



Aid, exports and employment in the UK

Max Mendez-Parra and Dirk Willem te Velde

Key messages

- In addition to its primary poverty-reducing objective, UK aid has direct benefits for firms and workers in the UK.
- New analysis has calculated that every \$1 of direct bilateral aid leads to a \$0.22 increase in UK exports.
- In 2014, \$5.9 billion in UK direct bilateral aid increased UK exports by almost \$1.3 billion. This amount of exports creates 12,000 UK jobs.

In 2014, the UK gave \$5.9 billion in direct bilateral development assistance.¹ This contribution makes the UK one of the largest individual aid donors in the world. UK efforts help developing countries improve education, combat diseases and become more productive and competitive internationally. This paper explores and quantifies the direct benefit of UK aid in relation to jobs in the UK.

Calculating the effects of aid on the donor country

Aid affects the economy of the donor country primarily through the channel of exports. First, aid generates an income effect in the recipient country that leads to an increase in its demand for goods and services from other countries, including donor countries. Second, some aid interventions lead to lower trade costs, which make imports in the recipient country more competitive. These effects benefit all exporters, regardless of whether they have provided aid or not. However, the effects are expected to vary depending on the underlying factors affecting trade, such as tariffs and the distance between donor and recipient.

There are other factors that, without implying any sort of tying of aid, will increase exports from the specific donor. For example, there may be some ‘goodwill’ towards donor exporters in the recipient country (Arvin and Choudry, 1997). Aid may also have similar effects to export-promoting activities, such as through a presence in the recipient country of an embassy or consulate and the celebration of trade missions (Moons and van Bergeijk, 2011).

Estimating the aid-generated exports in the UK

Using standard econometric techniques, we estimated the effect of direct bilateral aid provided by the UK on exports from the UK (Mendez-Parra and te Velde, 2017). We excluded aid provided through other institutions, as a direct link between the UK and the recipient cannot be identified. The analysis controlled for the influence of other factors that may affect the trade between the UK and each of the recipients. These factors include recipients’ gross domestic product (the higher the GDP, the greater the imports); tariffs applied by the recipient countries; and the existence of free trade agreements between the UK (through the EU) and the recipient country; as well as other factors affecting bilateral trade relationships. It also considered the effects of other countries’ aid to ensure we could identify more precisely the effect of aid from the UK.

The analysis found that, for every \$1 of direct bilateral aid,² the UK exported an additional \$0.22 worth in goods to recipient countries. Using official Organisation for Economic Co-operation and Development figures for UK direct bilateral aid for 2014 – the latest year for which data

was available at the time of the estimation – this amounted to almost \$1.3 billion of additional exports of goods.

Due to these additional exports, output in the UK expanded. This expansion in output affected not only the sectors in which the products exported were generated but also other sectors of the UK economy, including services. All these sectors provided inputs in the form of other goods and services used in production. In addition, these input-producing sectors will require additional intermediate goods and services. For example, business services are used in the production of exported transport equipment.

Working out all these relationships using an input-output matrix allows us to calculate the output effect of aid-generated exports in each of the sectors of the UK economy.

What does this mean for employment?

More importantly, the analysis calculated the effect in terms of the amount of the increased labour demand by producing firms. The input-output model allows us to find out how much labour is required to produce one unit of value of output in the UK. In fact, this also identifies the size of the demand divided into low-, middle- and high-skilled workers.

According to the calculation of the input-output relationship, exports created by means of UK direct bilateral aid generated almost 12,000 jobs in the UK in 2014. This includes both employees and any other person involved in the production process in a non-employee role. Almost half of the employment (48%) was among middle-skilled workers, and 24% among low-skilled workers. Figure 1 shows the disaggregation of the labour effects by sector.

