

Reinventing Foreign Aid

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foreword by Nancy Birdsall

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1 Introduction: Can't Take It Anymore?

William Easterly

Foreign aid is in the headlines more than ever before in its sixty-year history, and it has big ambitions. Such diverse scholars as George Clooney, Penelope Cruz, Alicia Keyes, Jay-Z, Will Smith, Stevie Wonder, Elton John, Paul McCartney, Salma Hayek, Brad Pitt, Mariah Carey, Bono, and Angelina Jolie have appeared in public events or in the media calling for an increase in foreign aid to poor countries. The objective of “the biggest ever antipoverty movement” was to “Make Poverty History.”

Strong claims are made about the potential of aid in many current aid agency documents. The UNDP makes a general statement: “International aid is one of the most effective weapons in the war against poverty.” However, at the same time, discontent with the existing aid system is also remarkably universal, including some of the same authors who make strong claims for aid. For example, the very next sentence in the UNDP report just cited seems to contradict the previous statement that the aid weapon is effective: “Today, that weapon is underused, inefficiently targeted and in need of repair.”¹ (UNDP 2005, p. 2).

Similarly the UN Millennium Project also makes the link from expert plans to foreign aid: “Poverty in the poorest countries can be dramatically reduced only if developing countries put well designed and well implemented plans in place to reduce poverty—and only if rich countries match their efforts with substantial increases in support.”² However, much later in the same report, we learn that “many national strategies will require significant international support. But the international system is ill equipped to provide it because of a shortage of supportive rules, effective institutional arrangements, and above all resolve to translate commitments to action.”³ To show how universal this bipolarity is, the Department for International Development (DFID) states, “Aid works. Aid helps reduce poverty by increasing economic growth, improving governance and increasing access to public services.” But again, toward the end of the same report, we have the seemingly contradictory statement: “But

some parts of the international system have become either too complicated and inefficient or simply do not work at all. They must change.”⁴

This bipolarity of “aid does work already and will work in the future, but aid is also not working” sometimes leads to remarkably penitential statements by the aid agencies themselves. For example, the international financial institutions—the World Bank and International Monetary Fund (IMF)—issued a report in 2006 in which a sentence in the opening paragraph of the executive summary states: “International financial institutions still emphasize loans and reports rather than development outcomes.”⁵

The mixture of grandiose expectations for future aid with frustration about existing aid captures well the current, muddled climate of opinion about what foreign aid is doing, will do, can do, or should do. Although many aspects of foreign aid are hotly debated, one view that seems to command almost universal assent from observers of the aid system (including from the aid agencies themselves about their own operations) is that the current aid system is not working very well.

Despite this dissatisfaction with the current system, all of the main political actors in the rich countries seem to agree on increasing the volume of aid. (They also talk about ways to improve the aid system, but progress on that appears inherently more problematic than increasing aid spending.) The World Bank and IMF in their *Global Monitoring Report 2006* say, “Donors are delivering more assistance, and the prospects for scaling up aid have brightened. At their summit in Gleneagles, the Group of Eight (G-8) leaders pledged to increase aid to Africa by \$25 billion a year by 2010—more than doubling assistance to the region—and Development Assistance Committee (DAC) members have agreed to expand aid to all developing countries by about \$50 billion.”⁶

After stagnating in the 1990s, total foreign aid has indeed increased sharply in the new millennium (figure 1.1).⁷ Hence, it is more important than ever before to think about how aid can effectively help the poorest people in the world.

In section 1.1, I sketch some of the larger issues in the foreign aid debate, which many of the authors of the chapters in this book are grappling with (although not necessarily in agreement with my take on the debate). Just as these chapters span the range from academic journal style to nontechnical opinion pieces, this introduction is not intended so much to be a scholarly contribution as it is to provoke debate and highlight the opposing points of view. Section 1.1 is frankly polemical, a style that I chose to reflect the dissatisfaction that I and others feel with a dysfunctional business that is supposed to be benefiting the most desperate people in the world (although not all of us are in agreement on diagnoses or cures). I then give a summary of the rest of the chapters in section 1.2.

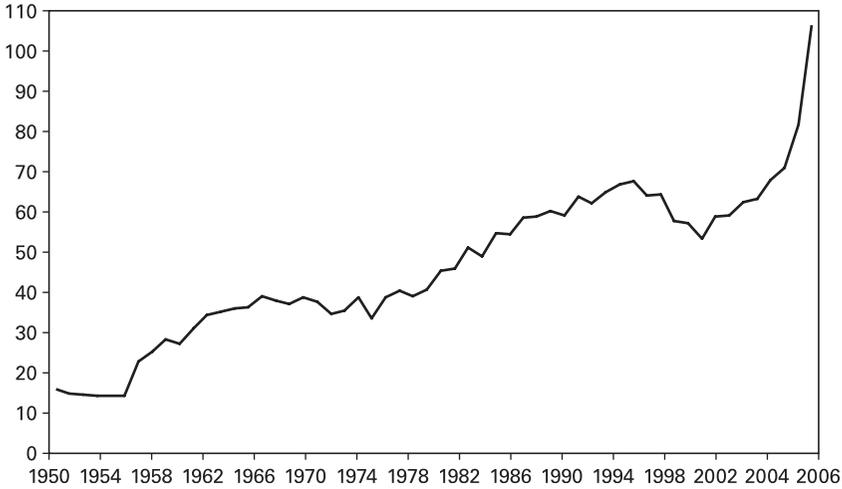


Figure 1.1
Total foreign aid from OECD countries in 2005 US\$ billion, 1950–2005

1.1 Comprehensive Planning versus Piecemeal Searching in Foreign Aid

The nature of man is intricate; the objects of society are of the greatest complexity; and therefore no simple disposition or direction of power can be suitable either to man’s nature or to the quality of his affairs.

—Edmund Burke (1790)

All of the major aid agencies are now engaged in an exercise to achieve what are known as the Millennium Development Goals (MDGs) by the year 2015. As the United Nations Development Program explains, “Five years ago, at the start of the new millennium, the world’s governments united to make a remarkable promise to the victims of global poverty. Meeting at the United Nations, they signed the Millennium declaration—a solemn pledge ‘to free our fellow men, women and children from the abject and dehumanizing conditions of extreme poverty.’”⁸

Jeffrey Sachs presents the aim of his recommendations as to “help foster economic systems that spread the benefits of science, technology to all parts of the world; Help foster international cooperation to secure a perpetual peace; Help promote science and technology, grounded in human rationality, to fuel the continued prospect of improving the human condition. This agenda is broad and bold, as it has been for two centuries, but many of its sweetest fruits are just within our reach.”⁹

U.K. Secretary of State for International Development Hilary Benn in a DFID white paper in 2006 agreed that “today . . .—for the first time—[the human family] has the capacity to make sure that every one of its members is lifted out of poverty. What people want and need is enough food to eat and water to drink. A roof over their heads, a job, a school for their children, and medicine and care when they are sick. The chance to live in peace, without fear of violence or war. And the opportunity to realise the potential in each and every one of us. . . . It is up to us to accept that responsibility and do what needs to be done.”¹⁰

These statements could be just inspirational rhetoric, and these campaigns do talk about specific, feasible tasks. However, an important part of the field of economic development has always been influenced by utopian ideals, which in turn seem to influence the approach to foreign aid (as they do for the UNDP, DFID, and Sachs). “Economic development” is sometimes presented as something like a teleological philosophy of history, in which all countries are destined to attain the goal of development, meaning industrialization and a high mass standard of living, not to mention peace and democracy. In this view, economic development is something like the other teleological philosophies of history, like Hegelianism and Marxism. The teleological worldview goes all the way back at least to Aristotle, who talked about a Final Cause that was more fundamental than the proximate causes of events. The Final Cause was the goal or destiny toward which the object was progressing. In this worldview, the future causes the present, so the destiny of development causes all countries (if not already developed) to be developing. Unfortunately, like all other teleological theories, the claims of this approach to economic development are non-testable and nonfalsifiable. (You can test hypotheses about the past but not about the future.)

A curious paradox of the teleological philosophies of history is that they give great importance to vigorous action by a small chosen group of actors to achieve what is predestined to happen anyway. Hegel talked about “world-historical individuals,” Marxists talked about the revolutionary vanguard of the working class, and economic development has a prominent role for development experts, who come with a plan of government actions to promote development. The Make Poverty History campaign urges its members to “take action now to pressure politicians and decision makers to help make poverty history.”¹¹

Discussions of world poverty often begin with a question something like, “What must we do”? Lenin may have helped launch this twentieth-century fad with his 1902 pamphlet, “What Is to Be Done?” in which he looked for the intelligentsia to find the answers for the masses. He reprints an 1874 quote

from Engels: “It is the specified duty of the leaders to gain an ever-clearer understanding of the theoretical problems, to free themselves more and more from the influence of traditional phrases inherited from the old conception of the world. The task of the leaders will be to bring understanding, thus acquired and clarified to the working masses, to spread it with increased enthusiasm.”¹²

Sachs says, “I have gradually come to understand through my scientific research and on the ground advisory work the awesome power in our generation’s hands to end the massive suffering of the extreme poor.” Sachs boldly states that “success in ending the poverty trap will be much easier than it appears.”¹³

DFID puts it a little less eloquently: “There needs to be rapid progress on the commitments made by developing countries and the international community to provide peace and security, encourage economic growth, and invest in the most important public services.”¹⁴

Like the teleological view of development, the impact of development experts is presented in a way that makes it nonfalsifiable: if a past group of experts did not achieve development, they were bad experts, whereas now we have good experts. Or there has been progress in knowledge or technology such that the latest generation of experts can now for the first time eliminate poverty: “The practical solutions exist. . . . And for the first time, the cost is utterly affordable.”¹⁵ As Hilary Benn said in the DFID report quoted above, world poverty can now be ended “for the first time.” This claim of a brand new opportunity to reduce poverty at an “utterly affordable” cost is important, because otherwise one wonders why previous development experts did not already achieve the easy solutions promised by the current experts to world poverty and its attendant miseries.

The expert plans are to be financed by foreign aid. Thus, the UNDP places aid at the center of achieving the promise of attaining the MDGs: “If donor countries are serious about tackling global poverty, reducing inequality and securing a safer and more prosperous future for their own citizens, they need to set their sights firmly on the target of delivering 0.5% of their national income in aid by 2010 and 0.7% by 2015.”¹⁶

DFID concurs that to finance peace, economic growth, and public services, “Additional resources will be essential for this. We must, therefore, ensure that the international community delivers the US\$50 billion increase in aid promised by 2010.”¹⁷

1.1.1 Two Alternative Philosophies of Foreign Aid

The response of this introduction to the statements I have quoted is frankly polemical, a word that is often given a negative connotation. This introduction

argues that polemics is useful in aid debates, because too often the aid policy-making community tolerates approaches that go against common sense and basic economics.

For example, the utopian expectations of what foreign aid should do often create an unfortunate approach to aid. Seventeen years after the fall of the Berlin Wall, there is only one major area of the world in which something that sounds a lot like central planning is still seen as a way to achieve prosperity: countries that receive foreign aid. Behind the aid wall that divides poor countries from rich, the aid community is awash in plans, strategies, and frameworks to meet the very real needs of the world's poor. These exercises make sense only in a central planning mentality in which the answer to the tragedies of poverty is a large bureaucratic apparatus to dictate quantities of different development goods and services by administrative fiat.¹⁸ The planning mind-set is in turn linked to previously discredited theories, such as that poverty is due to a "poverty trap," which can be alleviated only by a large inflow of aid from rich country to poor country governments to fill a "financing gap" for poor countries (I examine this idea yet again below). The aid inflow is, of course, administered by this same planning apparatus.

