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## What Donors Mean by Good Governance

### Heroic Ends, Limited Means, and Traditional Dilemmas of Development Co-operation

Why are the ambitions of economic development and reform so often disappointed, especially in low-income countries? One answer is that conventional reform strategies are seriously deficient. Another answer is that good plans are regularly defeated by those who occupy strategic positions in the implementation process. According to institutional economics, both answers may contain important grains of truth [Williamson, 1994].

While institutions are widely held to be critically important, institutional issues have frequently been neglected in the process of development and the design of policy reform. At an earlier stage of development economics, a macroeconomic planning approach was favoured, which Deepak Lal [1983] referred to as the "dirigiste dogma". This prescription called for governments to chart and implement a strategy for rapid and equitable growth. Prime importance was attached to macroeconomic accounting aggregates such as savings, the balance of payments, and the relative balance between broadly defined sectors such as industry and agriculture. In most instances, the planning approach failed to achieve its stated objectives.

As a result, the pendulum swung in the opposite direction [Williamson, 1994, p.3]. Many concluded that the most important advice that economists can offer is that of the so-called "price mechanist" [Lal, 1983, p.107]. "Get the prices right" became the principal message, according to which tariffs, quotas, subsidies, etc. had to be eliminated, and, more generally, market forces should be relied upon. Some notoriously conservative economists, including myself, maintain that this message is still highly relevant. Admittedly, however, more than undistorted prices is needed for markets to work efficiently.

It is here where institutional economics and the issue of good governance come in. A general consensus on the importance of good governance is easy to achieve, but, typically, its exact meaning and the role of external donors in this area are not precisely defined. The discussion centres around a rather confusing variety of catchwords: property rights, institutions, participatory development, rule of law, administrative capacity

building, and investment in human capital are only a few among them. For example, the World Bank [1994a, p.2] concludes from a recent assessment of economic adjustment programs in Sub-Saharan Africa: "Adjustment alone will not put countries on a sustained, poverty-reducing growth path. That is the challenge of long-term development, which requires better economic policies and more investment in human capital, infrastructure, and institution-building, along with better governance".

It is clearly beyond the scope of this short paper to clarify the confusion prevailing in the discussion on good governance. In what follows the focus is on donor perspectives. Section II summarizes and critically discusses one of the potentially influential documents, i.e. the recent OECD publication on orientations of the Development Assistance Committee (DAC) on participatory development and good governance [OECD, 1994].<sup>1</sup> These orientations were endorsed by the DAC at its High Level Meeting in December 1993 and may indicate the donors' future stance in development co-operation. Subsequently, we will argue that only limited means are available to achieve the impressive - though not always consistent - list of heroic ends (Section III). What is feasible largely resembles earlier suggestions for reforming traditional aid policies. In Section IV, it will be discussed whether a bottom-up approach with respect to participatory development offers a promising alternative to the top-down approach applied by public international aid agencies. Section V concludes that changing donor perspectives will have little impact unless aid recipients are ready to tackle the fundamental bottlenecks hampering economic and social development in their own realm.

### 1. Heroic Donor Perspectives

The OECD document on participation and governance [OECD, 1994] presents a most impressive agenda for achieving sustained economic and social development in Third World economies. It addresses a fairly wide range of issues and identifies a number of close to 100 policy measures, part of which are broadly defined while others are highly specific. The document covers five topics and, thereby, applies a most comprehensive definition of socio-political conditions for development. The topics are:

- (i) participatory development,
- (ii) democratization,
- (iii) good governance including the rule of law, public sector management, controlling corruption and reducing military expenditure,
- (iv) human rights, and
- (v) coherence and co-ordination of donor policies.

Participatory development or popular participation is defined as a process by which people take an active and influential hand in shaping decisions that affect their lives. Empowering groups, communities, and organisations to negotiate with political institutions and bureaucracies is considered essential for influencing public policy, providing a check on government discretion, as well as enhancing the effectiveness and sustainability of development programs. The request for popular participation ranges from the grassroots level to the political life of the country. Participatory development is linked to equity goals of external aid policies. Priority is attached to programs providing effective services for education, training, and health for the population, with equal access for women. Practically, donors are requested:

- to support grassroots organisations and intermediary organizations such as professional associations, consumer groups, and trade unions,
- to involve all project stakeholders in program design and implementation, and
- to provide support for decentralization programs.

