagenda.pdf

[134] Q18 of evidence given to the Committee on 18 June 2002 by DFID's Permanent Secretary in relation to our inquiry into DFID's Annual Report.

[135] Conditionality or contract: Perspectives on partnership for development, published in Journal of International Development, 1998, Volume 10, pp.257–268—reference to p.265.

[136] Second Report from the International Development Committee, Session 2001–2002, *The effectiveness of the reforms of European development assistance*, HC417, paragraph 20.

[137] Q112

there is a spectrum of types of countries, or of regimes, so donors should have an array of instruments which they can use (see figure 12). Recent events in Kenya, Malawi, and Zimbabwe—countries whose governments' commitments to poverty reduction are at the very least questionable—clearly illustrate the importance of working out how to help poor people in poorly-governed countries. We are pleased that DFID is alive to such issues and is working hard on pragmatic answers to what Clare Short described as "the toughest question in international development".[138]

Figure 12: The spectrum of country types and forms of engagement

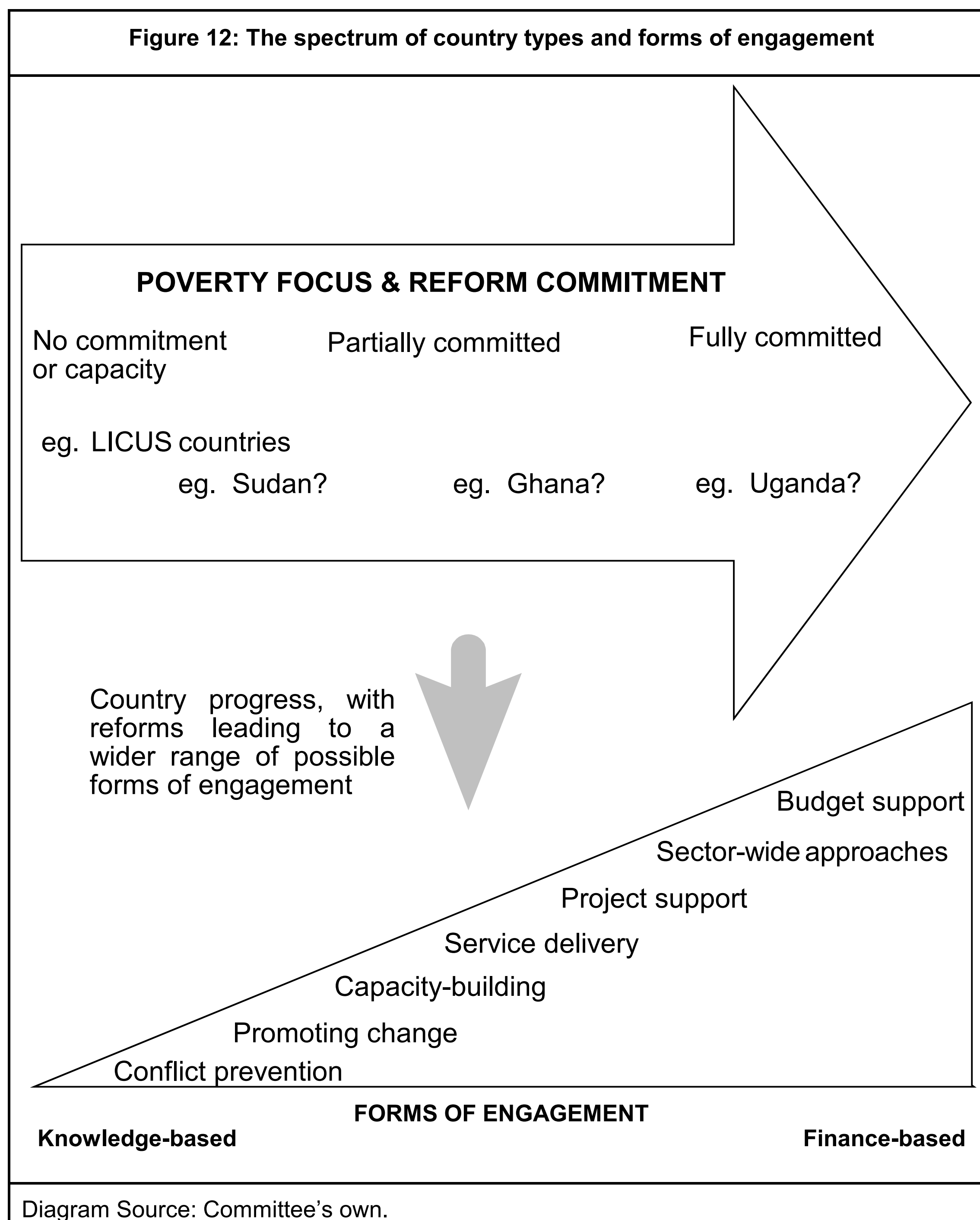

Diagram Source: Committee's own.