This is bad news for the world's poor, as historically poverty has not been ended by central planners. It is ended by "searchers," both economic and political, who explore solutions by trial and error, have a way to get feedback on the ones that work, and then expand the ones that work, all of this in an unplanned, spontaneous way. Examples of searchers are firms in private markets and democratically accountable politicians.

What are some of the characteristics of planners and searchers? In foreign aid, the planners set out a predetermined big goal, like ending world poverty, to be solved. They also determine a big plan to reach the big goal and throw an endless supply of resources and a large administrative apparatus at that big goal.

The searcher is more humble about how little she knows about other people's problems. Searchers do not set predetermined problems and do not have big plans; they are just on the lookout for favorable opportunities to solve problems—any problem no matter how big or small, whose solution will benefit themselves or others. Searchers must learn enough about each little problem to solve it, which means they must get feedback from the people affected by the problem and what they need to fix it.

A planner thinks he already knows the answers; he thinks of poverty as a technical engineering problem that his answers will solve. As the UN Millennium Project put it in 2005, "Throughout, we stress that the specific technologies for achieving the [Millennium Development] Goals are known. What is needed is to apply them at scale."¹⁹

A searcher admits she does not know the answers in advance; she believes that poverty is a complicated tangle of political, social, historical, institutional, and technological factors. A searcher only hopes to find answers to individual problems of the world's poor by trial-and-error experimentation.

Planners conceive the key to progress on poverty as a grand international effort at collective action. Sachs says in the opening pages of *The End of Poverty*: “Although introductory economics textbooks preach individualism and decentralized markets, our safety and prosperity depend at least as much on collective decisions to fight disease, promote good science and widespread education, provide critical infrastructure, and act in unison to help the poorest of the poor. . . . Collective action, through effective government provision of health, education, infrastructure, as well as foreign assistance when needed, underpins economic success.”²⁰ He says that each poor country should have five plans, such as an “Investment Plan, which shows the size, timing, and costs of the required investments” and a “Financial Plan to fund the Investment Plan, including the calculation of the Millennium Development Goals Financing Gap, the portion of financial needs the donors will have to fill.”²¹

U.N. secretary-general from Kofi Annan, uses the collective action *we*: “We will have time to reach the Millennium Development Goals—worldwide and in most, or even all, individual countries—but only if we break with business as usual. We cannot win overnight. Success will require sustained action across the entire decade between now and the deadline. It takes time to train the teachers, nurses and engineers; to build the roads, schools and hospitals; to grow the small and large businesses able to create the jobs and income needed. So we must start now. And we must more than double global development assistance over the next few years. Nothing less will help to achieve the Goals.”²² Annan uses *grow* as an active verb applied to business—something that “we must start now.” To the UN, collective action will create jobs and income, as opposed to the decentralized efforts of individual entrepreneurs and firms operating in free markets.

Insofar as the MDG campaign mentions private entrepreneurs, they are “partners” subject to “our” resolve: “We resolve further: . . . To develop and implement strategies that give young people everywhere a real chance to find decent and productive work. . . . To develop strong partnerships with the private sector and with civil society organizations in pursuit of development and poverty eradication.”²³

For their part, the IMF and World Bank are fervent advocates of free markets for prosperity, not statist strategizing, but some unlucky countries are so poor that they face the requirement to do statist strategizing anyway. This is in the form of what is called a poverty reduction strategy paper (PRSP). The

preparation of the PRSP requires planning that would overwhelm the most sophisticated government bureaucracy anywhere, much less the underskilled and underpaid government workers in the poorest countries: “The sector ministries prepare medium-term strategic plans that set out the sector’s key objectives, together with their associated outcomes, outputs, and expenditure forecasts (within the limits agreed upon by the Cabinet). These plans should consider the costs of both ongoing and new programs. Ideally, spending should be presented by program and spending category with financing needs for salaries, operations and maintenance, and investment clearly distinguished.”²⁴ If they have any time left after all this planning (not to mention time left after their meeting with the hundreds of donor missions that arrive every year to check up on the plan), they can also come up with a plan for those same donors: “an external assistance strategy in the context of the PRSP process that explicitly identifies the priority sectors and programs for donor financing. . . . More detailed external assistance strategies can then be developed for key areas through sectoral working groups in which representatives of major donors and line agencies participate. . . . Agreeing on financing priorities for individual donors within the framework of a global external assistance strategy, rather than through bilateral agreements.”²⁵

The World Bank and IMF further affirmed in the 2006 *Global Monitoring Report* a commitment to “accountability for achieving results by ‘Implementing the results agenda,’” in which they will draw “on MDB [multilateral development bank] frameworks and action plans to implement managing for development results (MfDR).” MfDR is summed up in a 2006 *MfDR Sourcebook*, prepared by the Organization for Economic Cooperation and Development (OECD) and the World Bank, which again places its faith in planning:

At the national level (see Part 2), MfDR is used in the planning and implementation of results-based national plans, budgets, and antipoverty strategies. International agencies may support this process with technical assistance.²⁶

In sector programs and projects (see Part 3), partner countries and development agencies use MfDR in planning assistance programs or individual projects that are based on country outcomes and priorities defined in national or sector development plans.

Of course, the failure to meet planning goals could occur because the goals were too optimistic or depend on factors beyond the control of the UN, IMF, and the World Bank. Far from absolving the aid community, however, this only raises the question of why so much energy is devoted to a campaign (the MDGs) that does not create any positive incentives for any actors because it is overpromising on things that the actors cannot control. The World Bank itself cautions poor countries against setting targets in the PRSPs that are too opti-

mistic for exactly this reason: “Most often [the PRSP targets] are overambitious; they are technically and fiscally unattainable, which defeats their role as effective incentives to action.”²⁷ The same PRSP Sourcebook of the World Bank also warns, “It must be possible to disentangle the effects of poor performance by the implementing actors from the effects of external shocks.”²⁸ The MDGs endorsed by the Bank fail both of the tests suggested by the Bank.

Even a group one might have expected to shy away from central planning—American private businesspeople—have shown surprising sympathy for it in foreign aid: “All 191 member states of the United Nations have agreed to eradicate extreme poverty and address the many other burdens facing the very poor through the Millennium Development Goals. Once a country has formulated a national development strategy, external donors and NGOs can then contribute their resources and expertise in support of the country’s priorities” (noted a consortium of Seattle-area private businessmen known as the Initiative for Global Development).²⁹

Of course, in between the extremes of central planning and anarchic searching, all human activities involve some degree of planning. Corporations operating in the free market have corporate plans and planning departments, and they coordinate their activities with these plans rather than with market mechanisms. Larger-scale projects are likely to involve more planning rather than small-scale projects. However, this kind of planning is not the same as the large-P Plans to end world poverty.

First, there is a difference between discovering what works (or what sells, to follow the corporate analogy) and then scaling up the discovery. Scaling up can be done by replicating a set of routine actions once the search for what works has found the right set of routine actions. Hence, scaling up often does involve some little-p planning. Discovering what works, however, can never be planned. Since the large-P Plans operate in many areas where there is not a good track record or knowledge base on what works (as the chapters in this book make clear), they are prematurely scaling up things about which there is no grounds to think they will work (or worse, scaling up things that have a demonstrated track record of failure).

Some of the (not very common) aid successes scaled up a discovery that did involve some small-p planning. For example, the vaccination campaigns of the World Health Organization (WHO), which successfully lowered infant mortality, certainly had some top-down planning. The success stemmed from finding that a combination vaccination package could be effectively administered (which was not automatic—perhaps it was due to the observability and ease of monitoring vaccinations and the simpler link between inputs and outcomes) and then scaled up campaign style to cover large numbers of children.³⁰ This

kind of success may have unfortunately led aid agencies to a stronger belief in the power of planning than was applicable in most other situations.

Second, although a large project like a dam or electric plant involves some planning, it takes place on purely engineering grounds. Ending world poverty is not an engineering problem (or even a vaccination problem); it presents many variables of human behavior as well as technical complexity.

Nevertheless, the aid agencies often seem to have in mind the kind of engineering problem that a dam poses when designing Planning solutions to the problems of poverty. They seem to assume a Leontief production function between aid inputs and development outcomes that lends itself to detailed planning (and makes it possible to come up with precise estimates for costs of attaining plan targets): “The starting point is for donors and aid recipients to agree on a financial needs assessment that identifies the aid requirements for achieving the MDGs. Donors then need to provide predictable, multiyear funding to cover these requirements, and developing countries need to implement the reforms that will optimize returns to aid.”³¹

The UN Millennium Project even talks about planning the growth rate, using a mechanical relationship joining aid, public investment, and growth: “By entering the projected public investments from the needs assessment into the macroeconomic framework, planners can assess whether the resulting growth rate is consistent with achieving the poverty target using country-specific poverty-growth elasticities and incremental capital-output ratios. Any major discrepancies between projected investment needs can be adapted to prepare an MDG consistent scenario.”³²

The World Bank has pursued a similar exercise of “costing the MDGs,” which then become the basis for recommendations about aid volume. Devarajan et al. report an attempt to derive aid needs for the MDGs based on the costs of inputs to the health and education outcomes covered by the MDGs.³³ There are two problems: first, the technology is seldom so simple as to know the precise “input requirement” for a particular output, and there is no reason to suppose that unit costs are constant as volume varies. Second, even if it were possible to overcome the first problem, it is one thing to estimate the cost of providing a health service as being, say, \$1 per drug dose, and a completely different thing to assume that an additional \$1 of foreign aid will result in a drug dose being given to a sick patient. Unwilling to stop themselves from being good economists, Devarajan et al. themselves state that they see no reason to believe their own calculations: “Empirical evidence from developing countries suggests only a weak link between public spending on education and school enrollments, or between health expenditures and mortality or disease.”³⁴

Unfortunately, many health problems in foreign aid are more difficult than the vaccination example I gave (and even this success story has stalled, with only partial coverage of, for example, African children against measles). The authors whom Devarajan et al. cite for this weak link, Deon Filmer, Jeffrey Hammer, and Lant Pritchett (also World Bank researchers—Pritchett and Woolcock have a similar discussion in this book), point out such stories as the results of a survey at government health centers in the Mutasa district of Tanzania. In the survey, new mothers reported what they least liked about their birthing experiences assisted by government nurses. The poor expectant mothers were “ridiculed by nurses for not having baby clothes (22 percent) . . . and nurses hit mothers during delivery (13 percent).”³⁵ Because of the insistence on working through governments, aid funds get lost in patronage-swollen national health bureaucracies, not to mention international health bureaucracies. In countries where corruption is as endemic as any other disease, health officials often sell aid-financed drugs on the black market. Studies in Guinea, Cameroon, Uganda, and Tanzania estimated that 30 to 70 percent of government drugs disappeared before reaching any patients. In one low-income country, a crusading journalist accused the Ministry of Health of misappropriating \$50 million in aid funds. The ministry issued an astonishing rebuttal: the journalist had irresponsibly implied the \$50 million went AWOL in a single year, whereas they had actually misappropriated the \$50 million over a three-year period.

