



Age of choice: How developing countries are managing the new aid landscape

A summary

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Key messages

- Since the early 2000s the share of non-ODA development assistance has significantly increased in the countries reviewed, albeit to different degrees.
- Non-DAC bilateral donors were the main drivers of the increase in non-traditional development assistance, with China the largest among them.
- International philanthropic assistance flows were found to be small at country level and have yet to change the aid landscape significantly.
- Countries' ability to attract and manage climate finance appeared to depend heavily on defining their own strategies for managing assistance.
- Developing country governments welcomed more options for financing development, which outweighs the costs associated with greater fragmentation. Their three most commonly stated priorities with respect to the terms and conditions of development assistance were ownership, alignment to national priorities (especially sectoral alignment) and speed of delivery.

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1 Introduction

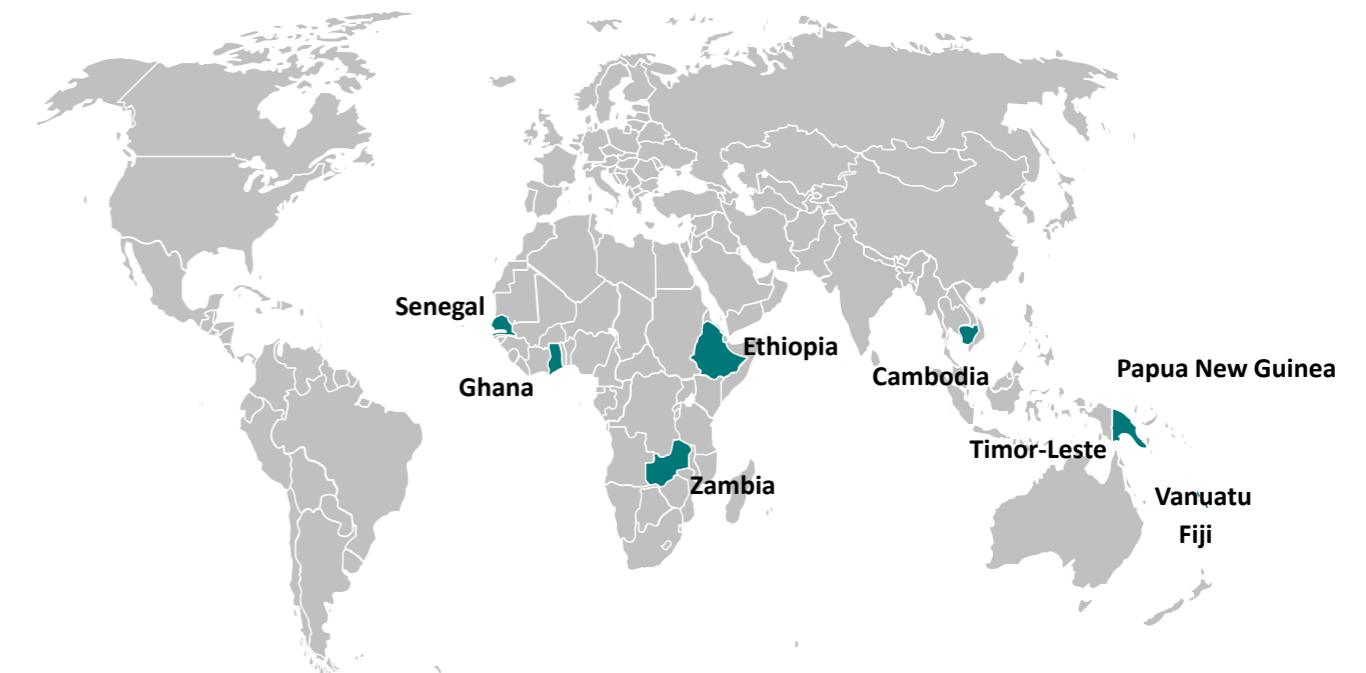
This summary outlines the main findings from nine case studies undertaken by ODI between 2012 and 2014 (Figure 1) exploring the implications of the changing global development assistance landscape for partner country governments. It provides policy recommendations for developing country governments, development partners and the international aid effectiveness community. The case studies covered four countries in sub-Saharan Africa (Ethiopia, Ghana, Senegal and Zambia), two in Asia (Cambodia and Timor-Leste) and three Pacific island states (Fiji, Papua New Guinea and Vanuatu).