78. In addition to targeting their aid at countries where it is likely to be most effective, all donors attach conditions to aid to encourage the adoption of policies which are thought likely to improve the chances of aid being effective. For critics of conditionality this

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[138] Q117

amounts to the intrusive exercise of power by donors; for others it is a legitimate effort to encourage the adoption of policies which are likely to maximise aid effectiveness and poverty reduction, and a necessary safeguard to ensure that money provided by the tax-paying electorate in donor countries is used effectively. Donor-imposed conditionalities have been criticised for undermining the local ownership of development and poverty reduction strategies, and for weakening local accountability. As Tony German of Development Initiatives told us "a plethora of conditions is ridiculous because it simply does not work and it puts an immense burden on countries in trying to comply with all the conditions."[139] There are doubts too about the extent to which conditionality leads to reform, with DFID's view being that it is unlikely to persuade non-reformers to reform, but that aid with conditions attached can give governments which wish to reform their policy environment more room to manoeuvre, and add momentum to the reform process.[140]

79. Despite the criticisms of conditionality, and doubts about its effectiveness in leveraging policy change, donors will no doubt continue to attach conditions to their aid. As Tony German put it in evidence, "Nobody gives aid without having a view about where it should go and how it should be spent. It is a question of striking a balance between ownership and conditionality. You have to have a view and as a donor you have a right, even an obligation to have a view about what the money is spent on".[141] **Donors have a right and a responsibility to ensure that aid is used effectively, that recipient countries are committed to poverty reduction, and that appropriate policies are in place. However, we recognise that the external imposition of conditions can undermine local ownership and accountability. Conditionality, in some form, is sure to continue, but it needs to be practised flexibly so that countries are treated on a case-by-case basis, rather than in a one-size-fits-all manner, and so that local ownership and accountability are not undermined.[142]**

80. The ways in which conditions are arrived at is perhaps as important as what the conditions stipulate: are conditions imposed by donors, or negotiated between donors and a range of stakeholders in the developing country? In the jargon, the path to such negotiated conditionalities is one of "policy dialogue". John Roberts of ODI explained to us what is novel about "policy dialogue". He said:

> "Uganda is a perfect example, but to a lesser extent also Tanzania, Mozambique. Uganda particularly in the late eighties was not developing in the free market [mould],[143] it had pegged exchange rates, it had all kinds of discouragements. Uncharacteristically, the donors did not come in with a battle axe. They very gently suggested possibilities for moving to a free market. To begin with nothing happened. By about 1992/93, by a process of gentle persuasion, it had reached the point where, when advice was needed, where Uganda had sometimes turned internally to the ministry of finance, the ministry of finance would then turn to the aid donors. The aid donors fed in a message about the need for a poverty related pattern of public expenditure that led the Ugandan Government to decide what, in the light of its priorities, would be the right way to do that. They came up with their own list and in this way a pattern of public expenditure was arrived at which has now borne fruit and the rate of poverty in Uganda has gone down from over 50 percent to under 30 percent. The important thing was that the donors were willing to play it long, they did not push Uganda too hard, they condoned things like an export tax on coffee in 1994. They

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[139] Q21

[140] The case for aid for the poorest countries, DFID/HM Treasury, March 2002—copy placed in library. See footnote 114 for web-site.

[141] Q40

[142] *Ibid.*

[143] The assumption made here, and perhaps borne out by subsequent results, is that Uganda needed to develop in a free market direction.

showed that they were willing to trust the Ugandans and in the end they were rewarded."[144]

81. If the MDG targets are to be met, and more aid is to be provided by donor countries, aid effectiveness will have to be improved. There is much scope for improvement, and substantial international agreement on the measures needed to produce such improvements: good governance and a commitment to poverty reduction on the part of aid recipients; the timely and harmonised delivery of sufficient quality untied aid on the part of aid donors; and the flexible and sensitive use of targeting and conditionality to govern aid allocations and donor-recipient relationships. Most importantly, **attaining the MDG targets will require a change in the relationship between donors and recipients, and the construction of development partnerships which allow for sufficient ownership at the local level, including in the production and implementation of Poverty Reduction Strategy Papers (PRSPs).** (See also paragraphs 88 and 89). As Clare Short put it:

> "we are trying to move it from 'We're the donors, we'll tell you what to do; jump over all these hurdles or you can't get your money', to 'This is a partnership, we have agreed on this Poverty Reduction Strategy together; let's check that it's on track'. And, often, with goodwill, countries go off the track a bit, they might have a drought, commodity prices might fall, and then it is a question of helping them to get it right, not always just saying 'You're off track, we'll cut off the money.' So we are trying to change the culture of how we interpret those conditionalities, and that work is going on and is a constant endeavour".[145]

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[144] Q59
[145] Q118

VII. DEVELOPMENT PARTNERSHIPS AND BURDEN-SHARING

Development Partnerships: From Rhetoric to Reality

82. The much-trumpeted shift from donors imposing conditionality on developing countries, to the practice of policy dialogue is part of what the Chancellor referred to as a change in the "international atmosphere",[146] and an increased emphasis being given to shared responsibilities and balanced partnerships. The suggestion that international development ought to be about partnership is far from new, dating back to at least the Pearson Commission's Report of 1969 on Partners in Development which proposed the 0.7 percent ODA target. However, the idea of partnership has been re-invigorated, particularly since the OECD/DAC report of 1996 on Shaping the 21st Century.[147]