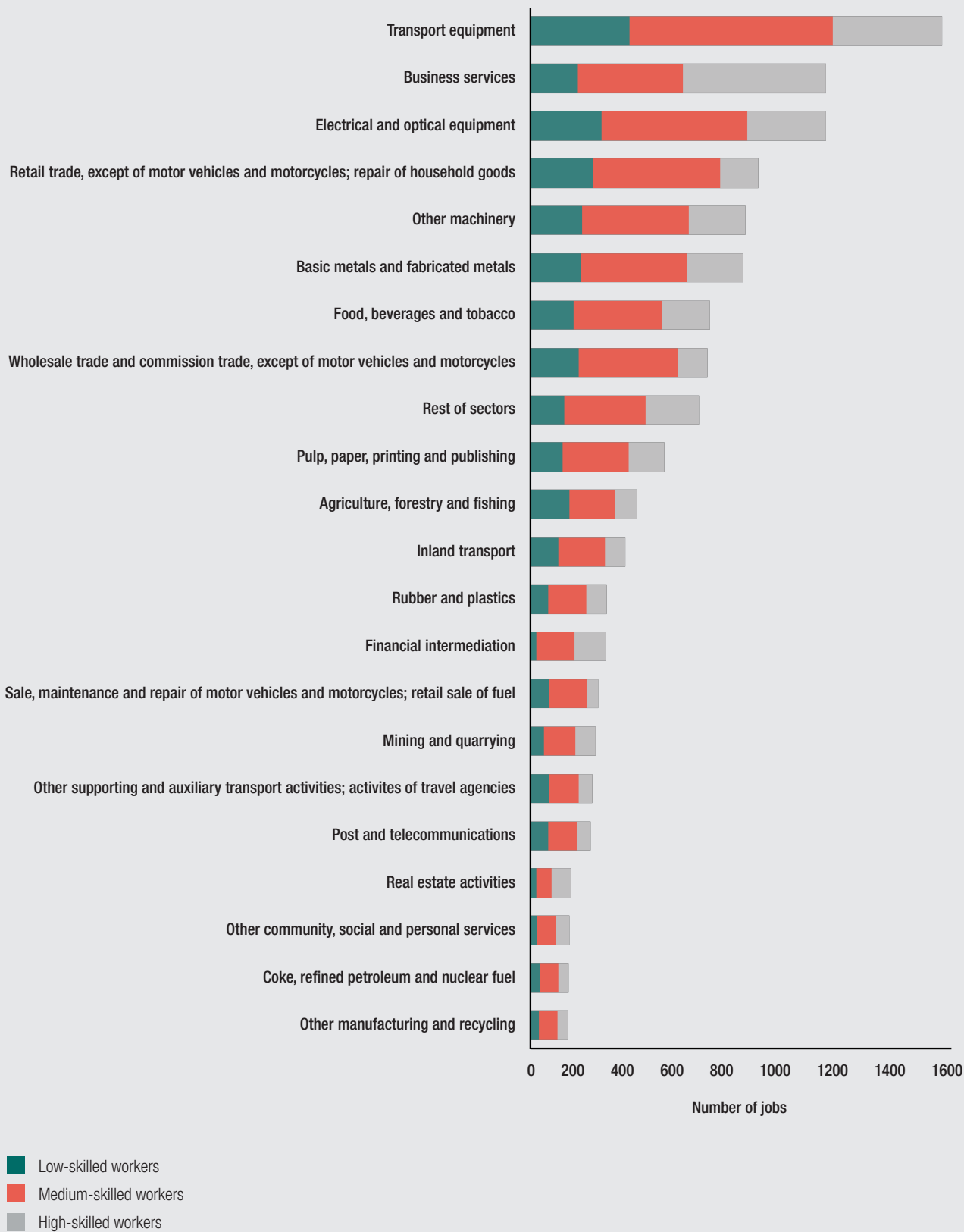
The calculation does not include aid provided by the UK through multilateral organisations. A more accurate calculation could at least double the estimated number of jobs and exports. Therefore, this result must be considered a lower estimation of the effects of UK aid on the UK economy.

Conclusion

The analysis suggests that there are direct benefits to the UK from the direct bilateral aid it provides, in terms of UK jobs creation. That is, UK aid increases exports and employment in the UK itself by increasing income, productivity and reducing trade costs in the recipient countries. This is due to an increase in the demand from developing countries for imports, in particular those coming from their donors. However, this does not imply any form of ‘tied aid’ by donors.

Despite the benefits that aid brings to the UK economy, the provision of aid to developing countries should continue to be motivated by its moral imperative. UK aid must remain untied. It should be focused on poverty reduction, economic transformation, and other actions that promote economic and social development.

Figure 1: UK jobs generated by direct bilateral aid, by sector



Source: Mendez-Parra and te Velde (2017).

Notes

- 1 OECD Development Finance Data 2014 was the latest data available when the estimations were made.
- 2 Approximately equal to Country Programmable Aid. Differences arise as a result of exchange rate valuations and differences in the computation of individual aid flows.

References

- Arvin, M. and Choudry, S. (1997) 'Untied aid and exports: Do untied disbursements create goodwill for donor exports?' *Canadian Journal of Development Studies* 18(1): 9–22.
- Moons, S. and van Bergeijk, P.A. (2011) 'Does economic diplomacy work? A meta analysis on the effect of economic diplomacy on international economic flows'. *The World Economy* 40(2): 336–368.
- Mendez-Parra, M. and te Velde, D.W. (2017) *The effects of aid on EU employment and trade: an econometric investigation*. Working Paper. London: ODI.
- OECD (2014) Development Finance Data.



Overseas Development Institute
203 Blackfriars Road
London SE1 8NJ
Tel +44 (0)20 7922 0300
Fax +44 (0)20 7922 0399
www.odi.org
info@odi.org

ODI is the UK's leading independent think tank on international development and humanitarian issues. Readers are encouraged to reproduce material for their own publications, as long as they are not being sold commercially. As copyright holder, ODI requests due acknowledgement and a copy of the publication. For online use, we ask readers to link to the original resource on the ODI website. The views presented in this paper are those of the author(s) and do not necessarily represent the views of ODI or our partners.

© Overseas Development Institute 2017. This work is licensed under a Creative Commons Attribution-NonCommercial Licence (CC BY-NC 4.0).