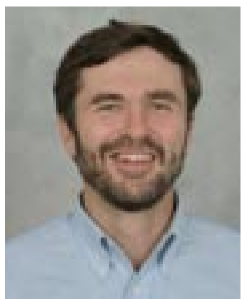
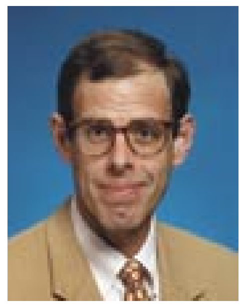
DIMENSIONS OF DEVELOPMENT

An Interview With Nicholas Eberstadt and Steve Radelet

Nicholas Eberstadt, the Henry Wendt chair in political economy at the Washington, D.C.-based American Enterprise Institute, and Steve Radelet, senior fellow at the Washington, D.C.-based Center for Global Development, respond to questions about the goals of the Millennium Declaration and U.S. development policy from the editors of Economic Perspectives.



Steve Radelet



Nicholas Eberstadt

Question: What is your assessment of progress to date by the global community in meeting the goals of the Millennium Declaration agreed to in the year 2000?

Radelet: There has been mixed progress. East Asia and South Asia have made significant progress on achieving the goals, particularly in the area of health standards, whereas countries in sub-Saharan Africa, as well as Haiti and Burma, are struggling to meet the goals.

Some countries—some of the world's largest, such as China, India, and Indonesia—are seeing rapid progress toward development. However, in other countries, there is much less likelihood that the "millennium" standards will be achieved by the 2015 target date.

The Millennium Development Goals (MDGs) are helpful in focusing the attention of the international community on establishing targets. This should help both developing countries and industrialized countries focus their attention more clearly on the problems and possible solutions. There is a worry, however, that the goals were set with arbitrary dates for achievement. The goals may have been set too high for some countries.

In the area of increasing primary school enrollment, for example, some countries may see gains, but if they don't have enough resources, they may not be able to achieve 100 percent enrollment. It has taken some countries decades to get from having 20 or 25 percent enrollment to having 50 percent. If they don't achieve 100 percent enrollment by 2015, their success should not necessarily be deemed a failure.

Eberstadt: Five years is not really enough time to judge the MDG program's effectiveness—in part because the data for so many low-income countries are so poor. We should look at longer-term measurements to get data that could substantiate the gains being achieved.

Let's look at development from a historical perspective. The 20th century, on balance, was a tremendous success for development and a huge jump forward in progress against poverty. During the century, life expectancy more than doubled. Over this same period, there was a tremendous increase in per capita income for the world as a whole.

The two greatest exceptions to this pattern of substantial advance were the detour under Communism—which is now essentially over—that affected much of the world, and the terrible record of developmental problems that emerged in sub-Saharan Africa in the 1960s and 1970s and still continue: long-term economic stagnation or economic decline, poor export performance, continuing dependence on aid, and, more recently, catastrophic health setbacks in many parts of the sub-Sahara due to the HIV/AIDS pandemic.

Q: Where has the most progress been made, and what are the major impediments to success?

Radelet: Where there has been economic growth, we've seen progress on the goals. Yet there are constraints to progress. Africa has significant geographic constraints. It has endemic diseases—significantly, HIV/AIDS—that will affect the achievement of some of the MDGs.

Botswana, for example, had been on track toward achieving the goals, especially in education and poverty reduction. But because of HIV/AIDS, the country's progress in some areas has reversed. Life expectancy in Botswana increased dramatically, going from 38 years to 61 years between 1975 and 1995. But since the mid-1990s, because of AIDS, life expectancy has fallen to about 43 years.

Another constraint Africa faces is that it has more land-locked, isolated nations than other regions. Being land-locked makes it much more difficult to participate in markets, and makes imports more expensive and exports less competitive.

We can see another geographic restriction in Africa. That is, a huge desert (the Sahel) in the west. The thin dispersion of people in this area makes it difficult to deliver services and track progress toward achieving the Millennium Development Goals.

However, while several African countries currently are facing very difficult problems, including Somalia, Ivory Coast, Zimbabwe, and the Congo, it is not all doom and gloom.

For example, we see a growing number of multiparty democracies. In 1990, there were four multiparty democracies in sub-Saharan Africa. Now there are approximately 20. Such countries as Ghana, Tanzania, South Africa, Nigeria, Mozambique, Mali, and Burkina Faso have made significant political and economic progress in recent years. This is an enormous shift that most of the world has not yet grasped. Several of these countries are also achieving greater economic stabilization and stronger economic growth.

Eberstadt: In terms of overall development, progress in reducing poverty in most parts of the world has been encouraging, except in sub-Saharan Africa, which has largely been going in the wrong direction. There has also been a reversal in health care indicators because of the HIV/AIDS catastrophe.

China has experienced the most important progress, and India has made substantial progress as well.