83. At the beginning of the twenty-first century, partnerships—or at least talk of partnership—are everywhere in international development, in the eighth of the MDGs ("Building a global partnership for development"), in the Monterrey Consensus, in the concept of global-burden sharing, in WSSD Type II outcomes, in the USA's Compact for Development, in the New Partnership for Africa's Development, in PRSPs, and in DFID's Partnership Programme Agreements with the major UK NGOs. What matters though, is the practice of international development, rather than the rhetoric. As ODI put it in evidence, "Partnership is a much-used word in development cooperation. It can sometimes offer little more than a fig-leaf to hide covert conditionality, with accountability working one way, from the recipient to the donor. At its best, however, partnership really does offer a new way of doing business: genuine debate about policy, clear commitments on both sides, good procedures for independent review, and the possibility of redress if things go wrong".[148]

84. Fundamentally, partnerships are agreements between two or more parties to work together in pursuit of shared goals. They are entered into voluntarily by participants, on the basis of overlapping objectives, and often, shared perceptions, and entail a commitment to work together, and to make decisions together, until the objectives are achieved. Effective partnerships make clear the rights and obligations—including the expected roles and contributions—of all the partners, and may well codify such agreements in the form of rules, codes and standards.

85. Indeed, the first three building blocks of the Chancellor's proposed Global New Deal concern rules of the game, codes, and standards, in relation to finance, investment and trade, with only the fourth building block concerning resource transfers.[149] Effective partnerships will also—in addition to being conducted transparently—include mechanisms for monitoring, preferably independent monitoring. The first purpose of monitoring is to check on participants' performance of their assigned roles and compliance with the rules; the second purpose is to evaluate progress towards the objectives so as to facilitate joint-learning. The final feature of effective partnerships is some sanctioning mechanism to punish a partner who fails to comply with the pre-agreed terms of the partnership, no matter whether the partner in question is powerful or relatively powerless. Workable mechanisms for coordinating joint actions exist in many spheres of social life; they would surely be of benefit in the sphere of international development. As ODI argued: "if you are a couple of plumbers working together and one of you lets the other down, there is a contract. You have a partnership agreement and, if the worst comes to the worst, you go to court. If an OECD

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[146] Q121

[147] Shaping the 21st Century: The contribution of development cooperation, OECD/DAC, May 1996.

[148] Not printed—see http://www.odi.org.uk/opinions/3_aid_architecture.pdf

[149] Tackling poverty: A global new deal—A modern Marshall plan for the developing world, HM Treasury, February 2002. See footnote 13 for web-site.

donor lets Ghana down there is absolutely nothing Ghana can do about it except to feel cross".[150]

86. In the real-world of international politics, national interests, distrust, misunderstanding, and massive inequalities of power and resources, the construction of effective partnerships is a huge challenge. If asymmetries of power are not to undermine partnerships, all participants must be accountable for their actions. In addition, safeguards must exist to protect the relatively powerless, and efforts must also be made to build the capacity of weaker partners, empowering them to play a fuller role in the development partnership. We are glad that DFID understands the importance of making partnerships more equal, as illustrated for instance in its efforts to build the negotiating and legal capacities of developing countries in the trade sphere.

87. Whilst the construction of development partnerships is a challenge, many organisations have taken up the challenge. Development partnerships, or incipient development partnerships, have been established at a variety of scales from local and project-based agreements, through national PRSPs, regional and continental partnerships, to the global new deal. Some of these partnerships employ mechanisms of mutual accountability, ranging from loose peer reviews to formal contractual arrangements. Global partnerships set the context for more local partnerships, in some cases providing resources and capacity-building assistance to make local partnerships work; the objectives enshrined in global partnerships will only be achieved if local partnerships can be made effective. This interplay between global and local partnerships is expressed in the tension between externally-imposed conditionalities, developed from global models and agreements about the conditions of aid effectiveness, and the need for local ownership of development strategies.

88. At country level PRSPs are the key mechanism through which the international community hopes to make progress towards the MDG targets. PRSPs are intended to provide a better balance between local ownership and externally-imposed conditionalities, but, as we heard during the course of our recent inquiry into European development assistance, and as the IMF and World Bank acknowledge, there is much room for improvement.[151] In particular, there needs to be more transparency, more room for country ownership, and more debate, including parliamentary debate about priorities, and parliamentary scrutiny of spending. In addition, as WDM pointed out in their evidence, if PRSPs are to be truly locally owned, the participation of in-country civil society, able to hold its government to account, is crucial.[152]

89. The PRSP process is full of promise, but if it is to deliver on poverty reduction, greater priority will have to be given to local ownership. As the Chancellor put it: "I think the key is how successful the Poverty Reduction Strategies are going to be in the future, because, in theory, these are country-owned, indeed, they are not just country-owned but they are civil society and community-owned, and obviously they have not been going for a great deal of time, but we believe that that is the key to future success. And I think there is some evidence that they give that sense of ownership, and there is some evidence also that they are working".[153] We intend to keep a close eye on developments in the PRSP framework, and on the implementation of PRSPs on the ground.

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[150] Q64

[151] See http://www.worldbank.org/poverty/strategies/review/earlyexp.pdf for the World Bank's review of the PRSP process.