The same belief in aid service costing implying aid service delivery appears in the Millennium Project’s *Investing in Development*, Sachs’s *The End of Poverty*, and the earlier report of the Commission on Macroeconomics and Health.³⁶ Each of these exercises has elaborate costing exercises based on unit costs of multitudinous inputs, but each fails to address the issue of who will be motivated to deliver these inputs to the poor in such a way that they produce better outcomes. Devarajan et al. cite the Commission on Macroeconomics and Health’s estimates as support for the estimates in their chapter, estimates based on the same flawed methodology that their chapter disqualifies on evidentiary grounds.³⁷

The UN Millennium Project also suffers from the first problem: that planners do not really know the precise technology that translates inputs into outputs. The participants in the Millennium Project themselves know this obvious point—“it is often difficult to precisely quantify the link between coverage of interventions and MDG outcomes”—yet insist in the same sentence that somehow “national MDG planning involves mapping interventions to MDG outcomes.”³⁸

The UN Millennium Project participants are also savvy enough to know that “on balance, it can be difficult to predict the direction of change for marginal costs—let alone its magnitude—as coverage increases.” Yet two pages earlier, the same authors are able to state that costs of meeting the MDGs follow from this simple formula:

$$[\text{Population size}] \times [\text{percentage of population reached}] \times [\text{number of interventions per person or household}] \times [\text{unit cost of the intervention}]^{39}$$

A key characteristic of the planners is that they decide on the nature of the foreign aid intervention in advance. They think they know both the technical fix and the manner of its implementation. To quote from Pritchett and Woolcock in chapter 5 in this book: on public service delivery, the planners opt for a preconceived solution:

That is, development activities (in general, and those supported by development agencies in particular) have almost uniformly attempted to remedy problems of “inadequate services” (in infrastructure, education, health, law enforcement, regulation) by calling upon a centralized bureaucracy to supply a top-down and uniform public service. These decisions to “skip straight to Weber” were historical, social, and political processes whereby the interactions between citizens, the state, and providers were simply overlooked. The solution was a coherent approach to service delivery in which a universal need was met by a technical (supply) solution, and then implemented by an impersonal, rules-driven, provider. That is, “need as the problem, supply as the solution, civil service as the instrument” became the standard organizational algorithm for solving public services concerns.

An even deeper problem is that plans can never have enough information about little problems since they are overwhelmed with the information requirements for hundreds of problems in hundreds of locales required to reach the big targets such as the MDGs. For a big plan involving myriads of intended beneficiaries, planners in the West have no way to use the knowledge of the poor people themselves about their own needs and problems. There is no way they can gather enough information to know which of the interventions has the highest payoffs in a given locale or even if a particular intervention has a high payoff or zero payoff.

A more subtle point is that development research itself may be hampered because the high social importance of human poverty is often taken as predetermining the research questions to be asked. Research in the natural sciences, in contrast, does not start with a predetermined research agenda, and so researchers can look for those questions that they can opportunistically solve. The first approach is more appealing morally, although Thomas Kuhn in *The*

Structure of Scientific Revolutions suggests that this difference in approach helps explain why progress in the natural sciences is faster than progress in the social sciences.⁴⁰

F. A. Hayek presciently noted more than sixty years ago how the complexity of knowledge made planning impossible. A representative quote is:

The interaction of individuals, possessing different knowledge and different views, is what constitutes the life of thought. The growth of reason is a social process based on the existence of such differences. It is of essence that its results cannot be predicted, that we cannot know which views will assist this growth and which will not—in short, that this growth cannot be governed by any views which we now possess without at the same time limiting it. To “plan” or “organize” the growth of mind, or for that matter, progress in general, is a contradiction in terms. The tragedy of collectivist thought is that, while it starts out to make reason supreme, it ends by destroying reason because it misconceives the process on which the growth of reason depends. Individualism is thus an attitude of humility before this social process and of tolerance to other opinions and is the exact opposite of that intellectual hubris which is at the root of the demand for comprehensive direction of the social process.⁴¹

The debate between planners and searchers in Western assistance is the latest installment in a long-standing philosophical divide in Western intellectual history about social change. The great philosopher of science Karl Popper described it eloquently as “utopian social engineering” versus “piecemeal democratic reform” (see chapter 19 in this book by John McMillan on the hubris of utopian social engineering): “The piecemeal engineer knows, like Socrates, how little he knows. He knows that we can learn only from our mistakes. Accordingly, he will make his way, step by step, carefully comparing the results expected with the results achieved, and always on the look-out for the unavoidable unwanted consequences of any reform; and he will avoid undertaking reforms of a complexity and scope which makes it impossible for him to disentangle causes and effects, and to know what he is really doing. Holistic or Utopian social engineering, as opposed to piecemeal social engineering... aims at remodeling the “whole of society” in accordance with a definite plan or blueprint.”⁴²

The missing elements in big plans, it can never be stressed enough, are feedback and accountability. Many chapters in this book (see, for example, chapters 6, 9, and 10 by, respectively, Reinikka, Martens, and Svensson) note the peculiar characteristic of foreign aid that distinguishes it from either commercial markets or democratic politics. In markets, the consumer is giving his own money to suppliers, who strive to satisfy his needs. In the domestic politics of democracies, the people who vote are the same ones who receive the services. In foreign aid, this feedback and accountability loop is broken: the rich people

who give the money or vote for foreign aid are not the ones receiving aid services. The poor have no way of registering their satisfaction or dissatisfaction with aid services by how they spend or how they vote. The bottom line is that aid agencies have more of an incentive to please the rich than the poor.

Alas, the planners are repeating the mistakes of history, just as my critique here is repeating criticisms that were made even at the time of the first development planners. As the blog AdamSmithee.com noted in response to Easterly (2006), the planner versus searcher debate goes back a long way.⁴³ S. Herbert Frankel, in the *Quarterly Journal of Economics* of August 1952, commented on the United Nations Primer for Development published in 1951: “It is . . . precisely because the authors of the report see economic development primarily as an intellectual or artistic exercise by leaders and governments that they fail to do justice to their examination of existing realities in underdeveloped countries. . . . Development depends not on the abstract national goals of, and the more or less enforced decisions by, a cadre of planners, but on the piecemeal adaptation of individuals to goals which emerge but slowly and become clearer only as those individuals work with the means at their disposal; and as they themselves become aware, in the process of doing, of what can and ought to be done.”⁴⁴

The planners have the rhetorical advantage of promising great things, the end of poverty. The only thing the planners have against them is that plans do not work.

1.1.2 Evaluating the Need for Big Plans

Another reason that planners dominate the debate on foreign aid is that poor countries are supposed to need a “big push” of foreign aid to get out of a “poverty trap.”⁴⁵ This taps in well to the planners’ affection for emphasizing resource transfers and implementing aid programs from the top. As Jeffrey Sachs explains in *The End of Poverty*, “When people are . . . utterly destitute, they need their entire income, or more, just to survive. There is no margin of income above survival that can be invested for the future. This is the main reason why the poorest of the poor are most prone to becoming trapped with low or negative economic growth rates. They are too poor to save for the future and thereby accumulate the capital that could pull them out of their current misery.”⁴⁶

Simple tests provide no support for either the low-income poverty trap or a role for aid in escaping it. Easterly divides the poorest quintile of countries at the beginning of each period in two between the half with the highest aid and the other half with the lowest.⁴⁷ There is no significant difference in growth rates between the two groups, despite average aid as percentage of GDP being

two to five times larger in the top group. The low-aid countries in the poorest quintile had no trouble registering positive growth for the whole period 1950–2001 and in the period 1950–1975. The bottom quintile (like the middle and second to bottom quintiles) had worse growth in more recent periods, possibly consistent with a poverty trap. However, this was the period in which the poorest countries had much higher aid, which should have made a poverty trap less likely according to the standard narrative. While possibly reflecting reverse causality from poor growth to higher aid, the stylized facts are not consistent with a low-income poverty trap due to insufficient aid.

To be sure, there were individual poor countries that failed to grow among the poorest countries. Chad had zero growth from 1950 to 2001, and Zaire/Democratic Republic of the Congo had negative per capita growth over this period. However, the stagnant economies were offset by such success stories as Botswana, which was the fourth poorest in 1950 but increased its income by a factor of thirteen by 2001. Lesotho was the fifth poorest in 1950 but increased its income by a factor of five over the half-century. Other subsequent success stories that were among the poorest in 1950 are China and India.

Other scholars have also failed to find any evidence for a “poverty trap.” Aart Kraay and Claudio Raddatz studied the saving rate and found that saving does not behave the way the poverty trap requires at low income. The reasons countries stay poor must lie elsewhere.⁴⁸

Poor countries do have lower growth rates relative to rich countries in some time periods, and so there is evidence of divergence between poorest and richest. This is not the same as the absolute poverty trap hypothesized above, but it is still of interest to ask why there is divergence. The UN Millennium Project and Jeffrey Sachs argue that it is the poverty trap rather than bad government that explains poor growth of low-income countries and the failure to make progress toward the MDGs. Sachs says, “The claim that Africa’s corruption is the basic source of the problem [the poverty trap] does not withstand practical experience or serious scrutiny.”⁴⁹ Likewise the Millennium Project says, “Many reasonably well governed countries are too poor to make the investments to climb the first steps of the ladder.”⁵⁰

The case for planners is even weaker if they must deal with the complexities of bad government, as many chapters in this book document. Jeffrey Sachs worries in *The End of Poverty*: “If the poor are poor because . . . their governments are corrupt, how could global cooperation help?”⁵¹ Unfortunately, whether governments of poor countries are corrupt must be determined by evidence, not by the writer’s chosen advocacy campaign.

The search for the elusive “well-governed low-income countries” casts a broad net. The Millennium Project report lists sixty-three poor countries that

are “potentially well governed,” and thus potentially eligible for a massive increase in foreign aid. The list includes five of the seven countries singled out by Transparency International in October 2004 as the most corrupt in the world: Azerbaijan, Bangladesh, Chad, Nigeria, and Paraguay. The list of “potentially well-governed” countries also includes fifteen governments that Freedom House classifies as “not free.” Such dictators as Paul Biya of Cameroon, Hun Sen of Cambodia, and Ilham Aliyev of Azerbaijan are on the list. President Aliyev of Azerbaijan scored a double as most autocratic and most corrupt since he was “elected” to succeed his autocratic father in 2003.⁵²

Although convinced that bad government was not the problem, the UN report did rule out aid to the four most awful rulers in the world. The report identifies these four governments—Belarus, Myanmar, North Korea, and Zimbabwe—as beyond the pale. This is a pretty small number for bad governments of the world. Even a dictator like the late Saparmurat Niyazov of Turkmenistan, who so terrorized his country that he renamed the months of the year after himself and his late mother, did not get into the UN bad despots club.

The UN seems desperately to want to deny the existence of bad government because it threatens another cherished model of traditional aid delivery, which this book will examine critically: the government-to-government aid model. In this view, the altruistic rich country government (either directly or through multilateral organizations) gives money to an altruistic poor country government, which implements aid projects to benefit the poor in the poor country.

Actually if the UN Millennium Project report about escaping the well-governed poverty trap had looked in its own country studies, it would have found interesting clues to this result, such as the following vignette on Cambodian schoolteachers: “Many supplement their income by soliciting bribes from students, including the sale of examination questions and answers. . . . The end result is a high dropout rate.”⁵³

Another camp of planners has a variant on the UN model of overlooking bad government. This other camp (associated with the U.S. government, World Bank, and IMF) says governments of poor countries are bad and the West should get tough with the bad governments—force them to change in return for aid. This contrasts with the UN/Sachs camps that says these governments are not so bad and should be free to determine their own development strategies. However, this artificially restricts the debate. It may be true that governments of poor countries are bad, and it may be just as true that Western attempts to change them have been fruitless.

Again evidence should decide the debate. The hypothesis is so straightforward as to lend itself to a test of bad government against the poverty trap as a story for poor economic growth in low income countries. Easterly runs a horse

race between initial income and various measures of quality of institutions.⁵⁴ There was divergence between 1960 and 2002. This does not contradict the evidence on lack of an absolute poverty trap over 1960 to 2001 presented earlier, since the predicted growth rate of the lowest-income group in the regression below is still significantly above zero. Both the following statements are true: (1) we can reject that the coefficient of growth from 1960 to 2002 on initial income is zero (unconditionally, it is positive), and (2) we cannot reject the hypothesis that the poorest quintile had the same growth as the top four-fifths of the sample. We could still detect a tendency toward absolute divergence with the help of the middle-income and high-income observations, even though we cannot detect abnormally low growth of the bottom quintile over the past four decades.

