

THE ROLE OF **FOREIGN AID** IN THE DEVELOPMENT OF SUB-SAHARAN AFRICA



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Introduction

Foreign aid can be defined as “financial or technical help given by one country’s government to another country to assist social and economic development or to respond to a disaster” (Oxfam n.d.). This is often in the form of grants, loans and subsidies, but also includes technical advice, training and commodities (Wells 2015). Annually, Official Assistance gives \$134.38 billion in aid globally, with \$36 billion going to Sub-Saharan Africa (SSA)—the most of any region by around \$15 billion (OECD, 2015). Despite this, it is the poorest region in the world. Sub-Saharan African countries require aid to finance large investment projects needed for growth and development as borrowing on the open market is made difficult by poor sovereign credit ratings and they are not considered creditworthy.

This was highlighted in a ratings report of 17 Sub-Saharan African countries which found that 15 were considered unworthy of investment (Bhatia 2017)—classified by a rating lower than BAA from Moody’s Investors Service (Moody’s 2017). Similarly, borrowing on the open market is deterred due to African countries paying more to borrow through sovereign bonds. African governments in general pay a premium in borrowing costs of approximately 2.9% which suggests a penalty on the governments or investor bias (Olabisi 2015). This penalty represents a total present value of \$2.2 billion which is unaffordable to some of the poorest countries in the world (Olabisi 2015). Sub-Saharan African levels of development have been very slow since aid donations increased in the 1950s. Therefore, this paper will look at why this is the case taking into account aid and development theories, the consequences of aid such as corruption and dependence and how we can begin to overcome these issues to use aid effectively.

Background and Theories

One of the most commonly referred to contributions to a poverty trap is a savings gap which arises when high levels of poverty make it almost impossible to generate sufficient savings to provide the funds needed to fund investment projects (Abuzeid 2009). Foreign aid has conventionally been viewed as a means for overcoming this gap. Sachs explores the role of aid in stimulating economic development through the Big Push theory in his book “The End of Poverty”.

It’s argued that foreign aid can make up for the lack of capital in poor countries because “if the foreign assistance is substantial enough, and lasts long enough, the capital stock rises sufficiently to lift households above subsistence” (Sachs 2006).

He states that donors must give the entire sum of aid needed to begin to reverse the poverty trap, allowing the public sector to invest in human capital, business capital, infrastructure, natural capital, public institutional capital, and knowledge capital (Sachs 2006).

It’s believed that once public institutions invest in capital and provide public goods, the country can begin developing from the “take-off” stage of Rostow’s Modernisation theory. Then the country will be able to reach the stages of “drive to maturity” and eventually “the age of mass consumption” (Rostow 1960), representing the “highest” level of development.

However, there are often unintended consequences. An example of this is Dependency Theory popularised by Raul Prebisch which states that resources flow from a “periphery” of poorer, developing countries to wealthier, developed “core” countries that reinforces the capitalist, unequal world system (Amin 1976). Within this, the

richer core sends flows of foreign aid, which increases debt and incurs political instabilities, and high-value manufactured goods to the developing world which they rely upon to maintain standards of living and avoid economic crisis. Conversely, flows like debt repayments, low value goods and highly skilled labour flow from the periphery countries to the core. The result is the “development of underdevelopment” within these poorer countries as they become highly indebted and reliant which leads to a loss of economic autonomy as well as brain-drain, thus leading to a decline in productivity and employment (Frank 1966).

Consequences of Foreign Aid

Increased Corruption

The negative effects on growth can be allied to the tendency of substantial aid to deteriorate the quality of governing institutions. The most severe consequence is that of corruption in Sub-Saharan Africa. Indeed, development aid can potentially encourage misallocation of resource and in some cases embezzlement in part because money is “cheap” (concessional terms) and accessible to less productive governments, as suggested by F. Hayek. Hall and Jones (1999) highlight “the institutions and policies that determine the economic environment within which individuals accumulate skills, and firms accumulate capital and produce output” as the most important factor when aiming for better economic performance.