[152] Ev 112, para 13

[153] Q118

90. Rwanda provides a second instance of partnership at a local scale; the shared objectives, long term commitment, and independent monitoring. Clare Short recounted the story to us, explaining:

> "So we got involved, trying to get others in, who would not go to Rwanda, because it was difficult politically, to commit aid resources over time, to get the Bank and the Fund to have a slightly more ambitious programme for the country. And this route led us to a memorandum of understanding, the UK with Rwanda, committing long term our resources, behind a reform agenda, in a high risk environment, and Rwanda tends to be very scarred by its history and not trust anyone very much. So we agreed that the Rwandan Government would commit to reforms, we would commit to deliver, and there would be an independent monitoring of how we both kept to our commitments. And that has been seen as a model, in some parts of the world. It really has helped move Rwanda forward."[154]

91. On a larger scale there is the New Partnership for Africa's Development (NEPAD). NEPAD will, as part of its accountability mechanisms, make provision both for peer review of African countries' adherence to agreed standards of good governance, and, for African countries to review the practices of donor countries. The intended objective of the peer review process is to encourage mutual learning, monitor progress towards agreed goals, apply peer pressure on governments to adhere to agreed standards and benchmarks, and to disseminate good practice. Of longer pedigree, there is the Cotonou Agreement—formerly Lomé Convention—which governs relationships between the European Union and its African, Caribbean and Pacific (ACP) partners. The Cotonou Agreement is perhaps the most contractual of international development partnerships, including joint parliamentary assemblies and arbitrators, and legally enforceable reciprocal agreements. In their evidence, ODI suggested the Cotonou Agreement as a possible model of partnership, explaining that:

> "The Cotonou Agreement between the EU and 77 ACP countries covers aid, trade and the political relationship. It is governed by a joint Council of Ministers on which all parties sit. If the provisions of the Agreement are broken, with respect to human rights, democratic principles, or the rule of law, then 'appropriate measures' may be taken, including suspension. The joint Council of Ministers acts as a court of appeal, but independent arbitration is also available. This framework has yet to be tested fully, but it has real potential and should be extended to make EU countries more accountable".[155]

The Cotonou Agreement certainly has its critics,[156] with serious questions being asked about the nature of the partnerships between powerful aid-wielding EU countries and their ACP partners, and about the balance between local ownership and imposed conditionalities, but as Poul Nielson, the EU's Development Commissioner, put it when we visited Brussels in February, the Cotonou Agreement is "the only thing on earth between north and south with such a contractual relationship in it".[157]

92. **Partnerships are not a panacea for international development, but they do offer a way forward. The Committee is keen to play its role in the construction of a global partnership for development. Indeed we believe that parliaments and parliamentarians—in the developed world, the developing world, and in collaboration with each other—have important roles to play in helping to ensure that development partners live up to their promises, and that global partnerships are translated into national and local legislation and local action. We urge DFID, along with networks**

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[154] Q121

[155] Not printed—see http://www.odi.org.uk/opinions/3_aid_architecture.pdf

[156] See, for instance, Reality of Aid, 2002, pp.131–134.

[157] Q210 of evidence given to the Committee in relation to its recent inquiry into the effectiveness of the reforms of European development assistance. See Second Report from the International Development Committee, Session 2001-–2002, *The effectiveness of the reforms of European development assistance*, HC417.

such the Commonwealth Parliamentary Association, the Inter-Parliamentary Union, and the Parliamentary Network on the World Bank to help build the capacity of developing countries' parliaments to play their role in scrutinising decision-making and spending on their side of the emerging global development partnership.

Burden-Sharing and the Role of the USA

93. In our view, global partnerships for development must include the USA. Without the USA's active participation, the MDG targets will not be reached. If the USA does not share the burden of financing, the US$50 billion extra per year required to finance the achievement of the MDG targets will not be raised. We warmly welcome therefore, the USA's renewed commitment to international development, signalled by the 50 percent increase in ODA announced by President Bush shortly before the Monterrey Summit. We heard in evidence that the USA was a determined negotiator in the run up to Monterrey, objecting to mentions of the 0.7 percent target and the MDGs in the Monterrey Consensus,[158] and seeking to dilute and exclude the more radical proposals put forward in the Zedillo Report.[159] We have also heard the USA's explanations: the USA never agreed to what it sees as the now-outdated the 0.7 percent target; the USA regards effectiveness rather than volumes of ODA as most important; the USA is the greatest source of private capital to developing countries; the USA leads the world in charitable donations to developing countries; and, the USA, whilst signing up to the Millennium Declaration, had not endorsed the subsequent road map of targets, indicators and deadlines.[160]

94. Given this background, the aid increases announced by the USA were an extremely welcome surprise. However, it must be remembered that even after the increases in aid come fully on stream in 2006, ODA provided by the USA will still amount to only 0.15 percent of its national income. The US Government is not generous with its aid. As Jenny Ross of BOND reminded us, "For the US, the extra annual spending of $11 billion required to meet the 0.7 percent target represents around a quarter of the increase in military spending scheduled for 2003 and announced after 11 September, and a seventh of the tax cuts for the period 2002–2014".[161] **Persuading the USA to engage seriously with international development issues, to support rather than undermine an emerging multilateralism, and to share the burden of financing development, remains a challenge.**

95. The announced aid increases are a key component of President Bush's new Compact for Development, a compact which is described as a shared effort between developed and developing nations to stop the cycle of poverty in the developing world. The Compact for Development is to be a "new partnership between the United States and those governments in developing countries that have made and are demonstrating a commitment to domestic reforms that are necessary for sustained growth".[162] A second component of the Compact is the Millennium Challenge Account, the structures through which the new funds will be disbursed. In this results-oriented approach, developing countries which wish to gain access to funds will have to show that they are implementing sound policies that promote growth, development and also poverty reduction.

