The Cartel of Good Intentions

The world’s richest governments have pledged to boost poor nations’ growth. But can they overcome the obstacles of bureaucracy out of touch with the forces of market?

By William Easterly

The mere mention of a “cartel” usually strikes fear in the hearts and wallets of consumers and regulators around the globe. Though the term normally evokes images of greedy oil producers or murderous drug lords, a new, more well-intentioned cartel has emerged on the global scene. Its members are the world’s leading foreign aid organizations, which constitute a near monopoly relative to the powerless poor.

This state of affairs helps explain why the global foreign aid bureaucracy has run amok in recent years. Consider the steps that beleaguered government officials in low-income countries must take to receive foreign aid. Among other things, they must prepare a Participatory Poverty Reduction Strategy Paper (PRSP)—a detailed plan for uplifting the destitute that the World Bank and International Monetary Fund (IMF) require before granting debt forgiveness and new loans. This document in turn must adhere to the World Bank’s Comprehensive Development Framework, a 14-point checklist covering everything from labor market policy to labor practices. And the list goes on: Policymakers seeking aid dollars must also prepare a Financial Information Management System report, a Report on Observance of Standards and Codes, a Medium Term Expenditure Framework, and a Debt Sustainability Analysis for the Enhanced Heavily Indebted Poor Countries Initiative. Each document can run to hundreds of pages and consume months of preparation time. For example, Niger’s recently completed PRSP is 187 pages long, took 15 months to prepare, and sets out spending for a 2002–05 poverty reduction plan with such detailed line items as $17,600 a year on “sensitizing population to traffic circulation.”

Meanwhile, the U.N. International Conference on Financing for Development held in Monterrey, Mexico, in March 2002 produced a document—the Monterrey Consensus—that has a welcome emphasis on partnership between rich donor and poor recipient nations. But it’s somewhat challenging for poor countries to carry out the 73 actions that the document recommends, including such ambitions as establishing democracy, equality between boys and girls, and peace on Earth.

Visitors to the World Bank Web site will find 31 major development topics listed there, each with multiple subtopics. For example, browsers can explore 13 subcategories under “Social Development,” including indigenous peoples, resettlement, and culture in sustainable development. This last item in turn includes the music industry in Africa, the preservation of cultural artifacts, a seven-point framework for action, and—and, well, you get the idea.

It’s not that aid bureaucrats are bad; in fact, many smart, hardworking, dedicated professionals toil away in the world’s top aid agencies. But the perverse incentives they face explain the organizations’ obtuse behavior. The international aid bureaucracy will never work properly under the conditions that make it operate like a cartel—the cartel of good intentions.

All Together Now

Cartels thrive when customers have little opportunity to complain or to find alternative suppliers. In its heyday during the 1970s, for example, the Organization of the Petroleum Exporting Countries (OPEC) could dictate severe terms to customers; it was only when more non–OPEC oil exporters emerged that the cartel’s power weakened. In the foreign aid business, customers (i.e., poor citizens in developing countries) have few chances to express their needs, yet they cannot exit the system. Meanwhile, rich nations paying the aid bills are clueless about what those customers want. Non-
The Aid Cartel’s Golden Oldies

Many of the “new” themes that the international aid agencies emphasize today have actually been around for several decades.

Donor Coordination

| (Foreign aid) should be a cooperative enterprise in which all nations work together through the United Nations and its specialized agencies. | (World Bank, 1945) |
| Aid coordination ... has been recognized as increasingly important. | (World Bank, 1981) |
| We should improve coherence through better coordination of efforts amongst international institutions and agencies, the donor community, the private sector, and civil society. | (World Bank President James Wolfensohn, 2002) |

Aid Selectivity

| Objective No. 1: To apply stricter standards of selectivity in aiding developing countries. | (President John F. Kennedy, 1963) |
| The relief of poverty depends both on aid and on the policies of the recipient countries. | (Gareyn Development Committee Task Force, 1985) |
| (The International Development Association) should increase its selectivity by directing more assistance to borrowers with sound policy environments. | (International Development Association, 2001) |