A robustness check on these results would be to consider whether there might be interaction effects such that the payoff to better government may depend on income, or vice versa. To consider such a possibility, Easterly does some simple nonparametric tests. The exercise divides the sample into upper and lower halves of good government (according to the various measures) and upper and lower halves of initial income, and then considers average per capita growth in the four groups: low income and poor government, low income and good government, high income and poor government, and high income and good government.⁵⁵ Figure 1.2 illustrates the results.

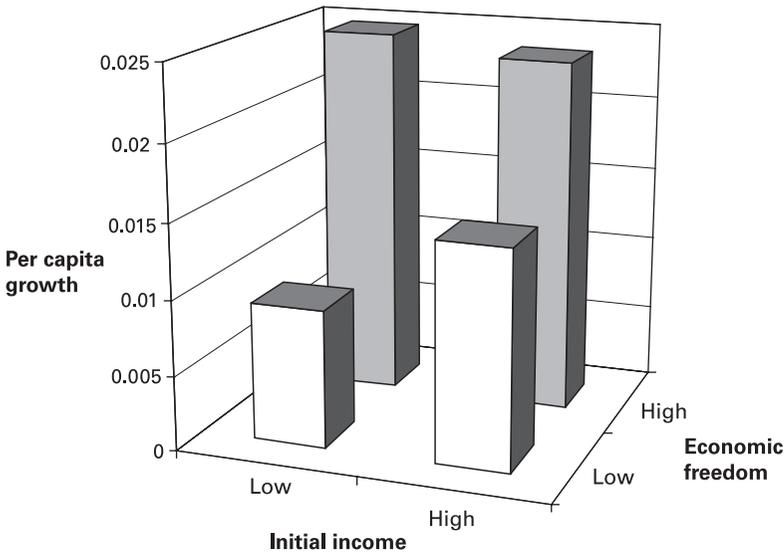


Figure 1.2
Economics growth, economic freedom, and initial income, 1950–2002

Economic growth increases with more economic freedom over 1960 to 2002 at both low and high income (the differences are statistically significant at the 5 percent level). Growth increases with more income at low economic freedom (but the difference is not statistically significant even at the 10 percent level) but decreases slightly at high economic freedom.

Of course, the largest question is whether aid raises economic growth. There is a vast and inconclusive literature on aid and growth (for a dissenting view that argues for clearly positive growth effects of aid, see chapter 16 by Radelet and Levine in this book). The literature suffers from such unrestricted specifications and endless iteration among these specifications that virtually any result on aid and growth is possible, and indeed virtually all possible results have already been presented in the literature: aid effects are conditional on good policies, they are not conditional on good policies; aid has a positive effect on growth, aid has no effect on growth; aid has a linear effect on growth, aid has a quadratic effect on growth; only certain types of aid matter, all types of aid are equivalent. Growth regressions in general have been criticized on the grounds of data mining and specification searching, since there are more right-hand-side variables that have been identified as empirical determinants of growth than there are degrees of freedom in the sample.⁵⁶ The aid and growth literature seems like a particularly egregious example of this problem (interestingly Durlauf, Johnson, and Temple did not even list aid as one of the right-hand-side variables that had been shown to determine growth).

What makes the big plan debate so contentious is that it is not easy to evaluate the effect of big plans. No identification strategy with such a deeply endogenous variable as aid is going to convince everyone, and indeed the regression wars on foreign aid and growth show no sign of ending any time soon. It is perhaps never going to be possible to have a natural experiment in aggregate data that conclusively resolves the effect of aid on growth. Far from being a defense of the big plan approach to aid, however, this is an argument against it. Why would anyone recommend a public policy to be pursued on a large scale without knowing whether its effects are going to be positive or negative?

As far as disentangling the different things that worked even if a big plan does work, this is pretty much hopeless. Doing everything at once is not a good search strategy for finding out what works to promote development.

1.1.3 How Searchers Handle Uncertainty Better Than Planners

What the planning vision always misses is that success is rare and failure is common. Economic success is always very uneven and unpredictable, across almost any possible unit of analysis one might consider.⁵⁷ The decentralized search for success is one big reason that free markets outperformed central

planning. It is seldom known in advance what will succeed. Many thousands of searchers mount myriads of different trials as to what will please consumers. A free market system gives rapid feedback as to which products are succeeding and which are not, and searchers adjust accordingly. Activities that succeed attract more financing and more factors of production so that they can be scaled up enormously; activities that fail to please consumers are discontinued. Planners do not have a search and feedback mentality; they implement a pre-conceived notion of what will work and keep implementing it whether it is working or not.

Economic success stories are often unexpected and unpredicted. MP3 players were invented several years ago and seemed to offer great promise as a great new way for music lovers to listen to large amounts of their favorite music. Despite this promise, none of the early players caught consumers' fancy. The Apple Corporation was known mainly for its failures in the PC market. It was a surprise when Apple suddenly found a huge hit in the iPod, which as of March 2006 had 78 percent of the market for MP3 players. So far Apple has sold 50 million iPods. The matching iTunes program of selling songs online to put on iPod accounts for 87 percent of the legal music downloads in the United States.⁵⁸

Histories of large firms are full of accidental discoveries of big hits. 3M today is a \$20 billion corporation. It started in 1904 with a failed attempt to mine corundum (3M stands for Minnesota Mining and Manufacturing). It then adapted to the failure by using the grit from its failed mine to make sandpaper. It was more successful when it tinkered to get a waterproof sandpaper. Its breakthrough product arrived by accident more than two decades later, discovered again by accident and by tinkering to find waterproof packaging tape that became an iconic consumer product: Scotch tape.⁵⁹

Johnson and Johnson, a \$50 billion corporation today, was founded in 1886. It produced a wide array of medical products such as medical plasters. In 1890, it started including a can of talc in shipments of its other products, in response to the request of a doctor for something to treat skin irritation from the plasters. To its surprise, the customers started requesting that they send just the talc. Thus was born another iconic consumer product of the twentieth century: Johnson's Baby Powder. Another happy accident came along in 1920 when an employee stitched together surgical tape and a small piece of gauze for his wife, who kept cutting herself in the kitchen, giving the world the Band-Aid.⁶⁰

Another easily observable example of the rarity of big hits is the Hollywood movie. Over the years 2000–2005, the top-grossing 5 percent of all movies released accounted for nearly half of total box office gross revenues over that period. Of course, the flip side of these success stories are the much more

numerous product failures—the bottom-grossing half of movies released from 2000 to 2005 accounted for a mere 0.4 percent of box office gross. This does not even take into account the numerous movie projects that never even get accepted by Hollywood studios.

Predicting what is going to be a hit in the movies is famously difficult. As William Goldman wrote in his classic *Adventures in the Screen Trade*, “Nobody knows anything. Why did Paramount say yes [to *Raiders of the Lost Ark*]? Because nobody knows anything. And why did all the other studios say no? Because nobody knows anything. And why did Universal, the mightiest studio of all, pass on *Star Wars*? . . . Because nobody, nobody—not now, not ever—knows the least goddamn thing about what is or isn’t going to work at the box office.”⁶¹

Uneven product success is closely related to uneven firm success. Just 0.3 percent of firms in the United States accounted for 65 percent of all firm sales in 2002.⁶² Firm size is well known to follow what is known as Zipf’s law, also known as a power law, in which the log of the size is a negative linear function of the frequency of this size occurring (or, equivalently, the rank). Power laws have generated a lot of hype; for the purposes of this chapter, it is enough to point out how large-scale success is rare, while failure is common. In other words, the frequency distribution of firms (or whatever other unit we are interested in) has a fat and long right-hand-side tail, of which there are many special cases such as a log-normal distribution and a power law (Pareto distribution).⁶³ In other words, most of the distribution is concentrated at some mediocre level; then there are a small number of firms that are just totally off the charts (way above what something like a standard bell curve would predict).

Of course, one reason that some large firms are so large is that they have been able to make the execution of a successful business formula routine, so that it can be replicated at low cost by inexpensive (not heavily trained) workers subject to managerial oversight. To return to the theme of the first section of this chapter, this is corporate “planning” at work, but only after the search for the right formula was successful. McDonalds could grow enormous using minimum-wage high school graduates following simple instructions to prepare meals. However, even this kind of planning is subject to competition from searchers, continually changing the environment and always threatening to make existing corporate plans obsolete. McDonalds has lost market share as other searchers have discovered Americans’ increasing desire for low-fat alternatives to Big Macs.

Maybe this is why, even though large firms dominate the marketplace, it is not so easy to be a large firm. Of the world’s largest one hundred companies

in 1912, some, like Procter & Gamble and British Petroleum, were many times larger in 1995. However, they were the exception, as 1912's big 100 firms also included such dinosaurs as Central Leather and Cudhay Packing in the United States. Only 19 of the top 100 in 1912 were still in the top 100 in 1995, and 48 of 1912's big 100 had disappeared altogether by 1995.⁶⁴

This unpredictable behavior has given rise to pseudoscience even worse than development pseudoscience. Business books lay out the secrets for success of a few large companies celebrated by the author, only to see the firms fall on hard times after the book is published. Business writers celebrated Enron for its innovative approach right up to the last minute.⁶⁵ Even the most successful business gurus have their embarrassments: Tom Peters' and Robert Waterman's 1982 mega-best seller, *In Search of Excellence*, included among its celebrated companies some that would later go bankrupt, such as Atari, Wang, and Delta. This generation's guru is Jim Collins, who coauthored the 1994 *Built to Last* (3.5 million sold over its first ten years) and followed up with another big hit in 2001 in *Good to Great*. The magazine *Fast Company* concluded in 2004 that about half of the companies identified as built to last in 1994 have since stumbled badly (among them are Motorola, Ford, Sony, Walt Disney, Boeing, Nordstrom, and Merck) and would not meet the criteria for a 2004 *Built to Last* list. In fact, Jim Collins's own *Good to Great* suggested in 2001 that Merck was now second rate and identified a new pharmaceutical success story: Abbott Laboratories.⁶⁶

Another from an inexhaustible list of such examples is Harvard Business School strategy guru Michael Porter. As late as 1990, Porter was celebrating Digital Equipment Corporation (DEC), which was destroyed by the competition from personal computers a mere two years later.⁶⁷

Such business books have no predictive power because they are based on slippery propositions that cannot be tested or falsified (what Collins calls a "law of physics" is "preserve the core, but stimulate progress"—in other words, a business should both change and not change).⁶⁸ You could say the best-selling business authors do meet the market test themselves, but so do astrologists.

The difficulty of achieving and maintaining success is not peculiar to large firms. Every year, about 10 percent of existing firms of all sizes go out of business. Not that it is so easy to start a new firm to replace the ones that go out of business. More than half of new firms fail within four years of their founding in the United States.⁶⁹ With so much uncertainty even in an economy with well-developed institutions, infrastructure, and technology, imagine how much riskier is the world of foreign aid and economic development.

1.1.4 The Strategy of Search

What is the best way to handle this uncertainty? A mathematical example may help illustrate this. Suppose an aid agent tries to execute a comprehensive plan that has n components that each must work for the plan to be successful (this is the strongest version of complementarity, one of the traditional arguments for the big push). The components are such things as agricultural productivity, health, education, housing, sanitation, clean water, roads, and electricity. For each of these areas, an intervention is designed. If each component i has a probability of p_i of working, then the probability p_s that the n -component comprehensive plan will work is:

$$p_s = p_{1j}p_{2j}p_{3j}, \dots, p_{nj}. \quad (1.1)$$

It is of course more realistic to have a separate p_i for each component i , but let us assume that the probabilities are equal to illustrate how the number of components lowers probability of success of comprehensive plans:

$$p_s = p^n. \quad (1.2)$$

If the number of components is 10, then even with a probability of each component succeeding as high as .85, the overall probability of success of the comprehensive intervention is only .20. If the number of components is 20, the probability of success is only .04.