96. The underlying philosophy which apparently guides this highly selective approach to allocating and targeting aid is that "we want to do the greatest good for the greatest number of people".[163] To access funds, developing countries will have to demonstrate commitment to: firstly, good governance, including measures to root out corruption, uphold

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[158] Q4
[159] Ev 7
[160] Ev 26
[161] Q22
[162] Ev 27
[163] Ev 28

human rights, and adherence to the rule of law; secondly, its people, by investing in their health and education; and, thirdly, sound economic policies, including open markets, sustainable budget policies, and the fostering of enterprise and entrepreneurship.[164]

97. In a spirit of openness, the USA has been keen to solicit external comments on its proposed Millennium Challenge Accounts to inform its design of the new mechanisms. We hope that the USA will continue to consult widely and that our comments, and subsequent discussions, will assist in the debate about how best to contribute to the generation of a global partnership for development. As discussed above (see paragraph 76), we too believe that the effectiveness of aid should be maximised through careful and sensible allocations, and we believe that President Bush's initiative is proposed in good faith as a serious effort to renew American engagement with international development issues.

98. However, we do have some concerns about the Millennium Challenge Accounts, particularly about the sort of partnership that they and the USA's Compact for Development represent:

- We believe that rather than setting up a separate mechanism—the Millennium Challenge Accounts—it would be better if the USA were to move in the direction of harmonising the delivery of its aid with other major donors. Ideally, we would like to see the USA pooling its funds with those of other donors, supporting the PRSP approach, and, where prudent, providing direct budget support.

- We trust that the primary objective of the Millennium Challenge Accounts will be poverty reduction and elimination, and that assessments of countries' performance, and allocation decisions, will be driven by this objective, and by evidence-based models of development and of how aid works. The USA should make explicit the criteria which govern the allocation of Millennium Challenge Account funds, and desist from imposing additional restrictions on its aid. We are particularly concerned about the consequences for reproductive health services of the restoration of the "Mexico City Policy" which demands that NGOs in receipt of US aid must not perform abortions or promote abortion services.

- We trust that the allocation criteria will be applied flexibly and sensitively, taking account of individual countries' circumstances. We are particularly concerned that if the allocation criteria are applied too strictly the result may be that more money goes to Latin America at the expense of poorly-governed and conflict-ridden countries in sub-Saharan Africa. We are glad that at the recent G8 summit it was announced that 50 percent of the ODA increases announced previously at Monterrey will be earmarked for sub-Saharan Africa.

- We hope that the USA will recognise that development strategies need to be locally owned if they are to be successful, and will take account of this when it assesses countries' commitments to good governance and sound economic policies, and attaches conditions to its aid.

99. **We recognise the importance of engaging with the USA, as regards the Millennium Challenge Accounts, and in relation to its development-related activities in general.** As Clare Short put it: "you cannot not engage with the world's biggest economy and the world's only great power".[165] **DFID should seek to influence the establishment of the USA's Millennium Challenge Accounts to ensure that they are informed by up to date development thinking, focussed on poverty reduction, and do not neglect poor and poorly-governed countries, for instance in sub-Saharan Africa.** For our part, we

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[164] *Ibid.*
[165] Q115

intend, in the next session of Parliament, to engage further with parliamentarians and staff of the international financial institutions in Washington, D.C.

VIII. CONCLUSIONS

100. The Financing for Development process has been highly successful in focussing attention on international development and the resources needed to meet the MDG targets. As a consequence, there is now much greater awareness of the huge resource gap. If the Monterrey Summit is ultimately to be judged a success in terms of its contribution to meeting the MDG targets, this resource gap must be filled and soon. There has been enough discussion; now is the time for action by all who are committed to the Millennium Development Goals and the elimination of global poverty. Southern governments must commit themselves to poverty reduction and good governance. Northern governments—including our own—must fulfil their promises to provide sufficient, timely and quality aid, and to work for a fairer world in which no country is denied the opportunity to develop because of a lack of resources. Now is the time to make the global new deal a reality.

101. The UK Government is committed to eliminating poverty globally and to making globalisation work for the poor. The Chancellor has argued that the elimination of poverty is a moral imperative, a social duty and an economic necessity.[166] We agree wholeheartedly, and would add too that reducing poverty is a precondition for global security and integral to environmental sustainability. The Government recognises that the provision and mobilisation of finance for development is crucial to developing countries' efforts to meet the MDG targets and eliminate poverty, and appreciates the role that aid will continue to play. Aid should indeed be seen as investment; there is enough hard evidence to show that aid spent wisely produces excellent returns in terms of eliminating poverty. We welcome the Government's willingness to back up its development rhetoric with increased aid resources in the recently announced spending review, and urge continued efforts to improve the effectiveness of aid and to move quickly towards the 0.7 percent target.

