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## Rethinking the world of aid in the twenty first century

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Working Paper No. 2011/67

## **Rethinking the World of Aid in the Twenty First Century**

Peter S. Heller\*

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### **Abstract**

Many concerns can be raised about the effectiveness of current aid programmes to developing countries. The appropriateness of aid is particularly questionable when one considers the likely character of the challenges that the global economy will confront in 2025, as suggested by alternative global scenario exercises. This paper argues for urgent reconsideration of the focus of aid by Development Assistance Committee (DAC) countries, extending from: the priorities that aid should be used for (with greater emphasis on global public good initiatives); the ways that DAC donors can contribute to these different policy objectives; and the roles that different aid actors should play.

Keywords: aid, global public goods, scenario analysis

JEL classification: F35, H41, O10, O19

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The amount of aid and other external resource flows needed to address these challenges in the poorer countries remains very significant indeed, while prospects for significant resource increases are dim, at least in the short term. We live in extraordinary times—we must recognize this in global policy-making and analysis (Addison et al. 2010: 19)

## 1 Introduction

This is the best and worst of times for foreign aid. After sinking to new lows in the 1990s, the supportive atmosphere for the effort to alleviate poverty gained new momentum by the close of the century. Bilateral DAC flows increased and multiple new initiatives were developed by other donors, including from new emerging market countries and private philanthropies. Ambitious targets were set in the form of the Millennium Development Goals (MDGs) and vertical policy approaches were mounted in the health sphere. New financial instruments were created to generate alternative sources of funds. Nevertheless, in the last few years, new doubts have arisen as to the effectiveness or impact of aid on growth. Despite much success in terms of the realization of the MDGs, aid's contribution to such success is unclear and certainly many of the targets will remain unachieved by 2015. The recession has reduced both the share of ODA in GDP for the industrial countries and the volume of assistance in dollar terms. Even the terms 'aid' and 'ODA' are acquiring new meaning. Severino and Ray (2009) underscore the multiple sources of flows that are being channeled to low-income countries (LICs) for various objectives and argue convincingly that an alternative term—that of 'global policy finance'—better characterizes these flows.

This paper seeks to refocus the debate on aid by exploring the world in which such resource flows will function looking forward 15 to 20 years. It will contrast the patterns that seem likely to characterize aid in this period with the challenges that will confront the world in 2025. It then asks whether the focus of aid efforts is on the right track. Recognizing the need for humanitarian assistance, to the extent that a significant component of resource transfers are meant to facilitate the achievement of *sustainable* poverty reduction and growth (as opposed to short-term improvement of the welfare of the poor), this would seem an appropriate perspective with which to view the aid debate. Over the long term, such an approach might even lead to a reduced need for humanitarian assistance.

The principal focus will be on bilateral aid flows, with a specific emphasis on those arising from the DAC. While a broader definition might be considered, the DAC at least constitutes a forum and a mechanism whereby DAC member countries might reach agreed policies. This does not ignore however that these policies will operate in a changing context where other resource flows are also being provided, both from non-DAC countries and private sources.

The paper is organized as follows. Section 2 will examine current trends in the source, shape, and magnitude of current flows of 'aid', broadly defined. Section 3 will briefly examine alternative scenarios that characterize possible shapes of the world of 2025 and beyond. These provide a context within which to view the role that aid will need to play in meeting global needs in the next two decades as well as the constraints and pressures that will shape the aid environment. Section 4 will raise normative questions, asking what *should* be the role of aid in the kind of world that might emerge by the first quarter of the twenty-first century and what this would imply for the design of aid policies in the immediate years ahead.

This paper draws on a number of earlier thoughtful papers on the role of aid, and in particular, on the strategies that should be considered in the post-2015 world. Thus, many of the arguments in this paper, particularly in terms of new policy directions, benefit from these earlier writers, and where appropriate, credit is so given.

## **2 The starting point: what does the world of aid look like in 2011?**

It is useful to briefly summarize the current world of aid—its magnitude, character, focus, quality, and essential modalities. One starts with the recognition that the prospects for increased aid flows have not kept pace with global leaders' earlier aspirations at the time of Gleneagles in 2005 (see Addison et al. 2010). The global recession has affected both GDP levels and the budgetary priority attached to aid by industrial countries, particularly now, at a time of fiscal deficits and high public debt. This reality has been further influenced by a weakening of public support for aid in private opinion polls in some countries (e.g., the UK, see Menocal 2011). Yet the need for aid by many LICs has only increased, reflecting the effects of the recession, the concurrent challenges that have arisen in food availability, and the recognition that resource flows will also be needed to help them adapt to climate change and participate in mitigation efforts. Perhaps the only two palliative elements have been the increased role of some emerging market and new industrial countries (notably, China, India, Brazil and Korea) as independent providers of aid and the rise in philanthropic aid.