Most development economists will probably agree that human resource development is a precondition for popular participation. They have argued for years that external aid should be focused on basic education, training and health services. However, the aforementioned areas for DAC action involve several problems which cannot simply be ignored. For example, the experience of NGOs suggests that popular participation in aid programs is frequently resisted by Third World governments as it may undermine the power base of the ruling elites. So far it is completely open to question whether and in which way donor governments can overcome the widespread resistance to participatory development. Furthermore, it appears to be somewhat naive to assume that more participation and decentralization will automatically result in greater efficiency of aid projects. Exactly the opposite may happen if the conflicting demands of various groups and institutions have to be identified and co-ordinated in a time-consuming negotiation process.

The second topic, i.e. democratization, "integrates participation into the political life of the country" [OECD, 1994, p.12]. Democratic principles revolve around the keywords consent, legitimacy of the government and accountability to the people. Periodic free and fair elections are considered to be an essential feature of functioning democracies. Democratization requires "the development of a pluralist civil society comprised of a range of institutions and associations which represent diverse interests and provide a counterweight to government" [ibid]. Hence, the OECD

document calls for donors supporting pluralism and better access to information, as well as helping improve the functioning of representative political institutions, electoral processes and consultative mechanisms.

Donors consider democratisation to be of intrinsic value. In addition, they are tempted to sell the idea that political and economic progress are closely associated. The empirical foundations of this reasoning are weak, however.<sup>2</sup> The ambiguities are particularly pronounced when it comes to the question of causation. Sometimes, e.g. in the case of China, it is argued that the public demand for democratization will rise only after economic progress has been achieved. If so, economic development would be a major determinant of political liberalization. The available evidence at least provides little justification to assume causation running from democratization to better economic performance. The best performers among the developing countries are located in Southeast Asia, and most governments in this region have little reputation with respect to early moves towards Western style democracy.

By contrast, many Asian governments stand out in terms of their determination "to use ... political authority and exercise ... control in a society in relation to the management of its resources for social and economic development" [OECD, 1994, p.14], which appears to be a widely used definition of good governance. This implies that DAC orientations on participation and democratization on the one hand, and governance on the other hand may involve serious conflicts and trade-offs.

A closer look at the elements that the DAC considers to be part of good governance reveals that even the best performers in Asia would not pass the test. This is primarily because controlling corruption is one of the dimensions of good governance according to the OECD document. Another one concerns the request for reducing military expenditure if it is "excessive" so that development needs are sacrificed. Not surprisingly, however, donor perceptions are rather vague on how to improve governance in these respects. The problem of corruption shall be tackled by exposing corrupt practices, e.g. in the media, and reducing the opportunities for corruption, e.g. through greater reliance on transparent and competitive bidding processes in public procurement and on auctions in foreign exchange allocation. The difficulties in reducing military expenditure start with defining what is excessive in a particular case. Moreover, if donors cease to provide aid which may have helped sustaining excessive military spending, it is open to question whether the military or the population will be the first to suffer from such a move. Most importantly, Western aid administrations face tremendous credibility problems in campaigning against military spending as long as other government departments in donor countries

are deeply involved in promoting arms exports to developing countries [Moore and Robinson, 1994, p.148].

More concrete suggestions are made with respect to the two remaining dimensions of good governance, i.e. the rule of law and efficient public sector management. It is beyond serious doubt that inefficiencies in the legal system increase business costs, discourage investors and obstruct economic development. Such inefficiencies include the lack of predictability in the legal environment, the lack of an independent court system, delays in handling legal conflicts and insufficient enforcement of court decisions. A wide range of technical assistance by external donors may help to strengthen the rule of law. Donor support may relate to the dissemination of legal information, "legal literacy" programs, the design of appropriate and enforceable legal provisions for property rights, trade and investment, as well as training the legal staff.