102. **The case for aid is powerful. It is our strong belief that the Government could and should make the case for aid and international development even more strongly than it currently does, in international fora, to our EU partners, and to the electorate.**[167] As the Chancellor put it, prior to announcing in the spending review that UK aid will reach £4.9 billion per year by 2006: "it does come back to whether individual countries are prepared to say that they themselves are prepared to spend more, one way or another; because, if you are to raise money, you have got to get the consent of your own domestic legislature, whatever country you are, to do so".[168]

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[166] Tackling poverty: A global new deal—A modern Marshall plan for the developing world, HM Treasury, February 2002, p.1. See footnote 13 for web-site.
[167] See Development Initiatives' outline proposal for a UK Council for International Cooperation—copy placed in library and see http://www.devinit.org/cic.htm
[168] Q123

ACRONYMS

ACP	African Caribbean Pacific countries—the EU's partners in the Cotonou Agreement
BOND	British Overseas NGOs for Development
CTT	Currency Transactions Tax—"Tobin Tax"
DAC	Development Assistance Committee of the OECD
DFID	Department for International Development
FDI	Foreign Direct Investment
FfD	Financing for Development
GNI	Gross National Income—the measure of national income which has replaced GNP
HIPC	Heavily Indebted Poor Countries debt relief process
IDA	International Development Association—the World Bank's concessional lending window which lends to the poorest countries
IMF	International Monetary Fund
MDGs	Millennium Development Goals
NEPAD	New Partnership for Africa's Development
NGOs	Non-governmental Organisations
ODA	Official Development Assistance—Aid to developing countries
ODI	Overseas Development Institute
OECD	Organisation for Economic Cooperation and Development
PRSPs	Poverty Reduction Strategy Papers
SDRs	Special Drawing Rights
UN	United Nations
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
WDM	World Development Movement
WSSD	World Summit on Sustainable Development
WTO	World Trade Organisation

LIST OF MAIN CONCLUSIONS AND RECOMMENDATIONS

The United Nations Conference on Financing for Development: From preparations to outcomes

1. **We welcome the improved coordination between the various international organisations and feel that such efforts are crucial if there is to be policy coherence as regards international development. The appropriate response to greater coordination between the International Financial Institutions and the more democratic United Nations is to strengthen the voice of developing countries in all fora, rather than to decry such coordination (paragraph 8).**

2. **We commend the Government on its active role during the Financing for Development process, and trust that it will endeavour to inject international discussions and actions to meet the Millennium Development Goals (MDGs) with a sense of urgency (paragraph 11).**

3. **We share some of the disappointment which critics of the conference have voiced, but are keen to maintain the momentum gained at Monterrey rather than dwell on what might have been (paragraph 13).**

4. **We warmly welcome the aid increases announced by the EU and the USA. But, the success of the summit must ultimately be assessed in terms of its contribution to meeting the MDG targets. As such, it is too early to judge the summit's success. Thus far, little has been achieved and nothing has been implemented. If the Monterrey Summit is to be seen as a turning point rather than a talking shop, the international community must implement quickly the agreements reached, and use them as a starting point for a concerted international effort to eliminate poverty (paragraph 15).**

Resource flows: The big picture

5. **Financing for development must be considered in the round; the focus should not be solely on aid. Non-aid flows of resources are crucial for developing countries' prospects of meeting the MDG targets (paragraph 25).**

6. **If developing countries are to escape poverty they must take responsibility for their own development. Developing countries will need to establish policy environments, and local banking and financial systems, to both retain and mobilise domestic resources, and to attract and retain international resources (paragraph 20).**

7. **Developing countries must show that they are taking strong measures to tackle corruption and money laundering so that countries' resources benefit all the people rather than corrupt elites. Developed countries must rigorously enforce their own anti-corruption laws and insist that financial transactions by firms with developing countries are open and transparent (paragraph 21).**

8. **The current situation in which Northern governments advocate trade liberalisation whilst themselves engaging in agricultural protectionism is a disgrace, and puts at risk not only the Doha trade round, but also the MDGs. The developed countries must act now to eliminate agricultural subsidies and to enable developing countries to sell their products in**

Northern markets. We urge the Government to do its utmost to bring such changes about. We will be monitoring progress very closely (paragraph 26).

9. **We remain supportive of the Heavily Indebted Poor Countries (HIPC) process, but recognise that there are serious problems which require addressing, particularly as regards the speed of the process, the linking of debt relief to development needs, and the likelihood of countries exiting HIPC with sustainable debt burdens. The HIPC process must also be flexible enough to cope with the diversity of circumstances which developing countries face, including those which are emerging from conflict (paragraph 33).**

10. **Debt relief must provide additional real resources, and must never be provided at the expense of other official development assistance (ODA) flows (paragraph 36).**

11. **There are various flows of financial resources, any of which might be tapped by developing countries, but only aid can be truly focussed on poverty reduction. We are glad that DFID, the Treasury and the Government are so supportive of aid, and encourage them to continue to push the case for aid in both domestic and international fora (paragraph 38).**

Innovative sources of finance for development

12. **We share with many advocates of currency transactions taxes (CTTs) the view that exchange rate volatility contributes to poverty and hinders development, and we too wish to see more financial resources available for development. Many taxes—taxes on smoking, motoring, pollution—have two apparently contradictory purposes. This is not a significant criticism of CTTs, but the question remains as to whether a CTT is the best way, either of reducing speculation or of raising revenue. If we are to be persuaded fully, further investigation into issues of feasibility and practicality will be needed (paragraph 46).**