A predictable and impartial application of the rule of law is also argued by Keefer and Knack (1997) to be vital for developing countries, emphasising the significance of stable, trustworthy governance in the development of poorer countries. Sadly, huge debt service paid by most of the countries in SSA on foreign aid (loans) and corruption are crowding out priority spending on education, health, infrastructure development and on making sure the justice system is well funded and independent.

A recent demonstration of this principle can be observed through the “opaque pay practices and poor management” within the Democratic Republic of Congo (2020 CPI of 18/100 and ranked 170/180 countries) which has led to \$257 million of Covid funding being unaccounted for publicly (BBC 2021). Of the 10 most corrupt countries in the world, 6 are in Sub-Saharan Africa (Transparency International) and corruption is estimated to cost the African continent around \$148 billion annually (United Nation Economic Commission for Africa, Hanson 2009).

Case Study: Corruption in South Sudan

Globally, South Sudan is the second most corrupt and the twelfth poorest country in terms of GDP (Transparency International 2018). Post-2005, the nation’s political state became a kleptocracy, dominating every sector of their economy with over \$4 billion of government funds having been stolen since (Pinaud 2014) due to types of corruption such as patronage and embezzlement. Similarly, the military controls the national budget and strongly influences government spending, often directing foreign aid funds to military purposes, thus resulting in South Sudan having a higher budget for military spending of all African countries (Anti-Corruption Resource Centre).

In 2008, the Dura Saga scandal involved the government supposedly spending \$1 million of aid on importing food, to avoid a nation-wide famine, which never arrived. Instead, the funds were paid to fake companies with

very close government ties (Rwakaringi 2013). Although this was the most well-known case, there are numerous accounts in which government funds, including aid donations, have been used for private gain instead of for development. For example, between 2006 and 2012, the South Sudanese Ministry of Roads and Bridges overspent its budget by 1513% with \$1.7 billion supposedly being spent on roads alone despite only 74km of roads being constructed in this time. Instead, the money had been transferred into the accounts of former Governors and close friends of the President (Nguen 2013).

Although the funds are with the intention of investment in public services, reality is different. Aid does not combat the initial underlying issues that are stifling the development. Hence, it can be considered a hindrance on development as in the hands of corrupt leaders, the elite are becoming wealthier whilst making an already vulnerable population even more at risk.

Aid Dependence

Secondly, aid can lead to over-reliance which can delay vital policy reform needed for development.

“Aid dependence is a situation in which a country cannot perform many of the core functions of government, such as operations or the delivery of basic public services, without foreign aid funding” (Deborah Brautigam 2000).

Reliance can also be linked to the “rentier state” theory. In the context of aid and the state, the theory suggests that large foreign aid flows during institutional development cause distortions like dependence which has knock-on effects. It’s thought that aid provides an “easy” source of government revenue and reduces the necessity to form an effective government in terms of designed policies that encourage tax collection as an alternative source of funding as suggested above.

The lack of domestic revenue heightens dependence on foreign aid which results in the “rentier state” effect (Abuzeid 2011). Evidence of reliance is shown as taxation revenues on average constitute 12% of GDP across 42 Sub-Saharan African countries whereas the government’s consumption expenditure averaged at 15%, proving that aid and borrowing are vital (World Bank 2013). Uganda and Burundi experienced an increase in tax collection during periods of reduced donor support.

During the 1996-1999 embargo in Burundi, total tax revenues increased from \$116 million in 1996 to \$167 million by 1998. Uganda also experienced an increase in domestic revenue during its 5-year ‘bush war’ from 1981-1986, with domestic revenue reaching an 11-year high at 12.2% of GDP in 1983 (Bhushan and Samy 2012). In this time, aid was at an all-time-low representing only 0.6% of total government income. This shows that when aid is scarce, governments may feel pressured to design efficient policies which are beneficial for the economy, thus stimulating growth and development.

Counter-Productive Aid Programmes

The last severe, negative consequence of foreign aid stems from the nature of Structural Adjustment Programmes (SAPs). Since 1980, SAPs have been implemented in numerous Sub-Saharan African countries, often involving austerity measures, privatisation and shifts towards freer trade (Bello and Cunningham 1994). These policies are with the intention of stimulating export-led growth and investment which will lead to economic growth and a reduction in debt and poverty (Naiman and Watkins 1999).