Public sector reform is frequently required for two related reasons. On the one hand, many governments are tempted to extend their activities far beyond their role in providing public goods. Streamlining and reducing the size of public sector institutions is particularly important where "government market intervention ... (is) bordering on state economic management" [Hiemenz, 1989, p.6]. On the other hand, overcharged governments typically fail to fulfil their key tasks, among which the establishment of a predictable, coherent and transparent framework of basic rules and regulations guiding private economic activities figures prominently. But differently, good governance calls for strong, though small governments. For example, governments must be strong enough to resist well organized pressure groups. Obviously, this may involve conflicts with greater participation in public decision making. While such internal inconsistencies are largely ignored in the OECD document, the DAC agenda offers detailed suggestions to strengthen the competence of governments and public administrations in formulating and implementing appropriate policies. The long list of areas for action comprises:

- improved accounting by training the relevant staff and modernizing accounting and auditing procedures;
- improved budgeting and expenditure management, e.g. through efficient information systems, effective tax and customs administration, and technical support granted to finance ministries and central banks;
- civil service reform, which requires reliable data on employees, ghost employees, and payrolls in the first place, and may then proceed to appropriate adjustment measures.

As concerns human rights, a substantial body of international laws and agreements such as the 1993 Vienna Declaration can be referred to. DAC members expect developing country governments "to share a common commitment to securing the human rights of all human beings, regardless of gender, ethnic identity, religion, race or socio-economic status" [OECD, 1994, p.22]. In contrast to aid recipients, the human rights definition of external donors focuses on civil and political liberties, rather than socio-economic rights [Moore and Robinson, 1994]. However, the DAC acknowledges that extreme poverty has to be reduced by co-ordinated efforts of both donors and recipients of aid, since poverty is frequently linked with violations of civil rights, e.g. the widespread discrimination against women.

The donors' inclination to consider the human rights situation in recipient countries when deciding on the allocation of aid has grown since the end of the Cold War, during which politically motivated compromises were all abroad. Nevertheless, the credibility of donor governments continues to be seriously deficient. The critical question is about the donors' reaction if the policy dialogue with aid recipients, which is the approach favoured by donor governments, fails in protecting and promoting human rights. First indications are that donors will not apply the same criteria across all recipients when a reduction or suspension of aid is called for due to persistent violations of human rights. The recent termination of sanctions against China suggests that human rights are sacrificed sooner or later once significant export interests of industrial countries are at stake. It can safely be assumed that tougher standards will be applied in dealing with countries with small and stagnant markets.

As is evident from the previous discussion, the DAC orientations on participation and governance necessitate coherence and co-ordination of donor policies. As a matter of fact, the OECD document addresses this issue in a short section. However, a list of specific areas for action is missing, which is in striking contrast to all other sections of the document. The DAC appeal to improve policy coherence within donor governments "by promoting horizontal approaches to the issues encompassed in participatory development and good governance in developing countries" [OECD, 1994, p.25] will probably have little impact as aid ministries and agencies typically rank low in the power structure of donor governments. Furthermore, co-ordination of donor policies at the DAC level will prove difficult. For example, the US approach towards democratization in developing countries, with its vigorous insistence on formal electoral processes, is significantly different from the European approach [for details, see Moore and Robinson, 1994, pp.147f.].

## 2. What Donors Can Actually Do: Limited Means and Traditional Dilemmas

So far we may conclude that DAC donors have presented an impressive list of topical issues related to greater participation and improved governance. There is little to quarrel about the desirability of these aims. However, the list involves various problems in terms of consistency, credibility, feasibility, and enforceability. Inconsistencies may arise from ambiguous relations between different issues addressed in the OECD document. Democratization does not necessarily lead to better economic performance. Likewise, greater participation by various interest groups in public decision making may compromise good governance, which requires small but strong governments. The credibility of donors suffers if different branches of their own governments have conflicting objectives (e.g., reduced military spending versus ongoing arms exports), and if recipient countries are treated differently, e.g. according to their market potential for Western exports.

Further problems arise when it comes to the question by which means to achieve the heroic ends and, specifically, what donors can do in this respect. The DAC guidelines refer to incentives and external support on the one hand, and sanctions and conditionality on the other hand:

"A deepened and strengthened policy dialogue with development partners is the most important vehicle for advancing ... (donor) concerns at the policy level" [OECD, 1994, p.9].

Operationally, the focus of external assistance is placed on local capacity building, i.e. helping partners to develop and harness their own expertise. Better education, especially of women, is - rightly - emphasized as a critical prerequisite to economic, social, and political progress.

While donors "wish to rely to the maximum extent on measures of positive support, ... they also wish to be clear about the potential for negative measures affecting the volume and form of their aid, in areas of serious and systematic violations of human rights and brutal reversals from democratization, or when a complete lack of good governance renders efficient and effective aid impossible" [ibid].