13. **In our view it is imperative that generating the political will to finance development remains the central focus, and that the choice of methods by which to collect funds remains a secondary consideration (paragraph 46).**

14. **We are supportive of the Government's position on special drawing rights (SDRs). If the fourth amendment were ratified it would provide a welcome one-off increase in global liquidity, and might provide some resources for development. We encourage the Government to continue to press this case (paragraph 51).**

15. **We recognise the problems associated with proposals to use SDRs to finance development, but consider that there might be a limited role for SDRs, perhaps as part of an International Development Trust Fund (paragraph 51).**

16. **There is a funding gap which can only be filled by substantial North-South resource transfers. Such resource transfers will only be possible if sympathetic Northern governments show real political leadership, both in persuading other countries, and in securing domestic public support for the necessary resource transfers (paragraph 55).**

Official development assistance: Volumes

17. **If the MDG targets are to be met, there must be a massive increase in aid flows to developing countries. Making aid more effective is crucial too, but there is universal agreement that aid volumes will have to increase substantially (paragraph 56).**

18. **As far as the UK is concerned, recent years have seen welcome increases in aid contributions, from US$3.2 billion in 1997 to US$4.5 billion in 2000, raising the UK's contribution from 0.26 to 0.32 percent of Gross National Income (GNI), and bringing the UK level with France in these terms. In the recent spending review, the Chancellor announced that UK aid will rise to 0.4 percent of GNI by 2006. This increase, whilst leaving the UK well short of its 0.7 percent commitment, will lift it well above the current OECD/DAC average of 0.22 percent, enable it to meet and exceed the EU target of 0.39 percent by 2006, and reinforce the UK's position as the most generous G7 donor in ODA/GNI terms (paragraph 59).**

19. **We recommend that the Government follow the example of Belgium and Ireland in setting a date—a date which is sufficiently in advance of the 2015 MDGs' deadline—for reaching 0.7 percent, and a timetable for hitting that target (paragraph 62).**

Official development assistance: Effectiveness

20. **The estimated poverty-reduction productivity of ODA nearly tripled during the 1990s (paragraph 63).**

21. **We believe strongly that there need not be a tension between aid volume and aid effectiveness, and that improvements in aid effectiveness are essential if increases in aid volume are to be generated. As such, we are firmly of the view that donors and recipients of aid must work together to improve the effectiveness of aid. (paragraph 64).**

The good recipient

22. **Developing countries—their governments, but also civil society, business and the media—have the primary responsibility for ensuring that aid is used effectively. The ineffective use of aid or the diversion of aid into the pockets of elites pushes the poor deeper into poverty and robs them of the assistance provided to them. (paragraph 65).**

23. **The pre-requisite for poverty reduction and the effective use of aid is the commitment of the recipient government to poverty reduction (paragraph 66).**

The good donor

24. **We recommend that DFID, considers adopting a target for its aid allocation to basic social services, encourages its fellow DAC members to increase their allocations in line with the 20/20 Initiative, and, continues to encourage the recipients of its aid to prioritise spending on universal access to basic social services. (paragraph 67).**

25. **We applaud the Government's actions in untying UK aid, and encourage the Government to continue its efforts to persuade its more recalcitrant European partners to untie their aid too (paragraph 69).**

26. **Ideally, and subject to an assessment of the risks involved and the requirement of accountability, aid is best provided through direct budget support. (paragraph 70).**

27. **The choice of aid instruments—as well as the allocation of aid and the selection of development interventions in general—must take account of country specifics rather than follow a preset formula (paragraph 70).**

Aid as investment

28. **Aid should be conceptualised as investment. However, careful attention does need to be paid: first, to the allocation criteria which drive aid/investment decisions; second, to the implications for countries which are seen as offering low rates of return; and, third, to the nature of the conditions which investors might attach to aid flows (paragraph 71).**

29. **It would be helpful if DFID made explicit its underlying model of the ways in which aid is effective and its aid allocation criteria, and encouraged other donors to do the same. Such transparency is fundamental to any notion of a shared and jointly-owned development partnership, and would provide developing countries with the information necessary to—if they so wish—improve their performance in terms of the criteria (paragraph 75).**

30. **Aid resources must not be squandered in countries which lack the commitment to development and poverty reduction. In addition, aid must not be used to prop up governments that are not furthering the interests of their people. This must not mean that we forget such countries, or, more specifically, the millions of poor people who live in such countries. Rather, the nature of donor engagement with such countries—countries which the World Bank labels Low-Income Countries Under Stress or LICUS—ought to be different (paragraph 76).**

31. **Donors have a right and a responsibility to ensure that aid is used effectively, that recipient countries are committed to poverty reduction, and that appropriate policies are in place. However, we recognise that the external imposition of conditions can undermine local ownership and accountability. Conditionality, in some form, is sure to continue, but it needs to be practised flexibly so that countries are treated on a case-by-case basis, rather than in a one-size-fits-all manner, and so that local ownership and accountability are not undermined (paragraph 79).**