Also worth emphasizing is that ODA has always been a rather complex and imperfect policy instrument, provided for many different reasons that extend beyond the simple goal of assisting LICs to ultimately converge to the per capita income levels of industrial countries. Security concerns, political and geopolitical relations, the fostering of relations with past colonial or client states, the response to humanitarian crises, the promotion of exporter interests, and more recently the moral imperatives underlying the MDGs—all these contribute to explaining what one now sees in the direction and focus of aid.

Severino and Ray (2010) have highlighted the dramatic evolution of the world of aid over the last decade. Their insights are useful in considering how the world of aid might develop over the next decade. They point to three important developments:

1. an increased diversity in the goals to which resource transfers—public and private—are focused;
2. an expansion in the number of actors involved in the provision of resources for these more diverse goals; and
3. the use of increasingly varied financial instruments to provide these resources.

Specifically, as to broadened goals, they emphasize that beyond the objective of income convergence, aid now provides the financing of 'access to [people-centered] essential services' and for the 'protecting [of] global public goods'. The latter includes 'conflict prevention and management', and 'global collective action' (SARS, bird flu, global food security). They stress that 'international development assistance has *de facto* been assigned a new "grand purpose": managing global interdependence in a globalized world'; efforts that no one would have imagined 20 years ago.

One consequence of the increased financing of social service provision has been to elevate the challenge of ensuring that these services are *sustainably* provided. For example, with regard to the provision of resources for antiretroviral treatment of HIV/AIDS, Over (2010) has emphasized the ‘entitlement’ character of this form of aid. Essentially, a significant share of future aid resources is effectively committed to the continued provision of these therapeutic services. Unlike traditional aid that sought to finance the provision of physical capital assets for LICs, social service provision is at best a blend of consumption and human capital investment that will continually challenge governments—both donor and recipient—in finding the necessary financial resources. Moreover, while importantly enhancing welfare in the short term, such services do not solve (and indeed may engender) long-term challenges in terms of creating employment opportunities and providing for the future population growth that will be generated, given high prevailing fertility rates.<sup>1</sup>

Severino and Ray (ibid.) further underscore the explosion in the number and diversity of players in the world of aid that, in their words, ‘generates a governance conundrum for this eminently fragmented global policy’. These encompass a broad range of NGOs (many in part financed by bilateral aid agencies); vertical funds primarily focused on specific policy issues and providing direct project assistance (e.g., GAVI, the Global Fund); and non-DAC donors from emerging market countries that are unconstrained by DAC priorities in the way in which aid is to be provided. While the bulk of aid, in financial terms, is still provided by traditional bilateral and multilateral donors, the new diversity of players at least implies an important hiving-off of aid players on specific issues.

This latter trend may have merits to the extent that specialization by vertical funds provides greater efficiency and direction on specific policy issues than would arise from the world of the generalists who inhabit most bilateral and multilateral aid agencies. But these vertical funds also raise important policy questions, both as to which aid agencies ‘own’ policy leadership on specific issues, and whether such segmentation creates co-ordination challenges, both for recipient countries and for the realization of aid effectiveness, given that few issues can be dealt with independently from other sectors or issues. Climate change is a good example of this.

Severino and Ray (ibid.) also describe the mushrooming of instruments used to finance aid and global public policy objectives in the ‘wake of innovations in mainstream financial markets’. Several examples offer insights as to how aid might be financed in the future: the use of taxation or quasi-taxation mechanisms that earmark revenues for specific purposes (e.g., the voluntary airline ticket levy used to raise resources for medicine in Africa); the issuance of bonds (e.g., vaccine bonds) backed by future donor aid budgets, which allow the up-front financing of aid initiatives (the International Finance Facility for Immunization (IFFIm), with resources channeled to GAVI); the issuance of ‘catastrophe bonds’ intended to provide financing in the event of large shocks adversely affecting LICs’ agriculture or infrastructure; the development of market-based poverty reduction ‘social enterprise’ models which are profitable enough