The project sought to examine the challenges and opportunities experienced by governments in managing in the new landscape, particularly the growth of what we here call ‘non-traditional development assistance’ (NTDA) (see Box 1).

Each case study aimed to answer the following research questions:

1. What is the economic, political and aid management context that determines the ability of the government to mobilise and utilise development assistance and shapes the outcomes of negotiations between the government and providers?
2. How has the volume and composition of total development assistance and the breakdown between traditional and non-traditional sources changed since 2002?
3. What are the government’s priorities when it comes to the volume, purpose and terms and conditions of development assistance?
4. In which arenas does the government seek to engage with providers, and which strategies does it employ to negotiate with them? How do these arenas and strategies differ between different types of providers?
5. To what extent is the government achieving its objectives when it comes to negotiating with providers?

Figure 1: Case studies 2012-2014



The methodology for the case studies is adapted from Fraser and Whitfield (2008) and Ostrom et al. (2001). The key insight from Fraser and Whitfield is that the process of engagement between governments and donors or NTPs can be seen as one of negotiation, in contrast to much of the literature on the political economy of aid. Governments and providers are assumed to have possibly divergent sets of objectives that they seek to negotiate and reconcile. Fraser and Whitfield also focus heavily on the importance of context, both economic and political, in shaping country and donor negotiating capital and hence negotiation outcomes.

In this report we review the six African and Asian countries separately from the three Pacific island states, which are small island economies in a regional context dominated by a single donor (Australia), which clearly affects the rationale for aid coordination.

Box 1: Defining non-traditional development assistance

By non-traditional development assistance (NTDA) we mean cross-border sources of finance provided with some public or philanthropic purpose, which have some associated level of concessionality but also have funding or delivery mechanisms that differ from those of traditional donors and/or may not necessarily meet official development assistance (ODA) definitions.

We include within this category development assistance from donors outside the OECD Development Assistance Committee (DAC), philanthropic and institutional giving, social impact investment, global vertical funds, and climate finance. We also include other official flows (OOFs) in our upper range estimates because although many OOF providers are traditional donors (e.g. the International Bank for Reconstruction and Development), their assistance does not meet usual ODA concessionality thresholds.

The distinction between traditional and non-traditional is at best a useful approximation, inevitably involving a degree of subjective judgement. It does not seek to imply that traditional providers do not innovate or that non-traditional assistance is new. Total development assistance corresponds to NTDA plus the traditional component of ODA flows (traditional development assistance i.e. ODA excluding vertical health funds and ODA-eligible climate finance).

2 Summary of case studies: African and Asian countries

2.1 Economic and political background

With the exception of Senegal, all the countries reviewed experienced a period of high economic growth, averaging 5% over the past decade. In the case of resource-rich Ghana, Timor-Leste and Zambia it was fuelled by high commodity prices for oil or copper.

Four out of the six countries have good access to private capital flows, either via foreign direct investments (Ghana and Cambodia) or the capital market. Ghana, Senegal and Zambia have issued Eurobonds whose terms and conditions are very expensive (often close to a 10% annual interest rate) compared with the multilateral development banks' soft and hard loan windows. Sovereign debt levels are rising in Ghana and Senegal.

Strong growth and access to other external sources of finance have helped Ghana, Timor-Leste and Zambia drastically reduce dependency on aid for their economies, while Cambodia, Ethiopia and Senegal still remain reliant on aid.

For donors, Ethiopia is geostrategically important in East Africa as are Ghana and Senegal in West Africa. The two Asian countries in the group, Timor-Leste and Cambodia, are both classified as fragile countries as they have recently experienced a period of conflict and instability (until 2002 in Timor-Leste and until the early 1990s in Cambodia). The history of Cambodia still influences its policy today, leading to a preference for stability over other political goals.

2.2 Non-traditional development assistance is on the rise

Since the early 2000s the share of development assistance accounted for by non-traditional sources has increased in all six countries. In Cambodia in 2009, NTDA was estimated at \$191.5 million, or 23.5% of the value of total development assistance. This was an increase from only \$34.1 million (or 10.7% of total development assistance) in 2002. In Ghana, NTDA was already important in the early 2000s (20% of total development assistance) and it accounted on average for 36% of development assistance in the late 2000s. In contrast, in the case of Zambia non-traditional assistance accounted for around 2% of total development assistance in the early 2000s, growing