There is plenty of reason to think that the number of interventions has to be large for a comprehensive plan. Each of the components above has multiple subcomponents, which in turn have subcomponents. For example, attaining good health requires dealing with AIDS, malaria, tuberculosis, infant diarrhea, and other maladies, all of which have separate interventions. Dealing with malaria requires interventions like medicines for those who have malaria, and for prevention such measures as indoor spraying, bed nets, and drainage of standing water. Dispensing bed nets in turn will be successful if funding is available for the net, if the net is designed correctly (e.g., impregnated with insecticide, easy to use), if each intermediary along the way between manufacturer and consumer passes along the net (through an administrative or commercial transaction), if the consumer is successfully educated on the importance of sleeping under the net every night, and on a number of other idiosyncratic details that cannot even be anticipated.

It is little wonder, therefore, that in an attempt to be comprehensive, the UN Millennium Project listed 449 separate interventions to achieve the MDGs. For this number, even a probability of success of each intervention of 99 percent

would yield an overall success probability for the comprehensive plan of 1 percent. This is the ultimate revenge of complementarity: the same strong complementarity that big push advocates say requires a comprehensive plan also makes it unlikely that the comprehensive plan will work.

But suppose you search among m possible interventions and are content to find one that works, which you will then scale up. The reason that development is possible at all is that there are not only complementarities among inputs to development outcomes; there is also the possibility of substitution. Suppose that the m interventions are perfect substitutes for each other for your particular objective. If the objective is general—perhaps, “Find something that works to help a lot of poor people at a feasible cost,” which would be typical of the open-minded searchers’ approach to aid—then indeed many possible interventions are perfect substitutes. (This is the same principle that makes businesspeople successful searchers: they have the general objective of profits and can search among many possible products for one that delivers a profit. See Duggan 2003 on this point.)⁷⁰ The point of this section would be embarrassingly simple if it were not so widely violated in practice: setting a fixed intermediate goal to a more general good is counterproductive, since the chances of success are so much higher if you are willing to accept any intermediate step to the general good.

For example, chapters 2 and 3 by, respectively, Banerjee and He and by Duflo and Kremer in this book give many examples of interventions that have been found to work to alleviate poverty and can be scaled up with the limits of politically feasible aid budgets: remedial teaching, uniforms and textbooks, schooling vouchers, monetary rewards to parents for sending children to school, iron supplements, albendazole (deworming), iodine supplements, condom provision, improving management of sexually transmitted diseases, voluntary counseling and testing for HIV prevention, prophylaxis for opportunistic infections, short-course zidovudine regime, spraying for malaria, fertilizer, vaccines for various illnesses, school meals, and putting a second teacher in the classroom.

The probability that at least one intervention will work when searching among m interventions is:

$$p_s = 1 - (1 - p_1)(1 - p_2)(1 - p_3) \dots (1 - p_m). \quad (1.3)$$

For purely illustrative purposes, suppose that all the p 's are equal (of course, this does not make any sense since search would be pointless if all interventions have the same probability of success; we will say for the moment that the searchers do not know this until they try each one). With this, equation 1.3 simplifies to

$$p_s = 1 - (1 - p)^m. \quad (1.4)$$

With perfect substitutability, the power of multiplication works for us rather than against us. With a probability of success of each intervention of .85, you need to try only three different interventions to get a probability of .99 of success (because only one has to succeed). If the success probability for each intervention was as low as .5, then it would be enough to experiment with seven different interventions to reach a probability of .99 for success; a success probability of a miserable 0.2 would still require a less than herculean nineteen different experiments to attain .99 probability of at least one success.

Note that the power of searching compared to planning holds even when we consider the probabilities of one step being executed successfully as the same between comprehensive planning and decentralized searching. In reality, incentives for completing an intervention (presumably raising its probability of success) are more difficult to implement with planning than with searching. Moreover, the bureaucracy of planning could itself create a longer list of necessary conditions for success than with decentralized searching. For example, bureaucracies create rules that officials must sign off on different steps for a task to proceed. The risk that a careless or unmotivated official will not sign off on an otherwise successful task adds to the risk of failure.

Having multiple searches for what works may sound like a lot to a planner, who thinks in terms of a top-down bureaucratic hierarchy. However, the great thing about searching is that it can be totally decentralized. A myriad of searchers are available in the field to look for what works for each piece of the puzzle. The aid system just has to be designed so that it rewards successful searches and scales them up to achieve widespread benefits for the poor.

1.1.5 Conclusion

The comprehensive ambitions of the planners have misfired badly, crowding out more sensible and pragmatic approaches that are humble about their own limitations. The world's poor will mostly determine their own fate by their own home-grown institutions and initiatives, as much historical and contemporary evidence suggests.

In the meantime, however, the efforts of the rich world to help the poor could benefit from a lot more piecemeal searching and a lot less comprehensive planning. The 2006 Nobel Peace Prize was a contest between a searcher (Mohammad Yunus) and a planner (Bono). Maybe Yunus's award is a good omen for a more constructive approach to the tragic problems of the world's poor. The many constructive insights in this book are a good start.

1.2 How to Reinvent Aid

None of the chapter authors are claiming that their ideas will achieve the end of poverty. They just take on specific problems and propose hard-headed solutions. In this section, I weave together some of their conclusions and debates. My goal is more to stimulate a reading of the chapters and suggest how they fit together than to be a comprehensive summary of each chapter. Note, however, that not all the authors necessarily agree with each other (or with me). Rather, the value of this book is that it offers an airing of different viewpoints by some of the leading scholars in the field.

The chapters in part I discuss evaluation of aid interventions.

Abhijit Banerjee and Rumin He give examples in chapter 2 of interventions that have been verified as cost-effective uses of foreign aid (using the methodology discussed by in the following chapter by Duflo and Kremer): deworming; dietary supplements like those for iron, vitamin A, and iodine; education in using condoms and treating other sexually transmitted diseases to slow the spread of AIDS; indoor spraying to control malaria; fertilizer subsidies; vaccination; and urban water provision. None of these are keys to development according to some utopian scheme; they are modest interventions, but they make people's lives better. Banerjee and He also note many problems on the way to getting these interventions to the poor. Although they identified these interventions as effective through a careful scientific methodology, the donors themselves do not subject themselves to independent evaluation. They lament the lack of evaluation as one of the key weaknesses of aid agencies.

Duflo and Kremer in chapter 3 discuss the methodology of randomized controlled trials (RCTs) to evaluate aid interventions. They argue, "There is scope for considerably expanding their use, although they must necessarily remain a small fraction of all evaluations." The RCT is a welcome introduction of the scientific method into foreign aid and development, an area where wishful thinking, politically motivated conclusions, and pseudoscience have perhaps been more predominant than in other areas of economics. The RCTs are not a panacea, and they are not applicable to all areas of foreign aid and development, but they have already made a great contribution to the field of economic development.

The World Bank has recently endorsed the idea of RCTs on a very small scale with its Impact Evaluation group.⁷¹ These are used to evaluate which interventions work (a noble purpose), though not for holding the bank itself or any of its units accountable for results. The bank fails to specify any consequences it might have, for example, in managerial or staff rewards for good performance.

Chapter 4 by Lant Pritchett discusses the political economy of why rigorous evaluation is so rare in foreign aid, either for knowing what works or for accountability purposes. Even purely altruistic advocates for particular interventions and particular objectives have an incentive to do just enough to persuade the public to allocate funds to the program, without risking a possibly negative rigorous evaluation. Log-rolling coalitions of single-issue advocates can form, all agreeing that “I won’t demand rigorous evaluation of your program, if you don’t demand it of mine.” Pritchett goes into much more precise detail about how political incentives kill off rigorous evaluation. As with all other political economy analyses, it is hard to say what would break the logjam. Perhaps a more informed and more demanding public can force agencies to do evaluation anyway?⁷²

The chapters in part II address the Gordian knot of the state. Foreign aid has struggled mightily with the question of how to deal with the government in the aid recipient country. The central dilemma is that donors want to give money to states led by what the donors think is a good government, yet at the same time they believe that the “country” (always meaning the government) should “own” its homemade approach to development. There is an inescapable contradiction between the donors’ imposition of conditions on what it takes to be a good government and the logical implication of “ownership” that the “country” will decide on its own what is a good government. The donor agencies paper over this contradiction with euphemisms or simply present contradictory statements side by side in the same donor report. For example, DFID’s 2006 white paper is about “making governance work for the poor.” There is some ill-defined way in which “we [the donors] need to help governments and citizens make politics work for the poor,” putting “support for good governance at the centre of what we do.” DFID sternly lectures poor country governments that “unless governance improves, poor people will continue to suffer from a lack of security, public services and economic opportunities.” Yet the same report also takes the opposite approach: “If developing countries are to lead their own development, they [meaning the governments] must have more authority to ensure that the international development system responds to their needs.”⁷³

The more intellectually consistent researchers in this book struggle with these same questions. Are donors bound to give aid through the recipient state out of respect for its sovereignty? (This was the traditional idea that still binds the World Bank and IMF, for example.) Or should they bypass dysfunctional, often corrupt, states and try to get the aid directly to poor people? Or would such bypassing undermine and retard the political development of the state in the poor country? Or are donors currently making the state worse—more

corrupt, more bureaucratic, more accountable to donors than to their own citizens—with their current practices? There is no easy answer and no consensus on these questions by the authors of the chapters in part II, but plenty of dazzling insights.

Pritchett and Woolcock in chapter 5 have a tour d’horizon of the difficult issues facing state delivery of public services in poor countries. They draw an effective double dichotomy between discretionary versus nondiscretionary and transaction-intensive versus nontransaction-intensive activities. Areas that are discretionary but not transaction intensive can be handled with “ten smart people.” Areas that are nondiscretionary but transaction intensive can be handled with a nearly automated procedure that can handle the large volume of transactions (see the discussion of corporate planning above). The problem with most public services is that they are both discretionary and transaction intensive (think of nurse-patient and teacher-student interactions, for example). In the authors’ words, they “are intrinsically incompatible with the logic and imperatives of large-scale, routinized, administrative control.” They document failures in rural water supply (where 50 percent of standpipes administered by the central government broke down due to lack of maintenance), irrigation, schooling, family planning, agricultural extension, and health care (where patients often bypassed public clinics for private and traditional healers). When the failure of public institutions in all these areas was recognized, donors sent “experts” from rich country bureaucratic environments to redesign poor country bureaucratic institutions (the authors note that this is “like sending a cab driver to design a car”).

Pritchett and Woolcock document three other failed remedies, which they refer to as intensification (do the same, just try harder), amputation (privatize even if there is a market failure or political expectation of government responsibility that created the need for the public service in the first place), and policy reform (which fails to recognize that “policies” are not transaction intensive and are not hardest to change).

The current proposals for reform after these three failures now take us up to eight different choices: (1) supplier autonomy (public sector reform II), (2) single-sector participatory, (3) contracting out, (4) decentralization to states or provinces, (5) decentralization to localities or municipalities, (6) demand-side financing, (7) social funds, and (8) community-driven development. They see “no theoretical or empirical basis for making any claims about what the ‘right’ solution is for any sector in any country that has not itself tried the alternatives.” They conclude more constructively that “if the incessant quest for *the* solution is in fact the problem, development professionals need to help create the conditions under which genuine experiments to discern the most

appropriate local solutions to local problems can be nurtured and sustained.” (In terms of section 1.1 of this introduction, Pritchett and Woolcock recommend searching rather than planning.)