Development partnerships and burden-sharing

32. **Attaining the MDG targets will require a change in the relationship between donors and recipients, and the construction of development partnerships which allow for sufficient ownership at the local level, including in the production and implementation of Poverty Reduction Strategy Papers (paragraph 81).**

33. **Partnerships are not a panacea for international development, but they do offer a way forward. The Committee is keen to play its role in the**

construction of a global partnership for development. Indeed we believe that parliaments and parliamentarians—in the developed world, the developing world, and in collaboration with each other—have important roles to play in helping to ensure that development partners live up to their promises, and that global partnerships are translated into national and local legislation and local action. We urge DFID, along with networks such the Commonwealth Parliamentary Association, the Inter-Parliamentary Union, and the Parliamentary Network on the World Bank to help build the capacity of developing countries' parliaments to play their role in scrutinising decision-making and spending on their side of the emerging global development partnership (paragraph 92).

34. **Persuading the USA to engage seriously with international development issues, to support rather than undermine an emerging multilateralism, and to share the burden of financing development, remains a challenge (paragraph 94).**

35. **We recognise the importance of engaging with the USA, as regards the Millennium Challenge Accounts, and in relation to its development-related activities in general (paragraph 99).**

36. **DFID should seek to influence the establishment of the USA's Millennium Challenge Accounts to ensure that they are informed by up to date development thinking, focussed on poverty reduction, and do not neglect poor and poorly-governed countries, for instance in sub-Saharan Africa (paragraph 99).**

Conclusions

37. **The case for aid is powerful. It is our strong belief that the Government could and should make the case for aid and international development even more strongly than it currently does, in international fora, to our EU partners, and to the electorate (paragraph 102).**

PROCEEDINGS OF THE COMMITTEE RELATING TO THE REPORT

WEDNESDAY 17 JULY 2002

Members present:

Tony Baldry, in the Chair

Hugh Bayley	Chris McCafferty
Mr Tony Colman	Mr Andrew Robathan
Mr Piara Khabra	Tony Worthington

The Committee deliberated.

Draft Report [Financing for Development: Finding the money to eliminate world poverty], proposed by the Chairman, brought up and read the first time.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraph entitled 'Summary' read and postponed.

Paragraphs entitled 'Background and Acknowledgements' read and agreed to.

Paragraphs 1 to 102 read and agreed to.

Postponed paragraph entitled 'Summary' read again and agreed to.

Resolved, That the Report be the Fifth Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

Ordered, That the provisions of Standing Order No. 134 (Select committees (reports)) be applied to the Report.

Several papers were ordered to be appended to the Minutes of Evidence.

A paper was ordered to be reported to the House.

[Adjourned till Tuesday 23 July at half past Ten o'clock.

LIST OF WITNESSES

Tuesday 23 April 2002

Belen Vazquez, ActionAid, Jenny Ross, British Overseas NGOs for Development (BOND), and Judith Randel and Tony German, Development Initiatives . . . . Ev 15

Tuesday 30 April 2002

Mr Simon Maxwell, Director, and Mr John Roberts, Head of CAPE (Centre for Aid and Public Expenditure), Overseas Development Institute, and Professor Paul Mosley, University of Sheffield . . . . Ev 53

Professor Paul Bernd Spahn, Goethe University, Frankfurt, and Mr Steve Tibbett, Senior Campaigner, War on Want . . . . Ev 70

Tuesday 14 May 2002

The Rt. Hon. Gordon Brown, a Member of the House, Chancellor of the Exchequer, the Rt. Hon. Clare Short, a Member of the House, Secretary of State for International Development, Mr Gus O'Donnell, Managing Director, Macroeconomic Policy and International Finance, HM Treasury and Mr Barrie Ireton, Director General (Programmes), Department for International Development . . . . Ev 84

LIST OF MEMORANDA INCLUDED IN THE MINUTES OF EVIDENCE

1. ActionAid .... Ev 1, 35
2. British Overseas NGOs for Development (BOND) .... Ev 5, 35
3. Development Initiatives .... Ev 8, 30
4. USAID .... Ev 26
5. William S. Farish, US Ambassador .... Ev 27
6. Overseas Development Institute (ODI) .... Ev 40, 61
7. Mr John Roberts .... Ev 61
8. Professor Paul Mosley .... Ev 67
9. War on Want .... Ev 68, 99
10. Professor Paul Bernd Spahn .... Ev 75
11. Department for International Development and HM Treasury (Joint) ... Ev 78
12. Department for International Development .... Ev 100, 101
13. HM Treasury .... Ev 104

LIST OF APPENDICES TO THE MINUTES OF EVIDENCE

1. International Planned Parenthood Federation (IPPF) .... Ev 107
2. United Nations Development Programme (UNDP) .... Ev 109
3. World Development Movement (WDM) .... Ev 110
4. WWF-UK .... Ev 114

UNPRINTED MEMORANDUM

The following memorandum has been reported to the House, but to save printing costs it has not been printed and a copy has been placed in the House of Commons Library, where it may be inspected by Members. Other copies are in the Record Office, House of Lords, and are available to the public for inspection. Requests for inspection should be addressed to the Record Office, House of Lords, London SW1A 0PW (tel: 020 7219 3074). The Record Office is open to the public from 9.30 am to 5.00 pm on Mondays to Fridays.

1. New Economics Foundation