Focus on Poverty

| (The aid community must) place a greater emphasis on policies and projects which will begin to attack the problems of absolute poverty. | (World Bank President Robert McNamara, 1973) |
| The Deputies encouraged an even stronger emphasis on poverty reduction in [the International Development Association] programs. | (Former World Bank Managing Director Ernest Stern, 1990) |
| The Poverty Reduction Strategy Paper aims at increasing the focus of assistance on the overarching objective of poverty reduction. | (International Development Association, 2001) |

African Reforms

| Many African governments are more clearly aware of the need to take major steps to improve the efficiency of their economies. | (World Bank, 1983) |
| African countries have made great strides in improving policies and restoring growth. | (World Bank, 1994) |
| Africa’s leaders have recognized the need to improve their policies, spelled out in the New Partnership for African Development. | (World Bank, 2002) |

Sources: William Easterly, The Cartel of Good Intentions: Bureaucracy vs. Markets in Foreign Aid (Washington: Center for Global Development, 2002); James Wolfensohn, Note From the President of the World Bank (April 12, 2002)
By forming a united front and duplicating efforts, the foreign aid community is able to diffuse blame among its members when economic conditions in poor countries fail to improve.

THE $3,521 QUANDARY

Like any good monopoly, the cartel of good intentions seeks to maximize net revenues. Indeed, if any single objective has characterized the aid community since its inception, it is an obsession with increasing the total aid money mobilized. Traditionally, aid agencies justify this goal by identifying the aid “requirements” needed to achieve a target rate of economic growth, calculating the difference between existing aid and the require-ments, and then advocating a commensurate aid increase. In 1951, the U.N. Group of Experts calculated exactly how much aid poor countries needed to achieve an annual growth rate of 2 percent per capita, coming up with an amount that would equal $20 billion in today’s dollars. Similarly, the economist Walt Rostow calculated in 1960 the aid increase (roughly double the aid levels at the time) that would lift Asia, Africa, and Latin America into self-sustaining growth. (“Self-sustaining” meant that aid would no longer be necessary to 10 to 15 years after the increase.) Despite the looming expiration of the 15-year aid window, then World Bank President Robert McNamara called for a doubling of aid in 1973. The call for doubling was repeated at the World Bank in its 1990 “World Development Report.” Not to be outdone, current World Bank President James Wolfensohn is now advocating a doubling of aid.

The cartel’s efforts have succeeded: Total assistance flows to developing countries have doubled several times since the early days of large-scale foreign aid. (Meanwhile, the World Bank’s staff increased from 657 people in 1959–60 to some 10,000 today.) In fact, if all foreign aid given since 1950 had been invested in U.S. Treasury bills, the cumulative assets of poor countries by 2001 from foreign aid alone would have amounted to $2.3 trillion. This aid may have helped achieve such important accomplishments as lower infant mortality and rising literacy throughout the developing world. And high growth in aid-intensive coun-
tries like Botswana and Uganda is something to which aid agencies can (and do) point. The growth outcome in most aid recipients, however, has been extremely disappointing. For example, on average, aid-intensive African nations saw growth decline despite constant increases in aid as a percentage of their income [see figure on opposite page].

Aid agencies always claim that their main goal is to reduce the number of poor people and poverty defined as an annual income below $365. To this end, the World Bank’s 2002 aid accounting estimates that an extra $1 billion in overseas development assistance would lift more than 284,000 people out of poverty. (This claim has appeared prominently in the press and has been repeated in other government reports on aid effectiveness.) If these figures are correct, however, then the additional annual aid spending per person lifted out of poverty (whose annual income is less than $365) comes to $3,521. Of course, aid agencies don’t follow their own logic (often to their conclusion—common sense says that aid should help everyone and not just target those who can stagger across the minimum poverty threshold. Regrettably, this claim for aid’s effect on poverty has more to do with the aid bureaucracy’s desperate need for good publicity than with sound economics.

A FRAMEWORK FOR FAILURE

To the extent that anyone monitors the performance of global aid agencies, it is the politicians and the public in rich nations. Aid agencies therefore strive to produce outputs (projects, loans, etc.) that these audiences can easily observe, even if such outputs provide low economic returns for recipient nations. Conversely, aid bureaucrats don’t try as hard to produce less visible, high-return outputs. This emphasis on visibility results in shiny showcase projects, countless international meetings and summits, glossy reports for public consumption, and the proliferation of “frameworks” and strategy papers. Few are concerned about whether the showcase projects endure beyond the ribbon-cutting ceremony or if all those meetings, frame-
works, and strategies produce anything of value.