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<sup>1</sup> The key counterargument to this is that presumably higher human capital formation will eventually contribute to raising growth (and human capital is essential to move into higher skill areas), and rising human capital and household income will eventually reduce the preference for child quantity, versus quality.

to attract private capital;<sup>2</sup> and Kiva.org and Project RED, which are financial vehicles that exploit individuals' interest in contributing to developing country causes through, respectively, small internet-linked loans or financial sector firms issuing credit cards. Proposals for an international financial transactions tax as well as carbon taxes have also been linked to the financing of aid or of climate change mitigation and adaptation initiatives.

These mechanisms offer the prospect of delinking the provision of aid resources from the short-term pressures of donor government budget processes, including from the political factors that so often drive how aid resources are used. The possibility of mobilizing up-front resources has the advantage of allowing foreseeable long-term financing problems to be addressed earlier, when the effectiveness of interventions might be highest. But as with the increased multiplicity of actors, the burden of co-ordination across policy issues is hampered by the fragmentation of revenue sources.<sup>3</sup>

Finally, Birdsall and Kharas (2010) in another important paper from the Center for Global Development, provide a useful report card on the quality of the aid being provided by many development agencies, both bilateral and multilateral. They suggest indicators that should be associated with aid effectiveness, and then seek to measure how the different donor agencies stack up in terms of realizing these attributes. Their focus is on 'programmable aid', a concept defined by what is excluded from the normal definition of ODA. They exclude those uses of aid that are not intended for development projects and programmes (e.g., humanitarian relief, debt forgiveness, the administrative costs of donor aid agencies, refugee support, food aid, the core funding of NGOs, and in-kind technical co-operation).

Their four indicators of quality relate to:

- (i) the degree to which efficiency is maximized (including, inter alia, the share allocated to poor countries; the share of aid that is programmable; how much support is given to global public goods (GPGs); the share allocated to well developed countries, the share of untied aid);
- (ii) the degree to which there is a fostering of a recipient government's development priorities, budgets, and institutions as well as its capacity to implement development programs (including, inter alia, the predictability of aid flows; the extent of its inclusion in recipient budgets; and the avoidance of project implementation units);
- (iii) the degree of burden imposed by aid on a recipient country's bureaucracies; and
- (iv) the degree of transparency associated with a donor's aid programme.

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<sup>2</sup> One of the most successful and controversial examples is in the microfinance sector, Compartamos (Mexico) and SKS's (India) respective US\$467m and US\$354m IPOs.

<sup>3</sup> Note also that one problem with these efforts to mobilize upfront resources is that innovative finance mechanisms might just yield revenues that are spent on other areas of government, and not necessarily aid. There is not much in these mechanisms to ensure that the total resource envelope for aid rises.

What comes across in their results is the extent to which bilaterals do relatively poorly on most indicators relative to most multilaterals (a few bilateral agencies and the UN agencies being the exception).

- In terms of efficiency, bilaterals perform weakly on a whole range of indicators.
- On fostering institutions, again some important bilaterals (such as the USA) do poorly, as do most UN agencies.
- In the area of administrative burden, they note one ‘defining characteristic of aid today—a very long tail of small projects with little aggregate resource transfers coupled with a few large projects that account for the bulk of resource transfers. This structure is associated with a high administrative burden for aid recipients’.

They also note that ‘vertical funds do much better in maximizing efficiency, largely because of their specialized division of labour and the stability of their disbursements’.

One suspects that there is considerable durability to these results, in part because of long-standing institutional histories that have shaped how donors operate, in part because of the political pressures that force many agencies to adopt practices which deviate from what would be developmentally effective, and in part because of the different goals for which ODA is provided, with the latter shaping what is possible in terms of how aid is provided.

## **2.1 What is wrong with this picture?**

First, as Addison et al. (2010) note, this is a picture of inadequate resources relative to needs, particularly if one also recognizes the inefficiencies associated with the fragmentation of aid from many donors and the quality challenges uncovered by Birdsall and Kharas. Second, one observes a continuing lack of an institutional framework for determining where the needs for aid are the greatest and where resource transfers could make the most difference in terms of addressing these needs. Decisions on priorities are fragmented, both by recipients and by donor and multilateral institutions.