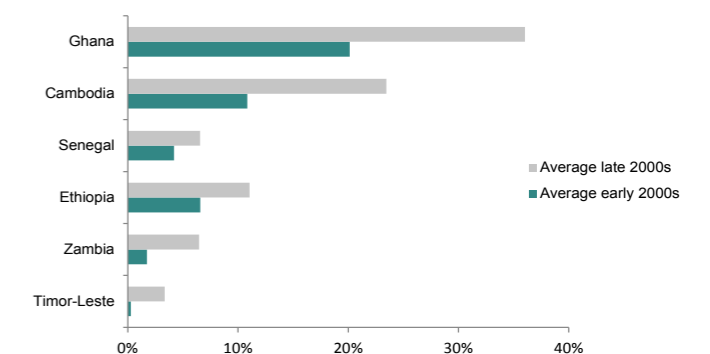
to around 6% between 2008 and 2010. NTDA accounted for 9.1% of total assistance in Ethiopia in 2009. Figure 2 illustrates the case for the six sub-Saharan African and Asian countries reviewed in this section.

2.2.1 In most countries sovereign non-DAC donors were the main non-traditional providers

The main drivers of the increase in NTDA are non-DAC bilateral donors, with China the largest among them. Between 2008 and 2010 China accounted for more than 90% of bilateral NTDA in Cambodia (\$210 million in total over that period), Ghana (\$12.6 billion), Timor-Leste (\$14.9 million) and Zambia (\$116 million), including both ODA and OOF equivalent flows. In comparison, in the 2000-2002 period Chinese assistance was \$51.7 million in Cambodia and \$270 million in Ghana, while no Chinese assistance was reported for either Zambia or Timor-Leste (which had just become independent but was not yet sovereign).

The second most important non-DAC donor is India, which is present in all the countries analysed except Timor-Leste. Its financial assistance to Ethiopia was \$161 million over the period 2008-2010 (Chinese assistance was \$14 million), making it the largest non-DAC donor in the country. The Islamic Development Bank and Saudi Arabia

Figure 2: Share of non-traditional development finance flows in total development assistance, African and Asian countries



Source: Case study reports and authors' calculation based on World Bank World Development Indicators, OECD Stats, AidData, The Foundation Centre, and Climate Funds Update. Different years apply.

are important donors in Ethiopia and Senegal, providing \$204 million to Ethiopia and \$264 million to Senegal over the 2000-2010 period. Brazil and South Africa have small development cooperation programmes providing mainly technical assistance. Brazil is present in Ghana, Timor-Leste and Zambia, while South Africa works in Zambia.

2.2.2 Vertical health funds are the second most important source of non-traditional assistance

Assistance from GAVI (the Vaccine Alliance) and the Global Fund to Fight AIDS, Tuberculosis and Malaria, both established in the early 2000s, grew sharply towards the end of the decade to become the second most important source of NTDA in most countries. Over the 2008-2010 period, the vertical health funds became the primary source of NTDA in Ethiopia and Zambia.

2.2.3 Climate finance and philanthropic assistance are less important

A country's ability to attract and manage climate finance appears to depend heavily on its own strategies for managing assistance. Ethiopia has developed and implemented a fully-fledged climate change strategy and has managed to attract more climate finance and at a better disbursement rate than the other countries.

International philanthropic assistance flows were found to be small at country level and have yet to change the aid landscape significantly. Philanthropic assistance accounted for less than 1% of total assistance over 2008-2010 and less than 5% of NTDA flows.

2.3 Key priorities of governments are often based on Paris Declaration principles

Developing country government officials welcomed more options for financing development, which for them outweighs the costs associated with greater fragmentation. Their three most common priorities with respect to the terms and conditions of development assistance are ownership, alignment with national priorities, especially sectoral alignment, and speed of delivery. Ownership and alignment are pillars of the Paris Declaration Principles on Aid Effectiveness.

Ownership and speed were especially emphasised in Cambodia and Ethiopia. General budget support is the preferred modality for assistance because of low transaction costs and alignment with national priorities.

Non-DAC donors scored well against all these priorities. Measured against ownership, non-DACs were found to be popular with governments because of their overall policy of non-interference in government policy and their limited

conditionality. In terms of alignment with national priorities, non-DAC donors were generally found to perform better as they focus on infrastructure, energy and growth-promoting sectors, which have historically been a lower priority for traditional donors but a high priority for governments. The Global Fund and philanthropic assistance, on the other hand, were both found to be not well aligned with government priorities in Cambodia and Zambia.