However, growth has fallen by 15% whilst external debt has increased by 500% and poverty has increased by 75% (Ismi 2004). For example, a SAP for Zimbabwe in 1990 required a reduction in government spending by 46% which led to the per capita budget for healthcare halving in 6 years. Likewise, fees for healthcare services significantly increased, “in some cases exceeding 1000%” (Naiman and Watkins 1999). The consequences of this included doubling the number of women in Harare hospitals dying of childbirth in 1993 compared to before 1990 and life expectancy falling from 61 to 48 years old. In the Ivory Coast, a SAP doubled the prevalence of poverty with 36.8% of its population living on less than \$1 a day (Ismi 2004).

Child slavery erupted, with 90% of cocoa farms employing children as young as 7 years old, working 20 hours a day for 7 days a week, some of whom were unpaid (Muindi 2001). As well as health and poverty, education also suffered under the introduction of SAPs in Sub-Saharan Africa.

In Ghana, cuts in public spending meant fees for education increased so significantly that the dropout rate for primary education rose to 40% and only 1 in 400 Ghanaians would enrol in post-secondary education (Kampfner 2001). In these countries, austerity measures will result in a downward spiral of economic decline and higher levels of poverty because of less spending on basic goods and necessities. Programmes should be focusing on the provision of public services rather than public debt, as in the long run this will prove more sustainable in terms of both living standards and debt.

Reducing Dependency and Corruption

Kofi Annan and Jeffrey Sachs suggested that developed countries should cancel or relieve the debts of Sub-Saharan Africa and failing that Africa should refuse to pay to reduce dependence (Easterly 2009). This has also been the view of previous African economists, politicians and presidents such as Ibrahim Lipumba and Thomas Sankara. Snider (1990) suggests that lower levels of public debt will also reduce the likelihood of political unrest from occurring, especially in the form of demonstrations, strikes and riots as unsustainable debt levels may reduce political capacity and public investment.

In 1996, the World Bank and the IMF launched the Heavily Indebted Poor Countries Initiative and the Multilateral Debt Relief Initiative in 2005 to reduce external debt to a manageable level. Around \$95 billion of debt has been cancelled since 1996, most of which was in Sub-Saharan Africa to allow funds to be used directly for investment and development (Eichengreen and Hausmann 2003)—Tanzania and Zambia show the positive impact that debt relief can have on a country’s development. Tanzania used the extra funds to invest in education, abolishing school fees in 2002 which boosted primary school enrolment from 49% to 98% from 1999-2008. Zambia used it to invest in free healthcare, providing free antiretroviral drugs to 100,000 people in 2005 alone to control HIV/AIDS and allow a more productive future workforce (Nkombo 2014).

However, anti-relief advocates argue that debt relief encourages moral hazard on an international level. It’s believed that “financial recklessness” would be encouraged in borrower countries as they would take excessive amounts of loans with the expectation that they will be written off or forgiven if expectations fail (BBC News, 2005). It may encourage counterproductive and wasteful spending which we have already explored as being a crucial contributor to Sub-Saharan Africa’s underdevelopment. The IMF has also argued against relief, suggesting that it could harm poorer countries in the future (IMF 2001). This is based on the logic that poor countries with written-off debt may be considered unreliable and not worthy of credit. The confidence of investors may be compromised as they may wish to invest their funds into “safer” nations where relief is impossible, knowing their returns will be paid (Aniago 2006).

However, regardless of the issue of debt relief, corruption still remains a significant concern. Cycles of corruption are very difficult to break and defining a “cleaner” government is incredibly difficult. Easterly argues that if a current highly corrupt government is still less harmful than a previous one, does this mean it’s more worthy of debt-relief? It can also be argued that high debt does not necessarily equate to poverty as it is not the individuals of the population that are indebted but their governments (Easterly 2009). This again falls within the transparency and actions of the government to direct funds to sound economic policies. Indeed, debt destination matters. Lastly, the burden of debt may actually encourage governments to reform. Eventually, the debt will be unsustainable which could force the government to seek to diversify the economy to generate higher revenues through increased economic activity (BBC News 2005).