In other words, donors have to rely on traditional concepts and mechanisms of development co-operation in dealing with the demanding issues of participation and governance. We are back to the old and well-known dilemmas of external aid, among which the following figure prominently: First, aid of whatever form and dimension will not turn the tide unless the recipients themselves are determined to establish the institutions

and implement the policies required for successful economic and socio-political development. Second, conditionality imposed on aid recipients by external donors has typically failed to compensate for a lack of "ownership" of economic reform programs by developing countries. Letters of intent have frequently been signed only to get access to the money involved; dozens of programs have been abandoned after the transfers had been made. The same is likely to happen if conditionality is extended to institutional and political conditions. Third, donors have rarely been committed to effectively sanction the breach of contractual obligations by aid recipients. As mentioned before, the credibility of donors is particularly deficient in the case of developing countries with promising markets.

In effect, it is little what donors can do beyond supporting moves towards participatory development and attempts at better governance that are initiated from within the developing countries. This is what has been coined premium approach in the late 1980s already [Hiemenz, 1989]. This concept requires external assistance to be sufficiently strong and timely in order not to frustrate local reform efforts. The need for positive donor response has to be stressed as traditional aid policies have sometimes responded rather reluctantly to promising economic reform programs and, thereby, contributed to their failure.<sup>3</sup> Especially at times of stagnating overall aid volumes, the premium approach calls for greater flexibility in aid allocations among developing countries.

Also in terms of substance, the recent discussion on participation and governance largely boils down to attaching new labels to rather conventional suggestions for reforming aid policies. If we had to define a common denominator of what appears to be feasible among the DAC orientations, we might refer to the earlier request for software orientation of external aid [Hiemenz, 1989]. This means that aid programs should concentrate on institution building and human resource development, rather than hardware (such as physical infrastructure) not related to the fundamental bottlenecks of economic and social development in recipient countries.

Provided local governments are committed to reform, institution building may be supported by external donors in various respects:

- The transparency within societies and the access to information may be improved by promoting diversity of written and broadcasted opinion, increasing the flow of relevant economic information, as well as facilitating the establishment and articulation of producer and consumer interests.
- In order to define, protect and enforce property rights, external support may be needed, e.g. for cadastral

surveys, land-registration authorities and independent courts.

- External aid may help revising accounting systems which neglect public use aspects of the environment, especially with respect to public health conditions. In this way, donors can contribute to preventing an excessive exploitation of natural resources.
- Efficient financial intermediation may be encouraged if donors provide more technical assistance related to financial accounting systems, credit procedures, branch networks of financial institutions and stock exchange facilities.
- Likewise, external support may foster institutional development in the area of customs and tax administration.

As institution building has an intra-regional dimension, donors may encourage the co-operation among neighbouring countries with respect to institutional development. Institution building at the intra-regional level may comprise: improving communication networks, rationalizing energy investment, strengthening ecological co-operation, joint food security policies, and removing barriers to the movement of goods and factors of production [Hiemenz, 1989, pp.18f.].

As concerns human resource development, the empirical evidence on the returns to investment in education clearly reveals that the earlier focus of aid policies on higher education was mistaken [see e.g. Psacharopoulos, 1993]. Similarly, the frequently favoured establishment of sophisticated health care facilities was not suited to local needs. It is mainly basic health care, primary education and vocational training that have been shown to increase productivity. External aid could involve the development of adequate curricula, the training of teachers and the supply of teaching equipment, as well as the improvement of hygienical conditions. NGOs may play an important role in these respects. As far as higher education is concerned, emphasis should be put on the transfer of management and marketing know-how. Finally, external assistance may help to stop the brain drain in many developing countries by supporting improved local research facilities, e.g. in the area of technologies for processing of commodities.

### 3. A Bottom-up Approach towards Participatory Development: A Promising Alternative?

The NGOs' contribution to a stronger software orientation of aid policies may well spread beyond more conventional activities in education, training and health care. Some development economists have indeed pinned

their faith on NGOs in order to initiate participatory processes from the grassroots level and, thereby, "building new constituencies for state reform" [Borner, Brunetti and Weder, 1993, p.208]. Such a bottom-up approach is believed to provide a way out of some of the inherent flaws of the top-down approach applied by Western governments and international aid agencies, notably the World Bank.