Third, it is difficult to avoid a substantial degree of fungibility by recipient countries in their use of aid, and this further diminishes the likely effectiveness of the resources being channeled to address any given problem identified by donors (though it is possible that the recipient might more effectively use the resources for other purposes). The challenge of fostering full additionality is well recognized and is made particularly problematic by the increased emphasis on the financing of social services in many LICs. The problem particularly speaks to the difficulty faced by donors in trying to ensure that their resources are in fact incrementing spending by recipient countries on the objectives they seek to finance.

A fourth issue of concern is the macroeconomic effects of significant aid flows to small LICs. Where aid flows engender a pronounced Dutch Disease effect, the short-term benefits to the aid recipient country may be offset by the longer-term costs associated with the undercutting of competitiveness. While the extensive literature on this issue does suggest that the problem can be addressed by focusing aid on building capacity in



the nontradeable goods sector, it is easy to argue that these considerations have little to do with how aid is actually allocated.

Finally, the world of aid is one where ‘sustainability’ is addressed only superficially. Sustainability needs to be considered in several ways. Budgetary sustainability relates to whether the budgetary resources that are used to finance a programme will be available in the future. Programmatic sustainability relates to whether the investment of resources in addressing a problem reduces the scale of the problem, such that the future need for such aid is diminished. Or, put another way, does aid reduce dependency or might it only realize short-term successes that later create larger longer-term problems? Operational sustainability relates to the availability of the requisite trained manpower (e.g., in the health sector, can the required medical and paramedical manpower be provided?). Inter alia, environmental sustainability relates to whether aid enhances environmental capital.

In short, in many areas, the current efforts involving the provision of aid give rise to the image of walking upwards on a fast-moving, downward escalator. Are the fundamental forces creating the problems that aid seeks to address far stronger than the effects of aid in reducing these problems? Indeed, it is also often argued that aid might be a far weaker tool for development than, say, donor removal of trade barriers or a greater opening up by these countries to migration from developing countries.

### **3 Characterizing the world of 2025: insights from scenario analysis**

Scenario analysis is a methodology that has been developed to explore the shape of the future. It accepts the essential unpredictability of the future. Indeed it accepts the fact that we are continually buffeted by surprises that channel the world in unexpected directions. Sometimes, these surprises create short-term volatility around an underlying trend, but sometimes they change the fundamentals of the underlying trends, which we previously took for granted. The following quotation from a recent op-ed by Thomas Friedman highlights how much the underlying assumptions about the nature of the world may need to be reconsidered:

Hold onto your hats and your wallets. Since the end of the Cold War, the global system has been held together to a large degree by four critical ruling bargains. Today all four are coming unstuck at once and will need to be rebuilt. Whether and how that rebuilding happens—beginning in the USA—will determine a lot about what’s in your wallet and whether your hat flies off. Now let me say that in English: the European Union is cracking up. The Arab world is cracking up. China’s growth model is under pressure and America’s credit-driven capitalist model has suffered a warning heart attack and needs a total rethink. Recasting any one of these alone would be huge. Doing all four at once—when the world has never been more interconnected—is mind-boggling. We are again ‘present at the creation’—but of what? (Thomas Friedman, 27 August 2011, *New York Times*).

Most scenario analyses seek to provide two critical products. First, they offer several alternative, quite contrasting, pictures of what the world might look like in the near future. These are explicitly recognized as *not* being forecasts, given the essential unpredictability of the future. Rather, scenarios are meant to focus on the fundamental uncertainties that cloud our ability to know the future, and to assume alternative,

disparate, outcomes for these uncertain factors. By implication, this means that a scenario does assume that some fundamental forces that will influence the future *are* predetermined and thus reasonably predictable. For example, demographic patterns are usually seen as predetermined. Second, each scenario should be accompanied by a specific story line that elaborates how the world evolved from its present state to that of the given scenario. These story lines should be highly plausible.

Note that scenario analyses are *not* meant to offer probabilities on the likelihood of any given scenario. All scenarios are meant to be viewed as plausible. While scenarios tend to encompass states of the world that might seem extreme, their value is in providing alternative perspectives for evaluating the viability and prospects of alternative policy choices.<sup>4</sup> Often policy choices involve a significant commitment of resources—for investments, for institutions, for individuals. Exploring their viability and productivity in the context of very different economic and political environments is thus useful for the decision-making process of any organization.