This quest for visibility explains why donors like to finance new, high-profile capital investment projects yet seem reluctant to spend operating funds with poverty with aid. Nonetheless, “self-sustaining” aid is frequently lie idle for lack of spare parts, repairs, gasoline, or other necessities. Schools lack operating funds for salaries and teaching materials, and agricultural research stations have difficulty keeping up field trials. Roads, public buildings, and processing facilities suffer from lack of maintenance.” Five years later, another study of Africa found that “road maintenance crews lack fuel and bitumen ... teachers lack books ... [and] health workers have no medicines to distribute.” In 1986, the World Bank declared that in Africa, “schools are now short of books, clinics lack medicines, and infrastructure maintenance is avoided.” Mean-
while, a recent study for a number of different poor countries estimated that the return on spending on educational instructional materials was up to 14 times higher than the return on spending on physical facilities.

And then there are the frameworks. In 1999, World Bank President James Wolfensohn unveiled his Comprehensive Development Framework, a checklist of 14 items, each with multiple subitems. The framework covers clean government, property rights, finance, social safety nets, education, health, water, ...
The product: From left to right, a crew of foresters plants trees in Costa Rica, a cholera-stricken child receives treatment in a refugee camp in the Democratic Republic of the Congo, and workers in Pakistan load international food aid near the Afghan border.

Pity the poor aid bureaucracy that must maintain support for foreign assistance while bad news is breaking out everywhere. Aid agencies have thus perfected the art of smoothing out unpleasant realities with diplomatic language. A war is deemed a “conflict-related reallocation of resources.” Countries run by homicidal warlords like those in Liberia or Somalia are “low-income countries under stress.” Nations where presidents loot the treasury experience “government issues.” The meaning of other aid community jargon, like “investment climate,” remains elusive. The investment climate will be stormy in the morning, gradually clearing in the afternoon with scattered expropriations.

Another typical spin-control technique is to answer any criticism by acknowledging that, “Indeed, we aid agencies used to make that mistake, but now we have corrected it.” This defense is hard to refute, since it is much more difficult to evaluate the present than the past. (One only doubts that the sinner has now found true religion from the knowledge of many previous conversions.) Recent conversions typically include improved coordination among donors, a special focus on poverty alleviation, and renewed economic reform efforts in African countries. And among the most popular concepts the aid community has recently discovered is “selectivity”—the principle that aid will only work in countries with good economic policies and efficient, squeaky-clean institutions. The moment of aid donors’ conversion typically coincides with the end of the Cold War, but in truth, selectivity (and other “new” ideas) has been a recurrent aid theme over the last 40 years [see sidebar on page 42].

Unfortunately, evidence of a true conversion on selectivity remains mixed. Take Kenya, where President Daniel arap Moi has mismanaged the economy since 1978. Moi has consistently failed to keep conditions on the 19 economic reform loans his government obtained from the World Bank and IMF. In September 2000, representatives of 189 countries met at the U.N. Millennium General Assembly in New York and adopted the Millennium Declaration concerning peace, security, and development issues. The Millennium Development Goals (MDGs), listed below, emerged from this gathering. Since then, virtually all the leading aid institutions have endorsed the MDGs, including the World Bank, International Monetary Fund, Organisation for Economic Co-operation and Development, and the Inter-American Development Bank.

Goal 1: Eradicate extreme poverty and hunger
Halve, between 1990 and 2015, the proportion of people whose income is less than $1 a day. Halve, between 1990 and 2015, the number of people who suffer from hunger.

Goal 2: Achieve universal primary education
Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling.

Goal 3: Promote gender equality and empower women
Eliminate gender disparity in primary and secondary education preferably by 2005 and in all levels of education no later than 2015.

Goal 4: Reduce child mortality
Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.

Goal 5: Improve maternal health
Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.

Goal 6: Combat HIV/AIDS, malaria, and other diseases
Have halted by 2015 and begun to reverse the spread of HIV/AIDS. Have halted by 2015 and begun to reverse the incidence of malaria and other major diseases.