Chapter 6 takes on the issue of whether donors should bypass the government to deliver public services directly or work with the government. Reinikka sides clearly with the second, joining those concerned about aid agencies’ undermining the local state by interfering in the relationship between the state and the service providers. She points out that having aid donors deal directly with the latter can destroy the relationship of accountability between the state and the service providers that work for it. This is an important consideration in the three dozen developing countries where aid provides more than 40 percent of the country’s total public spending. Sometimes donors even set up parallel project units that are accountable only to the donors and drain off local professionals (in Kenya, for example, “a World Bank agricultural project paid eight local staff between \$3,000 and \$6,000 a month, many times the \$250 available to a senior economist in the civil service.”)

Reinikka would prefer that donors work within the local state, aligning their support with what it is doing. Measures to improve citizen voice and feedback to the state are more constructive than having the donors themselves force conditions down the throat of the state. But she notes that the “unintended negative effects of donor behavior” are a long-standing problem, in part explained by the donors’ having other objectives besides reducing poverty.

Chapter 8, by Moss, Pettersson, and Van de Walle, has a much less benign view of how the aid system interacts with governments in poor countries. These authors see aid as often reinforcing the patrimonial, patronage-driven, rent-seeking state in Africa, “where some countries have now entered into their third and fourth decades of receiving substantial volumes of aid.” In their own words:

Projects provide for the allocation of all sorts of discretionary goods to be politicized and patrimonialized, including expensive four-wheel drive cars, scholarships, decisions over where to place schools and roads, and so on. The common practice of paying cash “sitting fees” for civil servants attending donor-funded workshops, where the daily rates can exceed regular monthly salaries, even turns training into a rent to be distributed. . . . Aid dependence thus leads to a situation in which bureaucrats are often not rewarded for focusing on their core developmental functions but rather on getting money from donors.

They see a long history of aid agency attempts at improving governance, with little sign of progress: “The World Bank alone provided Africa with 70 civil service reform projects between 1987 and 1997.”

The authors then give voice to a long-standing worry about aid: that it makes government officials much more responsive to aid agencies than to their own citizens: “If donors are providing the majority of public finance and governments are primarily accountable to those external agencies, then it may simply not be possible to also expect a credible social contract to develop between the state and its citizens. Using the current terminology, aid may undercut the very principles the aid industry intends to promote: ownership, accountability, and participation.” Large aid flows can result in a reduction in governmental accountability because governing elites no longer need to ensure the support of their publics and the assent of their legislatures when they do not need to raise revenues from the local economy, as long as they keep the donors happy and willing to provide alternative sources of funding.

Aid may actually lead to a decrease in the country ownership the donors say they are promoting. Moss, Pettersson, and Van de Walle note that African leaders typically enjoy high longevity in office despite chronically poor economic performance. The African state is characterized by strong presidential rule, with weak legislatures and civil society and few participatory checks on the executive. Since donors play such an important role in governmental functions, the government can blame the donors for poor public service delivery (while the donors of course blame the government). The authors are sufficiently chastened by their review of the historical record that they close by suggesting that the extra public dollars now being proposed for traditional development assistance might well be better spent for other types of assistance that in the long run would have a greater impact on the development of the region.

Kremer and Miguel in chapter 7 also take a less sanguine view of the viability of aid working through governments. They note the stubborn persistence in the aid community of the notion of sustainability of projects, meaning that aid projects should be taken over by local or national governments, or at least some locally organized user committee. This is inspired more by the appealing dogmas of the self-help gospel than any appreciation of aid or political incentives. In reality, sustainability has been an illusion, as recipient governments or local groups seldom take over aid projects and so projects are not sustained. The consequences are unhappy. In one large water project in western Kenya, “43 percent of borehole wells were useless ten years after the shift from external donor support for water-well maintenance to the training of local maintenance committees.”

Kremer and Miguel study the case of deworming drugs to analyze different methods commonly put forward to promote sustainability. They point out one common problem: most of the benefits of taking drugs against highly

contagious worm infections accrue to others rather than to the individual. Hence, it is not so surprising that interventions that rely on strong individual incentives (e.g., user fees or education of individuals on the need for the drugs) fail in their study. Peer pressure could solve collective action problems created through externalities, perhaps leading to another path to sustainability. However, Kremer and Miguel also rigorously study peer effects on using the drugs and find them to be negative. They conclude that a good that has external benefits to others should be subsidized indefinitely. Locally funded governments would be best suited to provide a good with local externalities, like deworming drugs, but local governments in Africa are weak and do not raise their own revenue from local communities. Donors may or may not want to fund a public good that needs indefinite financial support, but there is no reason that they should keep chasing the illusory hope that temporary funding will ensure that a public good will be permanently sustainable.

Part III takes a step back to look at what aid agencies are supposed to do and what they actually do. In chapter 9, Martens asks the sensible question: Why does delivery of money have to be tied to implementation of programs and projects by the same agency? His answer is that aid agencies are intermediaries between the wishes of donors and the wishes of recipients. First, the donor may have other interests to accommodate besides meeting the needs of recipients, such as donor country foreign policy or commercial interests: “For instance, a bilateral aid agency may approve the delivery of water pumps to a village in the recipient country. Such a project satisfies the preferences of all donor interest groups: genuine wealth transfers and empowerment of (water-carrying) women, profits for commercial water pump suppliers and consultants involved in the project, visibility for the donor government, political goodwill from the influential village politician in support of the political interests of the donor country.”

Second, the donor agencies must deal with the nonalignment of donor and recipient preferences, because the recipients may be engaged in behavior of which the donor does not approve. The donors invest heavily in project management and monitoring and put conditions on aid to make sure the “right” recipient behavior takes place, although they seldom put it in these terms (citing instead their allegedly greater managerial and policy expertise).

Multilateral agencies are sometimes favored instead of bilateral agencies for aid delivery because they can realize economies of scale and scope for information gathering (such as for conditionality), and they can internalize externalities from aid-industry public goods that would be underprovided by each bilateral aid agency. This is the theory, at least; whether it works in practice will be considered more here.

Martens closes with a bracing dose of common sense on the current state of aid:

So far, there has been very little debate in the aid community on the merits of various types of agencies and aid instruments. This is partially due to the fact that the aid community has apparently rallied in recent years around the single objective of poverty reduction, with the implicit assumption that all donors, recipients, agencies and actors in the aid delivery process are motivated only by that same objective. . . . This is not only unrealistic but also unhelpful to understand the incentives that play a role in the aid delivery process and the comparative advantages of different types of aid agencies.

Martens is searching not only for which aid interventions work but also which types of aid agencies are best suited to carry out those interventions.

Svensson, in chapter 10, emphasizes the broken feedback loop between aid recipients in the poor country and taxpayers in the rich country who fund aid. This creates incentives in the aid agencies to emphasize things easily observable to the rich country public like volume of aid and to underemphasize getting (less observable) results with those funds.⁷⁴ (Another interesting example of this emphasis on observability is that a natural disaster heavily covered by the news media gets much more aid than a similar disaster less well covered. Earthquakes are better covered than famines, so a famine would have to have 40,000 times as many deaths as an earthquake to get equivalent news coverage and aid.)

Svensson suggests some practical measures to enhance visibility of results and get client feedback, backed up by field experience. A study that Svensson coauthored (with Reinikka, who contributed chapter 6 to this book) found that only 13 percent of aid and domestically funded central government grants to local schools were actually reaching the schools. The study prompted the government to start publishing the amounts of the grants in the newspapers, where they could be monitored by parents. After this program began, the schools started receiving 80 percent of their intended grants.

Other features of the emphasis on observable volumes of aid require different solutions. Since the country or sector allocation of the aid budget is made by a central unit in the aid agency, and then the disbursement decision is made by a lower-level department, the latter has an incentive to always spend the budget. This lowers the credibility of threats to withhold disbursements unless aid conditions are met. The recipients hence have little incentive to observe conditions, explaining the empirical record on how conditions are often violated. Svensson proposes an alternative: to have “aid tournaments,” in which the aid budget is allocated to a pool of countries and then disbursed only to the best-performing countries in the pool.

Next, Knack and Rahman note in chapter 11 the well-known problem of donor fragmentation, in which a large number of donors each have a small share of the total aid inflow into a country. In a typical African country, some thirty official donors and several dozen international nongovernmental organizations (NGOs) provide aid through over a thousand distinct projects and several hundred resident foreign experts.⁷⁵ Echoing Reinikka's concern about undermining government, Knack and Rahman give an example from Niger where several ex-government ministers left governments to set up local NGOs that received aid funding that otherwise would have gone to their former ministries. Knack and Rahman show that both a higher level of total aid and higher donor fragmentation are associated with worsening bureaucratic quality in aid recipient governments from 1982 to 2000, where bureaucratic quality measures "autonomy from political pressure," "strength and expertise to govern without drastic changes in policy or interruptions in government services" when governments change, and "established mechanisms for recruiting and training." While donors complain about the low quality of bureaucracy in poor countries, the results of Knack and Rahman suggest that donors themselves are partly to blame. The authors recommend holding aid agencies to account for "how each donor proliferates aid across recipients and sector."

Part IV considers two notable actors in the foreign aid arena: the International Monetary Fund and the World Bank. The IMF does not consider itself an aid agency and is not usually classified as such by others. It is seen instead as a bail-out lender for countries with economic crises. However, this conventional classification has eroded to the point of collapse because the IMF is a notorious repeat lender to low-income countries, much of whose debt was later forgiven, and so *de facto* was an aid provider to these countries. The World Bank does consider itself an aid agency, but exactly what kind of aid agency it should be has been much debated over time.

Vreeland finds in chapter 12 that IMF lending lowers economic growth in the loan recipients, a finding that is consistent with several other recent studies. Even less econometrically ambitious studies prior to Vreeland and the other recent literature has found a zero effect of IMF lending on growth. The finding of negative or zero growth effects of IMF lending echoes the findings on overall aid (the emphasis on negative results in the literature so far is stronger with IMF lending than with aid). So the question becomes, Why do countries borrow from the IMF if it lowers their growth, not to mention that it was politically unpopular anyway? Vreeland's answer is sobering and controversial:

Governments enter into IMF programs under bad economic circumstances. Their choice is not usually between good and bad economic performance, but between bad performance on their own—without the IMF—or worse performance under a program spon-

sored by the IMF. . . . By bringing in the IMF, governments gain political leverage—via conditionality—to help push through unpopular policies. For some constituencies, these policies dampen the effects of bad economic performance by redistributing income upward and thus rewarding elites. If the distributional consequences are strong enough, key groups can be made better off even though growth is hurt. But IMF programs doubly hurt the less well off in society: total output growth is lowered, and income is shifted away from them.

While the IMF claims to be apolitical (as all aid donors always do), to Vreeland it is clearly a political actor: “Yet the moment the IMF demands [some conditions to be met], it has entered into domestic politics. The influence of the IMF can be used as leverage to push through policies that favor some at the expense of others; the IMF should not pretend otherwise.” This portrait does not leave one sanguine about the current status quo of IMF lending and aid.

Morduch in chapter 13 has a complementary analysis about the World Bank’s claim to be a neutral actor, this time in the realm of knowledge about development. One problem is the bank’s universalist approach, celebrating “best practices” that are alleged to apply everywhere. This leads to complaints such as that the bank pays “little attention to local needs or ideas,” or to “local circumstances,” or to “alternative perspectives.” Even the bank’s dissemination of its knowledge is criticized as too focused on the government and to “top-down.”

Then there is the problem that the World Bank faces organizational incentives to be too favorable about a particular paradigm, even when evidence contradicts it. Morduch quotes a bank official with one such example, a review of a structural adjustment loan to Zambia in 1990:

Projects and programs of technical cooperation are developed within the governing sets of assumptions or paradigms, and must comply with them, even in situations where the staff and the client know that the prevailing paradigm is highly unreliable, if not downright wrong. The phenomenon is quite striking in the field of economic adjustment where an operation containing a few important measures is expected to return an entire economy to a strong growth path within a miraculously short timeframe, despite a backlog of decades of economic mismanagement. When, as might be expected, the operation by itself fails to achieve the promised economic growth, reports are written assigning reasons for the shortfall. Ironically, the one cause that such evaluation reports are not allowed to discover is frequently the real reason—namely a faulty paradigm.