In this paper, we rely on two alternative scenario analyses that were developed to characterize future global political and economic developments. One—developed by the US National Intelligence Council (NIC) (2008)—provides alternative views of the world of 2025. It was the product of a scenario-building process that occurs every five years within the US government to characterize the nature of the world 15 years out. The second set of scenarios was developed by the Tellus Institute, The Global Scenarios Group, and the Stockholm Environment Institute (Raskin et al. 2010). Their alternative scenarios for 2100

... tell [different stories] of the twenty first century with varying patterns of resource use, environmental impacts, and social conditions. The [focus is] on selected global-scale results, painting broad-brush pictures of these contrasting futures, and revealing the fundamental forces driving development away from or toward sustainability. Cross-scenario comparisons offer lessons for policy strategies, institutional change, and, ultimately, for human values.

In this section, we provide only a broad-brush description of these scenarios (also see Appendix Boxes 1 and 2). Our objective is to characterize plausible pictures of the world of 2025—highlighting the central features that have implications for the role and impact of aid. What is striking about both sets of scenarios is the daunting character of the futures that are described. Each set of scenarios does contain one ‘optimistic’ possible future, but even these would require a substantial turnaround in intergovernmental co-operation on shared global objectives relative to recent practices.

Before discussing the individual scenarios, it is useful to highlight the relatively predetermined forces that underlie these scenarios. Such forces are highlighted because they will have implications for the aid environment of 2025:

- **The aging of the industrial world** will soon be reflected in increasingly *aged* societies, with a dramatic change in the proportion of those aged 65 and over and a stabilization, if not a decline, in the size of the population as well as in the

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<sup>4</sup> Over time, they also serve to open up and accustom the mindset of decision makers to recognizing and considering the possibility of alternative worlds for the future.

share of the primary working age groups. Real growth will fall and will be highly dependent on productivity growth. Revenue growth will commensurately slow. Budgetary tensions will be exacerbated by the effects of these demographic forces as well as by difficult-to-control pressures from excess cost growth in the medical sector. These pressures will be further amplified in succeeding decades from the cost of meeting long-term care needs as the share of the very elderly rises. Industrial countries will also be pressured to invest in new energy plants (that contribute to the mitigation of climate change) and in new infrastructure vital for the realization of productivity growth. Given high current public debt ratios, even under the most optimistic scenario in relation to other potential sources of budgetary pressure, it would be difficult to imagine that industrial countries will find the fiscal space to increase the budget share devoted to ODA.

- **Continuing rapid growth in LIC populations**, particularly in some of the poorest and most troubled regions of the globe. Fertility rates in sub-Saharan Africa (SSA) and the Middle East remain substantial (over 4), and the large size of the youth population will further swell the size of female cohorts in childbearing ages over the next several decades. Even if fertility rates in these regions fell today, the effects, in terms of population growth, would only be realized much later in the century. The implications are several.

First, these economies will need to significantly improve their capacity for generating new employment opportunities for their growing work force, in order to exploit the ‘demographic dividend’ for economic growth of reduced dependency and a larger work force. Second, per capita income growth in these countries is likely to remain limited. Given high rates of inequality in these regions, the number of those in poverty, who are now the subject of most current aid efforts in the social sectors, will continue to grow substantially. Third, these countries are likely to experience continued pressures on the already limited land available for agriculture and livestock, intensifying the pressure on food supplies and generating a continuously increasing demand for food relief. These challenges are likely to be exacerbated by the effects of drought and unpredictable weather patterns that will arise from the effects of climate change (see below). Fourth, pressures on available water supplies will intensify, not only in SSA but also in the Middle East (e.g., Yemen). Fifth, urbanization trends, already marked to date, are likely to accelerate in most African countries, intensifying the need for costly infrastructural investments in housing, transport, water, communications, and waste treatment. Sixth, only a technological miracle in the development of vaccines or drugs would be able to stem the continued growth of those infected by HIV and in need of anti-retroviral treatment, as the growth in the number of newly infected individuals continues to outpace the number presently in treatment (see UNAIDS 2010: 8).

Finally, these are regions subject to political instability and conflict, and weak if not negative economic growth. The implications of a growing pool of unemployed youth in troubled countries will give rise to geopolitical pressures, the effects of which are hard to assay. All one can assert is that these situations have been one of the important foci of aid efforts in recent years. The likelihood is that such situations will continue to preoccupy industrial country policy makers and constitute a potential source of demand for financial transfers.