Ghana and Senegal have had two successful rounds of sovereign Eurobond issues and Senegal issued bonds on regional markets in 2013. In the case of Ghana, despite the substantial premium paid on Eurobonds (nearly 9% coupon on US dollar funds at the time of issuance) compared with cheaper options from official lenders, government respondents still favoured the bond route on the grounds of its higher volume, greater flexibility (e.g. in refinancing previous bonds) and the absence of conditionality. Some also emphasised the signalling effect inherent in this window, notably the need to tap markets periodically to show the country retains their confidence.

2.4 Lack of strategies for different sources of assistance

At the time of the study, only Cambodia and Ethiopia had a strategic approach in managing different sources and providers of development assistance. Both countries used the existence of non-traditional providers to increase their negotiating capital in relation to traditional donors, and there was some evidence to suggest they were able to secure better outcomes in relation to their priorities. Other countries still lacked an overall development finance framework, either implicit or explicit, that links national investment priorities to the perceived comparative advantage of different external sources in terms of financial cost, speed of delivery and conditionality.

2.5 Governments prefer bilateral aid negotiations

Although coordination rounds between government and donors are present in all countries, at least at the sector level, most governments preferred bilateral negotiation processes. Non-traditional donors were often invited to participate in donor coordination rounds – especially in high-profile diplomatic fora, less so in Sector Working Groups – but they did not always do so actively. In Zambia, though, their participation has improved as DAC and non-DAC donors have become more willing to learn from each other and to share information.

3 Summary of case studies: Pacific countries

3.1 Difficult economic and political conditions

Papua New Guinea (PNG) experienced a period of strong growth averaging 6.4% between 2004-2014, while Fiji and Vanuatu grew more slowly at a rate of around 2%. PNG's growth was fuelled by the mining and petroleum sector (natural resource rents are equivalent to 36% of PNG's gross domestic product). Its resource wealth enables it to attract foreign direct investment (FDI), while the tourism sector performs the same role in Fiji. FDI inflows to Vanuatu, however, are stagnant, and aid accounts for over 13% of its gross national income, compared with 5% in PNG and 2% in Fiji. For all three countries, Australia has historically been the main economic and development partner.

All three countries share a history of political instability. In September 2014 Fiji held its first elections since the military coup in 2006 that interrupted its relations with traditional donors. PNG and Vanuatu are marked by frequent government changes. The situation in PNG has stabilised in the past years, but Vanuatu's parliament is still frequently dismissed and re-elected.

3.2 Non-traditional development assistance has increased

Over the past ten years, the amount of NTDA has increased in these countries (Figure 3). While it was virtually non-existent in all three countries in the early 2000s, total NTDA between 2008 and 2010 rose to \$103 million in PNG, \$62 million in Fiji and \$52 million in Vanuatu.

3.2.1 China is the dominant non-DAC donor

In Fiji and Vanuatu, the main source of NTDA was non-DAC donors, especially China (Chinese Ex-Im Bank). China accounted for \$49 million in Fiji and \$40 million in Vanuatu (79% and 77% of NTDA flows respectively) over the 2008-2010 period.

Fiji and PNG also somewhat surprisingly received assistance from Taiwan (\$2.1 million and \$1.8 million over 2008-2010).

3.2.2 Health funds are important in Papua New Guinea

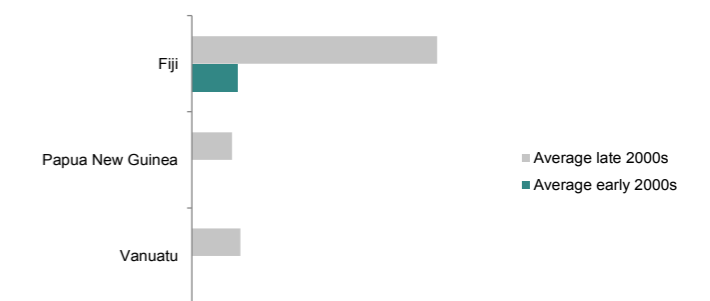
Assistance through vertical health funds has increased in PNG since the mid-2000s, from \$2 million in 2004 to \$34.7 million in 2009 (in 2010 only \$10.4 million was reported). In the 2008-2010 period they accounted on average for 55% of non-traditional assistance.