In countries with expanding economies, there has generally been a shift from a reliance on natural resources to a greater reliance on human resources. On the whole, natural resources have become less important to national economic growth.

Q: What role in a country's development can foreign aid play?

Radelet: There are two major areas. The first is the support for education programs and health care services to fight major diseases. Aid inflows have resulted in significant improvements in curtailing diseases such as polio and river blindness and in making available oral rehydration therapy. The second is support for efforts devoted to encouraging economic growth.

In the area of health, there has been tremendous progress since World War II around the world, including in developing countries. But in the last five years, we have clearly begun to see life expectancies being pulled down by HIV/AIDS. This disease is reversing the hard-fought gains in the area of basic health indicators achieved over the previous 20 years.

But there are some places where we've seen improvements in reducing HIV/AIDS. In Uganda, for instance, because of local community education efforts funded with the help of international aid, there has been a 10 percent reduction in the incidence of the disease in recent years. Thailand and Senegal are also cited as AIDS-reduction successes, keeping rates of the disease fairly low. In some parts of Zambia, there have been recent reductions as well.

In terms of economic growth, in some cases aid has clearly failed to help achieve that goal, and there is no question that some aid has been wasted. But in some countries, such as South Korea in the 1950s and 1960s, Indonesia, and, more recently, Uganda, Mozambique, and Tanzania, aid has helped support growth. It's fair to say that aid has worked in some countries but not in others, and there is much we can do to make aid more effective in the future.

Three things in the development world have changed donors' focus on aid in recent years. The first is the terrorist attacks of September 11, 2001, which caused donors to see more clearly the link between poverty and terrorism.

The second is the increasing awareness of the seriousness of HIV/AIDS. Not too long ago, AIDS was viewed mainly as an issue of "personal responsibility." Now it is rightly seen as a pandemic affecting nations in every hemisphere.

The third is the growth of multiparty democracies, mentioned before. Whereas in the 1970s and 1980s much aid was spent on allies in the Cold War, more aid today is aimed at supporting countries that are trying to establish multiparty democracies, and the world is slowly evolving in this direction.

Eberstadt: Forms of aid other than the conventional economic official development assistance (ODA) have often been effective in helping countries to develop. Take military aid, for instance. Taiwan and South Korea are two post-World War II success stories that gained much from U.S. military aid. One consequence of this aid was to permit South Korea to move toward being an export economy. More generally, military aid may help create a security environment in which material progress is more likely.

The international economy, through trade, investment, and knowledge transfers, is also absolutely instrumental in economic growth, productivity improvement, and poverty alleviation.

ODA's role in promoting material advance is much more limited—but it can be positive in the right settings.

Q: In recent weeks, the debate over aid levels and the capacity of countries to absorb aid has been in the news. Is there a law of diminishing returns to certain levels of foreign assistance?

Radelet: There is not so much a strict law as a strong tendency. As with other financial investments, we can see diminishing returns as the amount of investment grows. Research shows that aid directed at economic growth has a smaller and smaller impact as the amount of aid grows, but still tends to remain positive until aid is approximately 18 to 25 percent of a country's gross domestic product.

The issue is where the aid is directed. Aid directed to steady economic growth has had a stronger impact on growth than other forms of aid, such as that directed to humanitarian concerns and for hard-to-measure programs like judicial reform. It takes 10 to 15 years or more before results of judicial reform can really take hold. It is easier to measure results of aid for such things as agricultural development and the building of roads, since the results are easier to quantify and generally take less time to be realized.

One of the challenges going forward is to make aid more effective, both in terms of who it is provided to and how we provide it, to make sure we get the strongest impact possible for our aid dollars.

Eberstadt: Aid effectiveness depends critically on the economic environment in which it is introduced. Where disciplined and productive policies exist, resources are likely to generate higher returns.

The critical question is how extra concessional resources can affect the policy environment. The results of aid depend on a combination of timing, the recipient country's leadership—its mode of government—and its history.

One troubling phenomenon since the mid-1990s has been the increasing reliance of sub-Saharan Africa on official development assistance. In fact, heavy aid dependence in Africa's economies has been apparent—even increasing—since the 1970s. We have to wonder whether a surfeit of aid hasn't been "crowding out" export growth and domestic capital formation in parts of the sub-Sahara over the past generation. This might be part of the explanation for the area's strikingly poor long-term economic performance.

Q: What role do you see such programs as the U.S. Millennium Challenge Account (MCA), the African Growth and Opportunity Act (AGOA), and the Heavily Indebted Poor Country (HIPC) program* playing in the overall poverty reduction strategy?

Radelet: The $40-billion debt reduction deal announced during the meeting of the Group of 8 (G8) in July 2005 is a historic agreement that could end two decades of debt problems for at least 18 poor countries, and possibly for more. The challenge now is to help recipient countries achieve sustained economic growth and poverty reduction so they don't end up with unpayable debts again.