- **Climate change** is another important predetermined force that will influence the environment for aid policy. Most climate change scenarios are highly aggregative at the regional level (at best) and principally yield longer-term forecasts for the century as a whole. But it is reasonably clear that many of the poorest countries of the world, particularly in SSA, will experience serious and costly challenges in adaptation in agriculture, reflecting drought, high temperature, and uneven precipitation patterns. These pressures will generate heavy demands for relief outlays and rising agricultural prices as food supply levels are unable to meet rising demand. Low-lying areas in Asia and Africa will be at risk of storm surges from rising sea levels.

Thus, even if the most optimistic of the following scenarios would prevail, one confronts a world where the demand for aid, if channeled for its present purposes (MDG-related social services and poverty reduction, post-conflict and governance building efforts) will not diminish; the available supply of budgetary resources will be challenged; and new sources of demand for aid are likely to emerge.

### 3.1 The NIC scenarios

It is striking that even the most optimistic of the three NIC scenarios, *constant renewal*—where the ‘world moves in the right direction ... to tackle global problems’—is characterized by significant shocks and adverse events.<sup>5</sup> Indeed, such shocks are what ultimately motivate key global powers to accept the need for integrated and cohesive policy initiatives on major global issues and shared priorities. As possible shocks, they assume a major hurricane hitting New York City, a cyclone striking Shanghai, a severe drought in central China, a sustained global economic downturn, the collapse of the US dollar, and the complete implosion of Pakistan. SSA is projected to remain a ‘virtual quagmire’ ‘until adequate security is realized, with development and sustainability [largely] distant and nebulous goals’. ‘Even with the best of objectives, a strong economic performance that might reverse an increase in the number of people working in extreme poverty is unlikely. Many African countries will still be left behind’.

For this relatively optimistic scenario of economic growth and shared responsibilities to occur would require ‘crises [to] create the shocks needed to force fundamental changes in the mindsets among people in key countries [and] ... grassroots pressures [forcing] inter-governmental co-operation at a global level’. Foreign aid is explicitly mentioned as critical, in part ‘in the interest of capacity building for national security’.

A second NIC scenario—*borrowed time*—is a ‘business as usual’ scenario. It suggests that the world will soon pass the point of no return on the critical policy issues affecting the globe (particularly with regard to climate change), resulting in a world that is ‘ill-equipped to deal with global dilemmas’. Most ‘stakeholders (governments, corporations, etc.) are operating on a short-term basis, while many of the world’s challenges require long-term attention and commitment’. ‘Problems fester and future generations will be faced with greater challenges that might have been avoidable, or at least less severe, in the first place’ (e.g., with respect to water scarcity). Key nation states continue to fail to coalesce in addressing many issues. Non-state actors (NGOs,

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<sup>5</sup> In the description of the two scenarios, quotation marks are indicated where the language has been drawn directly from the US National Intelligence Council report (2008) and the Raskin et al. (2010) article.

private philanthropies, multinational corporations) seek to fill the gap ‘but find success elusive without the support of clear global state-based leadership’. Neither does a viable global governance system emerge from the traditional international institutions/structures. Emerging market powers focus on their own growth and avoid ‘distractions to that goal’ (such as issues of environmental sustainability, global poverty, and long-term energy constraints).

Global economic growth is limited and non-inclusive, with the share of the major industrial powers continuing to diminish. ‘World leaders ... are effectively writing off the ‘human cost’ of growth, with the concerns of the bottom four billion ‘not addressed in a serious and sustained way’, and with the G8 falling further behind on its efforts to help Africa meet the MDGs. Uneven and weak growth also characterizes key emerging market economies. Regional trading and security blocks emerge. Global security issues are addressed in an unco-ordinated and fitful way, the potential for terrorism expands, and ‘many other conflicts suffer from an insufficient response from an overwhelmed international community’. ‘Africa is collapsing under the combined four forces of high population growth, low economic growth, climate change and environmental degradation, and the persistence of widespread diseases’.

Climate change occurs faster than previously thought and the policy choices faced in 2025 concerning pollution, climate change, and weather volatility ... are more extreme than ... [were] faced in 2009’. Low-income countries receive only limited technology transfers from rich countries for either adaptation or mitigation. R&D initiatives are inefficient. ‘There is no human solidarity. The result is huge inequalities of growth, and a world that is fractured and divided’.