Health fund flows appeared much lower in Fiji and Vanuatu. In the case of Vanuatu this is explained by limited information on health fund allocation because the country receives funds from the Global Fund via a regional mechanism. In Fiji the amount received via the Global Fund is smaller as the country is not malaria-prone and so does not receive money for this health issue.

3.2.3 Limited role of international philanthropic assistance

International philanthropic assistance was limited and did not operate through country systems. In PNG, the PNG Sustainable Development Programme (PNG SDP) was a privately owned offshore fund financed through oil rents and was considered the second largest development agency in the country after Australia. This unique programme in the development finance landscape disbursed an average of \$43 million annually from 2002 to 2012 (or 7% of

Figure 3: Share of non-traditional development finance flows in total development assistance, Pacific island countries



Source: Case study reports and authors' calculation based on World Bank World Development Indicators, OECD Stats, AidData, The Foundation Centre, and Climate Funds Update. Different years apply.

ODA flows), and was a good example of large-scale philanthropic assistance. However, the mine is now state owned and the PNG SDP ended in 2013.

In Fiji and Vanuatu, assistance from US-based organisations was reported as quite small: \$2.5 million and \$0.8 million respectively over 2008-2010.

3.2.4 Climate finance is limited

Climate finance was relatively small in all three countries. Vanuatu received the highest amount of climate finance in the group in the 2008-2010 period with \$11.3 million (compared with total traditional assistance of \$292 million over the same period – see OECD DAC statistics). While approvals for new climate finance have since increased – especially in Vanuatu – a gap between approvals and disbursements existed. This is partly due to capacity constraints at the country level.

3.3 Governments have a preference for capacity-building, ownership and speed of delivery

For all three governments, capacity-building, ownership and speed of delivery were found priorities for development assistance. While the governments have been successful in securing capacity-building components, they

struggle in achieving the other two goals with respect to traditional donors.

China, however, scored well against priorities such as ownership and speed of delivery. These governments appreciated the flexibility and fast disbursement of Chinese assistance but, at least in the case of Fiji and Vanuatu, also criticised Chinese assistance for having few spillover effects for the local economy and lacking transparency in the negotiation process.

3.4 Formal aid coordination is limited

Aid coordination is affected by the political and geographic characteristics of the countries. In Fiji, the political situation after the 2006 coup shifted traditional donors' aid away from government systems, and formal aid coordination mechanisms did not exist. In PNG, the dominance of Australia as the main donor, with strong bilateral ties, has made aid coordination with other partners less relevant. Sector Working Groups exist in Vanuatu, but as in Fiji and PNG, it was found that the government preferred direct bilateral coordination with donors.

4 Recommendations

Even though findings were different across the case studies, a series of common themes and recommendations emerge from the evidence gathered.

- For developing country governments:
 - * Take an active approach to negotiating with all kinds of assistance providers and be strategic in how relationships with providers are managed. Recognising the distinctive characteristics of providers will help to secure negotiating success.
 - * Recognise that a country's economic, governance and aid management contexts play a role in determining its negotiating capital when dealing with both traditional and non-traditional providers. Factors such as geostrategic importance are largely outside of government control, but others, such as macroeconomic management, are not.
- For traditional donors:
 - * Recognise that in the 'age of choice' developing countries are likely to have more options when it comes to sources of development assistance. Ensuring that assistance supports country ownership and is well aligned with national priorities will be critical in ensuring traditional assistance is still in demand. Donors may also need to be clearer about their own niche in relation to competition from other kinds of providers.
 - * Direct donor conditionality is less likely to be effective in an age of choice. While recognising that traditional donors may have legitimate
- For non-traditional providers of development finance:
 - * Increase transparency of funding to improve data availability for policy planning.
 - * Better align assistance from vertical funds to national strategies and existing coordination mechanisms.
- For the international aid effectiveness community:
 - * Recognise that country priorities on aid effectiveness may not be fully in line with those currently articulated in the Paris Declaration on Aid Effectiveness. Speed is an important element missing from the Paris Declaration, while concerns on harmonisation and fragmentation appear to be overstated.
 - * Ensure that future aid effectiveness agreements better reflect country-level priorities. In particular, some countries may wish to negotiate with different groups of providers separately.
 - * Recognise that different providers have distinctive models of providing development assistance, which can each bring particular benefits and insights. A process of mutual learning between these approaches may be more constructive than attempts to agree a 'one-size-fits-all' approach to aid effectiveness.

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