Unfortunately, the deal leaves out many countries that had not borrowed enough to be considered heavily indebted, such as Kenya, Nigeria, and Sri Lanka. A similar deal should be offered to these countries. Aid should be directed to countries that are the poorest, not the most indebted.

The Millennium Challenge Account is a very important program conceptually. The general idea behind it is to have a more favorable and flexible mechanism for providing aid directed at countries that have shown the strongest commitment to good development policies. Its success in practice remains to be seen.

AGOA has been particularly useful, as it is based on the U.S. opening up its markets to African countries, allowing them to engage in global markets and produce goods that can help support long-term growth.

Eberstadt: The Millennium Challenge Account is a noble concept, but the program has been hard to operationalize so far. The program is too small to have much of an impact through "non-lending." That is to say, the MCA is not a large enough "player" to have much of an effect on the behavior of aid recipients or on the practices of other donors who account for most development grants and loans.

The MCA is intended to embody the World Bank's experimental concept of "selectivity" in deploying resources where they can have the greatest impact. Yet part of the reason donors have a hard time embracing selectivity is that they just can't say "no aid" for many countries. The donors' political relationships with aid-receiving governments are all too often more important than the actual development results achieved through these transfers. Under such circumstances, selectivity is all but impossible.

Q: How important are transparency and accountability to the effectiveness of aid? What can be done to improve governance?

Radelet: Better policies and public institutions both strongly affect a country's growth. Countries with strong institutions and healthy populations can absorb more aid than countries where there is a lot of corruption and people are less healthy.

There have been instances in the past—mainly during the Cold War—in which donors were too willing to give aid to countries where corruption was known to exist. This colored the public's view about the overall effectiveness of aid.

Eberstadt: One factor in corruption or in the misappropriation of aid funds is the political awareness of donors.

There is a positive relationship between economic development and rule of law. Rule of law is an important objective. Where there is more transparency accompanying rule of law, there is less investment uncertainty and lower transaction costs, and it is easier for economic activity to progress.

In many societies, wealth is distributed unevenly. But if a poor person knows he or she has legal protections, there is an almost revolutionary move toward equality.

Q: If fraud is found, should countries be cut off from development assistance?

Radelet: In many cases, yes, but not always. The fact that institutions in some counties are rife with corruption is at least partially because of poverty itself. It takes both strong local commitment and money to help build strong institutions that can work to prevent corruption in various sectors. It is not just a matter of internal political will.

Donors need to be much more specific about what they expect from aid.

Eberstadt: It depends entirely on what the objectives of the aid are, such as if aid is being allocated for military or political security purposes. When appropriation of funds is being compromised, there is a much stronger argument for ending humanitarian relief programs.

Q: What are the problems with policy conditionality? Some have argued that while fiscal restraint, trade liberalization, deregulation, and privatization are good things, the speed and the depth of such measures are critical to the success of development policy.

Radelet: We have learned that donors cannot just impose reforms from the outside, nor can they "buy" reforms with promises of more aid. Countries must be committed to strong reforms in the first place. Aid can be used to help provide support to good policies, but it can't force the implementation of those policies.

Eberstadt: Conditionality is desirable. But donors have a poor track record on achieving conditionality. Conditionality cannot occur where aid cannot be "cut off"—but how many examples can we find over the past generations wherein recipient governments have suffered aid cut-offs for adverse performance on their development programs?

Q: Any number of schemes have been forwarded to finance development—an International Finance Facility, global tax, SDRs (special drawing rights) for development purposes. In light of the huge demands on countries, what do you think are the best approaches to financing development?

Radelet: It is always good to think of innovative new systems for helping countries develop economically and reduce their debt. But no one system is a "silver bullet."

And none of these new ideas will wholly substitute for traditional aid flows or for private sector flows, which have become particularly important in middle-income countries.

The World Bank and the African Development Bank should provide more money as grants rather than loans, especially to the poorest countries. Countries with average annual per capita incomes below a certain level should get grants because they face the deepest development challenges and are most vulnerable to economic shocks.

But grants should not be just giveaways—they should be performance based. They should be clearly aimed at achieving specific targets, such as building certain roads or establishing certain numbers of health clinics. Donors should reward success in achieving goals with more aid, and penalize countries that do not meet specified goals.

Eberstadt: For highly indebted low-income countries with debt servicing problems, we have to remember that the contracted loans have usually been been highly concessional, but the returns generated on these loans have all too often been abysmally low.

In many low-income highly indebted countries, economic problems will not be solved simply through debt forgiveness. The problem with repaying concessional loans indicates a problem of overall economic performance.

It is more important to investigate first why rates of return are so low, rather than head immediately toward the idea of debt forgiveness. I'm not convinced that debt reduction is such an important tool in development. ■

* The HIPC Initiative is a comprehensive approach to debt reduction for heavily indebted poor countries pursuing IMF- and World Bank-supported adjustment and reform programs.