Morduch further analyzes how a priori attachment to questionable paradigms can even create poor incentives for data collection: “People with strong positions (either for careerist or ideological reasons) may actively work to discourage data collection that could undermine their credibility.” More generally, when the World Bank takes public positions on economic policies in its

operations, then its role of disinterested repository of evidence for and against these policies is not going to be credible. This is deeply problematic, as it tarnishes the reputational mechanism by which users—whose lack of resources to independently collect and verify knowledge created the need for the “knowledge bank” in the first place—could know what knowledge to accept as reliable.

Morduch gives an example of the “knowledge bank” misfiring on the issue of microcredit. The World Bank put forward as a best practice the idea that microfinance should be commercially self-sustaining (also endorsed enthusiastically by the U.S. Agency for International Development (USAID)). Morduch points out this view turned out to be both theoretically and empirically problematic. Theoretically, this creates obvious incentives for microlenders to drift to richer clients, contradicting the original objective of reaching the poor. Empirically it was not clear that the real world fit the ideal of commercially viable microlending. (Morduch’s magisterial book on the subject points out that many microcredit schemes rely on donor subsidies.) Nor were data collected to test the socioeconomic benefits of microlending (the universal standard for judging success of microlending was the repayment rate, hardly a clear measure of success at helping the poor.) The advocates for the “best practice” did not collect data that could be used to test these purely empirical questions—to such a notorious extent that the U.S. Congress passed a law in 2004 to force USAID to collect the data!

The final part of this book looks at various new and imaginative proposals for distributing aid.

Michael Kremer advocates in chapter 15 that aid resources be used to make an advance purchase commitment (APC) for vaccines against diseases such as malaria, AIDS, and tuberculosis. There is a global market incentive to do medical research on diseases that afflict those who will pay the most for the drugs: the rich. Infectious and parasitic diseases account for only 3 percent of the disease burden of the rich but one-third of the disease burden in poor countries. The result is as predicted: there is little research into drugs for such diseases. An APC would have donors guarantee to purchase X million doses of a vaccine for, say, malaria for a price of Y , giving private drug companies the incentive to do research on a malaria vaccine. The advantage of this pull mechanism for research is that money will be spent only on success. If the drug companies fail to find a cure, the initiative will have cost nothing. If the drug companies succeed, millions of lives will be saved. Since vaccine delivery has been more successful than many other aspects of foreign aid, since it is readily monitorable and needs to be delivered only once to each patient, a new vaccine will bypass those parts of the foreign aid system that are not working well.

Levine and Radelet discuss in chapter 16 some new mechanisms in aid that have already started: the Millennium Challenge Account (MCA) of the United States, the Global Fund against AIDS, TB, and Malaria (GFATM), and the Global Alliance on Vaccines and Immunizations (GAVI).

The MCA seeks to untie the Gordian knot of the state by seeking to screen out “bad” governments and then allow the “good” governments to determine their own programs. In practice, neither part works as well as in theory: (1) it is not so easy to find a group of sixteen or so countries that unambiguously have good government compared to the muddle in the middle, and (2) the MCA cannot bring itself to fully relinquish influence over the design of the programs. The MCA does place greater emphasis on evaluation and monitoring of results than existing aid programs, but it is operating on such a broad canvas that it is not clear how to measure its impact on outcomes that depend on many other factors.

GFATM was a notable advance in specializing in three diseases on which there is broad consensus that there could be high payoff to focused action. It also promised to be performance based, although the methodology for this still remains unclear. Its approach to the “bad state–good state” problem was to leave it up to each country to come up with a participatory country coordinating mechanism (CCM) to administer the funds, and it did not screen out any but the most egregiously “bad” states like North Korea. It still remains unclear how participatory the CCMs are, and all of these actions by the Global Fund have generated some controversy that has yet to be resolved.

GAVI is also noteworthy for taking a focused, performance-based approach to one set of interventions that are low cost and high benefit. As Levine and Radelet explain, “GAVI provides an incentive for expanded coverage by, first, ceasing funding if and when coverage declines or fails to increase at an acceptable rate; and, second, rewarding coverage increases with a one-time transfer of \$20 per additional fully-immunized child.” GAVI has already cut off some poor performers. It has been less successful in catalyzing supportive funding for immunization, and prices of new drugs have not fallen as quickly as GAVI expected.

All three new agencies have lean headquarters staff and hence begin to address the concerns about excessive bureaucracy in foreign aid. Nevertheless, the creation of three new agencies has itself added to the bureaucratic tangle of actors operating in foreign aid. As the authors note, “The United Nations is replete with specialized agencies that began with the promise of a narrow focus, clear objectives, a smaller bureaucracy, and more effective support for development.” Whether these three agencies will follow the fate of the now ineffective bureaucratized agencies at the UN or represent promising new

approaches that put competitive pressure on existing aid agencies is something that will be closely watched by aid observers in coming years.

In chapter 17, Whittle and Kuraishi are clearly negative on the existing aid bureaucracy. They condemn the current approach to aid in a manner similar to (and which helped inspire) the planners versus searchers dichotomy already discussed: “Efforts in international development are conducted largely by unwieldy bureaucracies that centrally plan economies of developing countries, by making large-scale choices. If the international aid regime were a national economy, one thing is clear: the World Bank and IMF would be after it to reform. . . . Top-down and agency-driven approaches translate into projects that are not responsive to the needs of local communities, tend to serve the priorities and perspectives of so-called aid experts rather than the aid recipients, and lead to inefficient results.” They suggest that the free market is a good metaphor (and possible inspiration) for how the aid system could work better. A free market rates borrowers and lenders. Could an aid marketplace develop ratings for aid donors and aid recipients? Markets feature entry and exit. Could an aid marketplace attract new promising entrants and close down poorly performing incumbents? Markets create competitive pressure to innovate. Could an aid marketplace force donors to innovate?

Unfortunately, there has not existed any “market square” where aid participants could meet. Whittle and Kuraishi are trying to change this both intellectually and physically. They have created a Web-based NGO, globalgiving.com, a sort of eBay approach to foreign aid. However, chapter 17 is about more than their own efforts. They suggest network theory as another market-type inspiration for foreign aid, where individuals in social networks spontaneously develop an emergent order without any top-down direction (the Internet being the current fashionable example).

How could this happen in foreign aid? This is clearly blue-sky territory where there has been little experimentation in foreign aid. But Whittle and Kuraishi suggest brainstorming based on precedents such as the American tradition of self-organizing community groups to meet local collective needs, the principle that decentralized choices outperform centralized decision making, the self-organization of cities (à la Jane Jacobs and Paul Krugman), and the agglomeration economies demonstrated by self-forming clusters like Silicon Valley.

To make this practical, an aid marketplace would have to face the problem of creating trust among participants. Decentralized monitoring, checking each participant’s identity and past history, and each participant’s concern for his or her reputation in a market where there are repeated transactions make these issues potentially tractable, although far from easy or straightforward to solve.

What other mechanisms could create markets in foreign aid? Easterly (2006, 2002, 2001) proposed the idea of “aid vouchers”:⁷⁶ “Another market-oriented step would be for the common pool [of aid money] 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.”⁷⁷ This idea was too poorly articulated, too crazy, or too threatening to the aid establishment to attract much support. Yet frustration with the existing bureaucratic, top-down, planner-dominated aid system is growing. UK Conservative leader David Cameron endorsed the idea of experimenting with vouchers in a speech on June 29, 2006: “One idea we will investigate, based on our belief in trusting people—and our instinctive dislike of top-down solutions—is aid vouchers. Aid vouchers, put directly in the hands of poor communities, would be redeemable for development services of any kind with an aid agency or supplier of their choice. The vouchers could be converted into cash by the aid agencies. For the first time, poor people themselves would be the masters, and aid agencies would have a direct and clear incentive to deliver effective services. Such an innovation would help show us what the poor really want—and who is most effective in meeting their needs.”⁷⁸

Chapter 18 by Hoffman is also very much informed by the examples of market mechanisms that reduce poverty. Hoffman wonders why so little aid actually goes to stimulate enterprise development, when private enterprise is well established as the means by which most people have historically escaped poverty. He points out that the aid system is “overwhelmingly focused on what local government, donors, or the other battalions of aid actors and NGOs need to do first to achieve the Millennium Development Goals. . . . ‘What to do about enterprise usually comes way down the list.’”

The second defect of the aid system, according to Hoffman, is its inability to think like a business. Business thinking would include risk assessment, knowing what the target “customer” wants, setting out precisely how the project is going to help meet those wants at lowest cost, and how many customers (in our case, pro-poor enterprises or poor people) are going to be measurably better off at the end of the project.

Hoffman suggests consequence accountability of donors to recipients similar to that which exists from a start-up firm to an investor, a corporate manager to shareholders, and businesses to customers. He calls for “business DNA” to make its way down the foreign aid supply chain, first with the donors themselves, and says that business DNA should be transferred to enterprises in

poor countries. Unfortunately, aid workers have little business experience and little business DNA to transfer. Oddly enough, even private corporations that have corporate social responsibility (CSR) departments operating in poor countries show little appreciation for the business principles that should be applied to aid. It is as if private corporations want to imitate aid agencies, while it should be the other way around.

An example of Hoffman's desired approach is a recent experiment to market cleaner indoor stoves to poor families in India. Smoky stoves are a leading source of indoor air pollution, which causes respiratory infections, leading to around 2 million deaths globally. The traditional approach was to design the perfect stove with little regard for costs or customer wants, only to see it rejected by the poor or fail to attain any significant scale. The recent experiment test-marketed stoves with the customers and kept costs down. The pilot successfully sold 65,000 stoves, and the objective now is to scale up dramatically.

Part VI of this book looks at the big picture in the aid system. Like Hoffman, McMillan in chapter 19 also uses the market as inspiration in his chapter. His concern is with the big-bang and shock therapy approach to economic reform often advocated by Jeffrey Sachs, the IMF, World Bank, and other aid agencies. He believes that comprehensive reform to all economic policies is just as misguided as trying to do all aid interventions at once: "Acknowledging our ignorance means moving step by step rather than betting everything on a comprehensive blueprint. . . . The whole point of the market economy, after all, is that it handles, better than any more centralized alternative, the unforeseen and the unforeseeable. If we could plan the reforms, we could have planned the economy."

McMillan contrasts piecemeal reform with utopian social engineering à la Popper. China is an example of the success of the first, Russia an example of the failure of the second. China achieved some easy gains by replacing collective farming with individual farming; it then moved to village enterprises, which competed with each other and could expand the scale of success using their powers of taxation. The reform process has since moved on, and village enterprises are no longer a good model for the next phase of growth in China, not to mention for other countries with very different circumstances. To McMillan, there is no room in policy reform for aid experts who apply universal blueprints; policy reform in each country should be intentionally experimental (searching rather than planning again). His most important advice to would-be aid experts on reforming other countries' policies is, "Avoid hubris."

Birdsall in chapter 20 analyzes the "sins" of the donors, some of them related to the emphasis on observable aid spending. Another version of the pressure to

spend is the reluctance to stop spending even when conditions become supremely unpromising: donors exit far less than they should. Pressure to spend the budget also leads to overemphasis on short-run outputs (or, worse, short-run inputs) and scandalously little emphasis on long-run results.