The activities of official donors, as far as they relate to the agenda on participation and governance, have largely been confined to technical assistance and training programs for improving public administration and legal systems.<sup>4</sup> Evidently, such projects fall short of the comprehensive reform agenda outlined above. The reluctance, for example, of the World Bank to enter into politically more sensitive issues related to popular participation may at least partly be attributed to statutory limitations. Furthermore, the well-known problem of intruding into the sovereignty of developing countries is further complicated when conditionality is extended to socio-political reform requirements.

NGOs may be less constrained in terms of their legal mandate and political considerations. Hence, they may be better prepared to engage in the mobilization and organization of marginalised groups and to help establishing new instruments and channels through which these groups can strengthen their participation in the economic and political sphere. This is what Borner, Brunetti and Weder [1993] have called entitlement and empowerment of marginalized groups:

- The former aims at participation through better access to the formal economic system. Entitlement comprises: endowing marginalized groups with property rights, e.g. legal titles for land and houses; granting them access to credit; enabling them to appropriate the returns of their investment; offering them access to the legal system; and reducing bureaucratic hurdles in formalizing their business.
- The latter aims at improving participation in the political system. Empowerment may start with organizing neighbourhood groups in the informal sector. Intermediary institutions may then provide the link through which political articulation at the grassroots level affects public decision making at the local, provincial and state level.

The proponents of the bottom-up approach argue that the organization of popular pressure and participation from below is a necessary prerequisite for political change and economic progress. They are extremely sceptical about the political system's ability and willingness to truly reform itself. Under such conditions, the effectiveness of the top-down approach may suffer

indeed, as official donors have to work mainly through the governments of recipient countries.

However, it is not as easy to build new constituencies for state reform from below as the bottom-up approach seems to suggest. It would be rather naive to assume that NGOs can foster participatory developments at the grassroots level to any significant extent in developing countries whose governments are notoriously unwilling to reform the political and economic systems. If governments are not reform-minded, they will suppress participatory developments wherever they emerge as soon as such developments threaten to undermine the power base of the ruling elites. The experience of NGOs in various countries provides ample evidence to this effect. Hence, the bottom-up approach does not provide an alternative to top-down attempts at greater participation and better governance. Rather, both approaches may supplement each other in countries revealing at least a minimum of domestic reform-mindedness.

#### 4. Summary

The ongoing discussion on participatory development and good governance arose from growing concerns about the effectiveness of conventional development co-operation. Externally financed programs and projects often failed to deliver the expected results. Economic recommendations fell on institutionally barren ground, and their implementation suffered from internal bottlenecks in terms of governance. Donors have neglected the political economy of decision making in low-income countries, while overtaxing the existing texture of their societies.

Past failures have led to an emerging consensus that development co-operation should be concerned primarily with strengthening the political bargaining process within developing countries and institution building at all levels of society [Hiemenz, 1989, p.24]. It is expected that progress in terms of participation and governance improves the local capabilities in coherent, rational policy formulation and enforcement of economic policies which are necessary preconditions for a return to sustained economic growth and social development.

So far, however, there is still a lack of coherent strategies which may guide the donors' aid policies in the future. As shown above, the DAC agenda on participation and governance is subject to various ambiguities and inconsistencies. Furthermore, the impact of changing donor perspectives on economic and social progress in Third World economies hinges critically on the donors' credibility and the recipients' reform-mindedness.

In order to be credible, donor principles for granting or suspending aid must not be compromised once export

interests are at stake. Moreover, external assistance must be timely and sufficiently strong, in order not to frustrate promising local reform efforts. Donors should be aware that conditionality is highly unlikely to achieve better results than in the past, if it is extended to socio-political conditions. In the end, donors cannot turn the tide unless aid recipients are ready to tackle the fundamental bottlenecks hampering economic, social and political development in their own realm. However, the discussion on participation and governance may help the re-orientation of conventional aid policies towards what has been coined premium approach and software orientation in the late 1980s already.

#### Notes

- (1) For the World Bank's perceptions and experience, see World Bank [1992; 1994b].
- (2) See also Moore and Robinson [1994]. Haggard and Kaufman [1989, p.233] argue that democratic and authoritarian categories are too broad to be of analytic use. Specifically, there is "no systematic association between either democracy or dictatorship and the ability to stabilize".
- (3) For empirical evidence related to Africa, see Gulhati and Nallari [1988]; Moore and Robinson [1994, pp.151f.] argue along similar lines.
- (4) For details and practical examples, see World Bank [1992; 1994b] as well as Borner, Brunetti and Weder [1993].

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