Goal 7: Ensure environmental sustainability
Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources.

Goal 8: Develop a global partnership for development
Develop further an open, rule-based, predictable, non-discriminatory trading and financial system.... Address the special needs of the least developed countries.... Address the special needs of the small island developing states.... Deal comprehensively with the debt problems of developing countries.... In cooperation with developing countries, develop and implement strategies for decent and productive work for youth and immigrants.... In cooperation with pharmaceutical companies, provide access to affordable, essential drugs in developing countries. In cooperation with the private sector, make available the benefits of new technologies, especially information and communications.
**Dismantling the Cartel**

How can the cartel of good intentions be reformed so that foreign aid might actually reach and benefit the world’s poor? Clearly, a good dose of humility is in order, considering all the bright ideas that have failed in the past. Moreover, those of us in the aid industry should not be so arrogant to think we are the main determinants of whether low-income countries develop—poor nations must accomplish that mainly on their own.

Still, if aid is to have some positive effect, the aid community cannot remain stuck in the same old bureaucratic rut. Perhaps using market mechanisms for foreign aid is a better approach. While bureaucratic cartels supply too many goods for which there is little demand and too few goods for which there is much demand, markets are about matching supply and demand. Cartels are all about “coordinated,” whereas markets are about the decentralized matching of customers and suppliers.

One option is to break the link between aid money and the obligatory use of a particular agency’s bureaucracy. A market for aid agencies could part with their resources into a common pool devoted to helping countries with acceptably pro-development governments. Governments would compete for the “pro-development” seal of approval, but donors should compete, too. Recipient nations could take the funds and work with any agency they choose. This scenario would minimize duplication and foster competition among aid agencies.

Another market-oriented step would be for the common pool to issue vouchers to poor individuals or communities, who could exchange them for development services at any aid agency, NGO, or domestic government agency. These service providers would in turn redeem the vouchers for cash out of the common pool. Aid agencies would be forced to compete to attract aid vouchers (and thus money) for their budgets. The vouchers could also trade in a secondary market; how far their price is below par would reflect the inefficiency of this aid scheme and would require remedial action. Most important, vouchers would provide real market power to the impoverished customers to express their true needs and desires.

Intermediaries such as a new Washington-based company called Development Space could help assemble the vouchers into blocks and identify aid suppliers; the intermediaries could even compete with each other to attract funding and find projects that satisfy the customers, much as venture capital firms do. Development Space is a private Web-based company established last year by former World Bank staff members—kind of an eBay for foreign aid. Aid agencies could establish their own intermediation units to add to the competition. An information bank could facilitate transparency and communication, posting news on projects searching for funding, donors searching for projects, and the reputation of various intermediaries.

Bureaucratic cartels probably last longer than private cartels, but they need not last forever. President George W. Bush’s proposed Millennium Challenge Account (under which, to use Bush’s words, “countries that live by these three broad standards—ruling justly, investing in their people, and encouraging economic freedom—will receive more aid from America”) and the accompanying increase in U.S. aid dollars will challenge the IMF and World Bank’s near monop-oly over reform-related lending. Development Space may be the first of many market-oriented endeavors to compete with aid agencies, but private philanthropists such as Bill Gates and George Soros have entered the industry as well.

This article is based on a longer research paper by Easterly, “Want to Know More?”

Want to Know More?


**Foreign Policy** has a long history of covering economic development and foreign aid, including Samuel Huntington’s “Foreign Aid: For What and for Whom” (Winter 1970–71), appearing in FP’s inaugural issue. Also see “Development: The End of Trickle Down?” (Fall 1973) by James Grant, “The Third World: Public Debt, Private Profit” (Spring 1978) by Albert Finklow, et al., “Funding Foreign Aid” (Summer 1988) by David R. Obey and Carol Lancaster, and “The IMF: A Cure or a Curse?” (Summer 1998) by Devesh Kapur. More recent FP coverage includes Ricardo Hausmann’s “Prisoners of Geography” (January/February 2001), Dani Rodrik’s “Trading in Illusions” (March/April 2001), Stephen Fuller’s “Who’s Minding the Bank?” (September/October 2001), and William Easterly’s “Think Again: Debt Relief” (November/December 2001).


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