Donors have also tried to give aid only to be spent on certain programmes which involves working with the recipient country’s national economic planning agencies and reducing the misallocation of resources. This way governments are forced to identify areas that need development, how they will use the aid and make the projects sustainable whilst donors only give the proven amount of funds required. This has been applied in Botswana. Botswana has used aid to move from a low to a middle-income country, having received around \$244 million in aid since 2005, making up approximately 60% of government expenditure (OECD 2011).

Botswana identified the areas of fiscal saving, a currency account surplus and heavy government investment in infrastructure and human capital to be of paramount importance for its own development. Public saving took place through the Public Service Debt Management Fund and the Revenue Stabilization Fund which progressed into successful mechanisms for macroeconomic management as well as generating income to be used as government revenue. As a result, public sector saving was positive for 25 consecutive years, consisting of 10-40% of GDP between 1975 and 2000 (Isham and Kaufmann 1999). The government of Botswana used aid to dedicate around 20% of the capital budget on education and 30% on infrastructure with a focus on water, electricity, roads and transport with a further 30% devoted to spending on maintenance over time. As a result of a stable, transparent government and effective use of aid, the number of paved roads increased from around 20km to 2300km in 20 years and in 1990, 90% of the population had access to clean, safe water compared to 29% in 1970 (World Bank 2009).

It must be noted that despite the above figures, researchers such as Branco (2008) and Nilsson (2014) have found that Botswana is not as developed as it is portrayed, suggesting that aid has not been as effective. The evidence includes the unemployment rate and income inequality (measured by the Gini coefficient) which are higher in Botswana than the average for Sub-Saharan Africa with 18% and 0.63 respectively (Nilsson 2014). It seems that the conflation in results stems from the indicators used in the measuring process. Whereas organisations may have placed greater emphasis on human development factors such as health and education progression, Branco and Nilsson have focused on macroeconomic performances. Both are of equal importance when considering the effects of aid and development and should not be considered in isolation.

Conclusion

There has been a largely negative relationship between foreign aid and development levels in Sub-Saharan Africa since the 1950s. For Sub-Saharan Africa, the Big Push theory of using foreign aid funds to fill savings gaps and provide capital has not proved to be successful in part because of a lack of government integrity and judicial effectiveness. Therefore, it seems that in the case of Sub-Saharan Africa, Prebisch's Dependency Theory may represent a more accurate depiction of reality with richer, donor countries keeping developing countries poorer by making them reliant on aid, spurring political instabilities and heightening debt repayments.

As suggested above, corruption and dependence, in particular, have led to GDP decreasing with aid, negatively impacting both human and physical capital development. Corruption is rife in Sub-Saharan Africa's public sector, diverting aid resources away from investment projects to increase military spending, the wealth of the elite and those with close ties to the government. Meanwhile, foreign aid has also been found to delay policy reform and distort incentives to introduce public policies like tax collection for government revenue like in Uganda and Burundi. Similarly, the free-market approach of SAPs proved crucial for the region's underdevelopment as austerity measures meant that investment in health, education and infrastructure suffered drastically, with Zimbabwe, Ghana and Ivory Coast's population suffering from higher levels of poverty as a result.

Despite significant debate around the effectiveness of debt relief, the conclusion is that this could promote moral hazard, encourage reckless spending and reduce the credibility of their credit rating for future loans. Lastly, we can reduce corruption by helping to make aid more efficient if aid is programme-specific. Once areas for improvement are identified and plans for development are produced, donors can match what is needed to develop certain areas of the economy like in Botswana whilst encouraging national planning and holding governments accountable (for example the civil society can be added as permanent member in the committee in charge of monitoring and evaluation of these specific programme's budget).

In the future, donors need to approach development policies in a less of a "one-fits-all" type of manner and stop applying austerity-based, Westernised perspectives to all developing countries. Austerity where investment is already poor will only make vulnerable populations worse off, even if it reduces their debt in the short run. Aid should be less donor-driven and less fragmented. This is not sufficient to build sustainable projects which result in more aid being needed in the future, thus contributing to ineffective economic planning and reliance. Instead, aid needs to be compatible and aligned with development priorities specific to the country. Based on the literature, more emphasis should be placed on improving the quality of institutions, particularly in countries with corrupt leaders, to strengthen national development strategies and central planning.

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