Even when the donors find something that has a long-run dimension, like the MDGs for 2015, these seem designed more for short-term publicity than for rewarding good long-run performance. For example, Burkina Faso is projected to raise net primary enrollment from its current level of 35 percent to 59 percent by 2015. The UNDP describes this projected performance as “off-track” to meet the MDG of universal primary enrollment by 2015, even though Burkina Faso’s performance would far outpace the historical performance of the United States over the same range.

A related sin that comes from aid agencies’ desire to “be seen” is the proliferation of projects, countries, and sectors within each aid agency’s portfolio, presumably because each additional project, country, and sector in which an aid agency is involved attracts additional observers. The consequence is the thicket of huge numbers of donors and projects with which even the smallest country must cope. One solution that Birdsall advocates is to pool donor funds at the country level, but this proposal has met stiff political resistance.

Another sin of the donors is the obfuscation that has surrounded the issue of ownership of development policies. Birdsall notes that “the misguided imposition of policy conditions morphed into the misguided imposition of participation. The prevailing approach to participation, as demanded by donors, has been narrow and apolitical. In practical terms, it has relied mostly on engagement of civil society groups in discussions of proposed government programs (including the PRSPs . . .) Members of minority groups and the truly poor are often excluded from apparently open discussions, reflecting the reality that participatory efforts alone are unlikely to alter the prevailing distribution of power and influence.”

Donors’ desire to show individual observable efforts has also led them to overemphasize countries as the receiving unit and to underemphasize global public goods, such as research on tropical agriculture and diseases.

The greatest sin of the donors emphasized by Birdsall is as easy to state and to solve as it is difficult to overcome the political resistance: the almost complete lack of independent evaluations of aid (as noted also in chapter 2 by Banerjee and He and chapter 3 by Duflo and Kremer), so that donors are both ignorant of their impact and unaccountable for that impact. Groups on the left, right, and center have called for an independent entity to do aid evaluation, Birdsall notes, and this could be easily funded by a small proportional contribution from each donor.

1.3 Conclusion

“Avoiding hubris” and “independent evaluation” is a fitting way to end this introduction. Focusing on specific feasible tasks and holding the aid actors responsible for whether they achieve them is a no-brainer, except for the absence of these simple principles in today’s foreign aid system. The talented explorers of the aid domain in this book offer much good sense and much hope for the future, even if they do not strive for the headline-grabbing and utopian promises of making poverty history anytime soon. To the extent that outsiders can assist the poor in their search for prosperity, the chapters in this book offer a promising set of ways to go forward.

Notes

1. *Human Development Report 2005: International Cooperation at a Crossroads: Aid, Trade and Security in an Unequal World* (New York: United Nations Development Program, 2005), p. 7.
2. United Nations Millennium Project, *Investing in Development: A Practical Plan to Achieve the Millennium Development Goals* (New York: United Nations, 2005), p. 4.
3. *Ibid.*, p. 193.
4. Department for International Development, *Eliminating World Poverty: Making Governance Work for the Poor* (London: Department for International Development, 2006), p. 13.
5. World Bank and International Monetary Fund, *Global Monitoring Report 2006: Millennium Development Goals: Strengthening Mutual Accountability, Aid, Trade, and Governance* (Washington, D.C.: World Bank and International Monetary Fund, 2006), p. xvii.
6. *Ibid.*
7. Some NGOs such as Oxfam have pointed out that the 2005 number was inflated by large-scale debt relief, which counts as aid. They argue that debt relief is not true aid, for example, because it writes off debt that is not being serviced anyway and should not be included. This is a paradoxical position, as the same NGOs (such as Oxfam) campaigned for debt relief under the argument that debt was strangling poor countries, so it is not clear why debt relief should not be counted as a boon to poor countries.
8. Human Development Report 2005. *Crossroads*, p. 1.
9. Jeffrey Sachs, *The End of Poverty: Economic Possibilities for Our Time* (New York: Penguin USA, 2005), 352.
10. Department for International Development, *Eliminating World Poverty*, p. iii.
11. <http://www.makepovertyhistory.org/>.
12. V. I. Lenin, *What Is to Be Done? Burning Questions of Our Movement* (New York: International Publishers, 1943), p. 80.
13. Sachs, *End of Poverty*, 2, 289.
14. Department for International Development, *Eliminating World Poverty*, 18–19.
15. United Nations Millennium Project, *Investing in Development*, 2.
16. Lenin, *What Has to be Done?*, p. 76.
17. Department for International Development, *Eliminating World Poverty*, 19.
18. William Duggan of Columbia University suggested the Aid Wall comparison to the Berlin Wall to me in private conversation. The chapter 17 by Whittle and Kuraishi in this book also inspired the central planning metaphor.

19. UN Millennium Project, *Investing in Development*, 2.
20. Sachs, *End of Poverty*, 2–3.
21. *Ibid.*, 273.
22. <http://www.un.org/millenniumgoals/>. July 6, 2005.
23. UN General Assembly, 55th Session. *UN Millennium Declaration (A/RES/55/2)*. September 8, 2000.
24. Jeni Klugman, ed., *Poverty Reduction Strategy Paper Sourcebook* (Washington, D.C.: World Bank, 2002).
25. *Ibid.*
26. <http://www.mfdr.org/Sourcebook/1stEdition/MfDRSourcebook-Feb-16-2006.pdf>. Organization for Economic Cooperation and Development and World Bank, *Managing for Development Results Principles in Action: Sourcebook on Emerging Good Practice*. p. 4. February 16, 2006.
27. Luc Christiaensen, Christopher Scott, and Quentin Wodon, “Development Targets and Costs,” in Klugman, ed., *Poverty Reduction Strategy Paper Sourcebook*, 132.
28. *Ibid.*
29. http://igdleaders.org/policy/documents/IGDDDevelopmentGuide_000.pdf. Initiative for Global Development, *The IGD Development Guide: A Business Approach to Ending Extreme Global Poverty*, p. 7.
30. See Ruth Revine, *Millions Saved: Proven Successes in Global Health* (Washington: Center for Global Development, 2007), for a description of the successful vaccination campaigns.
31. Human Development Report 2005. *Crossroads*, 77.
32. UN Millennium Project, *Preparing National Strategies to Meet the Millennium Development Goals: A Handbook* (New York: United Nations, 2005), p. 130.
33. Shantayanan Devarajan et al., “Goals for Development: History, Prospects and Costs,” *World Bank Discussion Paper* No. 2819 (Washington, D.C.: World Bank, 2002).
34. The research they cite is Deon Filmer, “A Note on Public Spending and Health and Education Outcomes” (Washington, D.C.: World Bank, 1999) (processed), and Deon Filmer, Jeffrey S. Hammer, and Lant H. Pritchett, “Weak Links in the Chain: A Diagnosis of Health Policy in Poor Countries,” *World Bank Research Observer* 15(2000): 199–224.
35. Filmer, Hammer, and Pritchett, “Weak Links in the Chain,” pp. 199–224.
36. UN Millennium Project, *Investing in Development*; Sachs, *End of Poverty*; Jeffrey Sachs, *Macroeconomics and Health: Investing in Health for Economic Development* (Geneva: World Health Organization, 2001).
37. Shantayanan Devarajan, et al., “Goals for Development.”
38. UN Millennium Project, *Preparing National Strategies*, 45–46.
39. *Ibid.*, 48, 50.
40. This discussion and the citation of Kuhn is based on William Duggan, *The Art of What Works: How Success Really Happens* (New York: McGraw-Hill, 2003) 234.
41. F. A. Hayek, *The Road to Serfdom* (Chicago: University of Chicago Press, 1944), 181.
42. Karl Popper, *The Poverty of Historicism* (London: Routledge, 2002), p. 61.
43. William Easterly, *The White Man’s Burden: Why the West’s Efforts to Aid the Rest Have Done So Much Ill and So Little Good* (New York: Penguin Press, 2006).
44. <http://adamsmitheeblogs.com/blog/> (posted May 19, 2006).
45. This section is based on William Easterly, “Reliving the 50s: The Big Push, Poverty Traps, and Takeoffs in Economic Development,” *Journal of Development Economics* 11, 4 (December 2006): 289–318.
46. Sachs, *End of Poverty*, 56–57.

47. This involved some data construction, since the World Development Indicators (WDI) have complete data on aid for the bottom quintile (the few aid observations missing can usually be interpreted as representing zero aid) but not on GDP. I used the Maddison per capita gross domestic product (GDP) numbers and population numbers to impute GDP for missing observations in WDI. Since the Maddison numbers are purchasing power parity (PPP), I used GDP in nominal dollars and PPP for that country in the year for which both were available in WDI closest to the sample period to convert the imputed Maddison number from PPP to nominal dollars.
48. Aart Kraay and Claudio Raddatz, "Poverty Traps, Aid, and Growth," mimeo., World Bank, January 2005, and Bryan Graham and Jonathan Temple, "Rich Nations, Poor Nations: How Much Can Multiple Equilibria Explain?" mimeo., Harvard University, 2004.
49. Sachs, *End of Poverty*, 191.
50. UN Millennium Project Report, *Investing in Development: A Practical Plan to Achieve the Millennium Development Goals: Main Report*, 34.
51. Sachs, *End of Poverty*, 226.
52. <http://www.underreported.com/modules.php?op=modload&name=News&file=article&sid=1241>.
53. UN Millennium Project Report, *Millennium Development Goals Needs Assessment* (January 2005), 119.
54. Easterly, "Reliving the 50s."
55. *Ibid.*
56. Durlauf, Johnson, and Jonathan Temple, "Rich Nations, Poor Nations."
57. A thoughtful and entertaining discussion of this theme is in Virginia Postrel, *The Future and Its Enemies: The Growing Conflict over Creativity, Enterprise, and Progress* (New York: Touchstone, 1998). She stresses a dichotomy between stasis and dynamism that is related to the dichotomy here between planning and searching. Another great book on unpredictable success is Paul Ormerod, *Why Most Things Fail: Evolution, Extinction, and Economics* (New York: Pantheon Books, 2005).
58. <http://www.macnn.com/articles/06/04/20/apples.music.business/>.
59. Jim Collins, *Built to Last* (New York: Harper Collins Publishers, 1994), p. 153.
60. *Ibid.*, 141.
61. Malcolm Gladwell, "The Formula," *New Yorker*, 16 October 2006, 138.
62. U.S. Small Business Administration, Office for Advocacy, <http://www.sba.gov/advo/research/data.html>.
63. Lada A. Adamic, *Zipf, Power-laws, and Pareto—A Ranking Tutorial* (Palo Alto, Calif.: Information Dynamics Lab, HP Labs, 2004), is a helpful primer on power laws.
64. Paul Ormerod, *Why Most Things Fail: Evolution, Extinction, and Economics* (New York: Pantheon Books, 2005).
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71. <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTPOVERTY/EXTISPMA/0,,menuPK:384336~pagePK:149018~piPK:149093~theSitePK:384329,00.html>.
72. For one attempt to mobilize political change and for further analysis, see *Report of the Evaluation Gap Working Group, When Will We Ever Learn? Improving Lives through Impact Evaluation* (Washington, D.C.: Center for Global Development, May 2006). William D. Savedoff, Ruth Levine, Nancy Birdsall Co-Chairs.
73. Department for International Development, *Eliminating World Poverty*, 10, 21, 78.
74. For an extended treatment of this theme for general audiences, see Easterly, *White Man's Burden* (2006).
75. Nicolas Van de Walle, *African Economies and the Politics of Permanent Crisis* (Cambridge: Cambridge University Press, 1991), 58.
76. William Easterly, *The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics* (Cambridge: MIT Press, 2001); "The Cartel of Good Intentions: The Problem of Bureaucracy in Foreign Aid," *Foreign Policy* 131 (July–August 2002): 40–49; *White Man's Burden* (2006).
77. Easterly, "Cartel of Good Intentions," 48.
78. David Cameron, Speech at Oxford Town Hall, U.K. 29 June 2006.