The *fragmented world scenario* suggests an even more dire global environment, with ‘parochial interests [taking] priority over sustainable economic growth’, and ‘a world in which events outpace actions’. ‘International co-operation [breaks down] in most spheres of policy—economic and financial, security, and global governance’. ‘The world is unmoored and disoriented’. There is diffusion and weakening of state power (accompanied by a collapse of international systems) and a rise of alternative power sources, extending beyond NGOs and MNCs to include criminal and terrorist networks. The diversity of actors is unusually broad with weakened states and a less reliable international system. With ‘many international institutions considered less ... legitimate there is fundamental redesign in the landscape of power occurring’.

‘The global economy experiences a prolonged slowdown and is characterized by high inflation, [and] relatively high levels of unemployment and low growth’, not only in aging Europe but also in China and India. Security risks extend from the erosion of the nonproliferation regime to regional conflicts and repeated acts of terrorism, with ‘violence endemic’. Immigration restrictions are imposed in Europe. Efforts at climate change mitigation falter as key nations go it alone. The effects of global warming extend to dramatic flooding in some parts of the world (e.g., Bangladesh). A dramatic slowdown in technology diffusion extends from the area of climate mitigation to other areas (‘e.g., pollution controls, health, biotechnology, ICT, weapons’), but ICT is increasingly a factor in this world. Poverty issues are widespread, with sharp increases in food prices (in part reflecting the extent to which biofuels absorb arable land).

### 3.2 The Tellus scenarios

The Tellus scenarios offer four visions of the next century. One—*market forces*—has many similarities with the NIC’s *borrowed time* scenario. It suggests a market-centered, growth-oriented globalization path that suffers from an exhaustion of natural resources and a lack of environmental sustainability. Resource depletion, widening inequity within and across countries, intensifying geopolitical tensions, and remorseless climate change characterizes the evolution. ‘If we muddle forward in a complacent Market Forces mode, the risks rise of deterioration of life-support ecosystems and civilized norms’, that could ‘invite a host of environmental and social crises that could feedback and amplify, undercutting its rosy assumption of perpetual economic growth’.

A second scenario, *fortress world*, is as bleak as the NIC’s *fragmented world*. Different political and social forces contribute to the breakdown of globalization, the emergence of an authoritarian order (and possibly the collapse of organized institutions), the segmentation of the world into those countries and societies dominated by the elite, with repression and inequity rampant, and climate change proceeding on a disastrous path. The latter is alleviated only mildly by the lower emissions rates associated with slower growth.

Tellus’ remaining two scenarios offer visions that are similar to NIC’s constant renewal scenario, with the principal differences arising from what happens between 2025 and 2100. Their *policy reform* scenario—involving ‘government-led redirection of growth toward sustainability goals’—represents a dramatic improvement over market forces in its policies to address environmental sustainability challenges and recognize more equity-inclusive growth. But this scenario ‘would require *unprecedented political will* (my italics) for establishing the necessary regulatory, economic, social, technological, and legal mechanisms’ for its success, given that little change is anticipated in the underlying ‘state-centric international order, modern institutional structures, and consumerist values’. Yet the scenario authors note that the ‘necessary political will for Policy Reform is nowhere in sight’.

Their final scenario, *great transition*, involves an even more dramatic, ‘values-led change in the guiding paradigm of global development’. As with *constant renewal*, the ‘transformation is catalyzed by the ‘push’ of deepening crises and the ‘pull’ of desire for a just, sustainable, and planetary civilization’. The scenario envisages the establishment of more effective governance institutions, less consumerist lifestyles, more rapid population stabilization, and greater and more effective intergovernmental co-operation.

### 3.3 Implications and questions provoked by these global scenarios for 2025

Recognizing that these scenarios were not constructed to shed light on aid policies, what do these scenarios imply about the world of aid looking ahead? One obvious inference is that there will still be a great need for aid, at least in terms of the traditional motivations for aid from industrial country aid donors (as described above). The successful growth experienced by many presently poor countries in the last decade, particularly in SSA, does not seem to be imperiled, particularly for those with abundant natural resources. But for most of these countries, the starting point in per capita income levels remains low, population growth will continue to be high, and the gains from growth will still be unevenly distributed. Even the continued success of these countries will bring its own challenges, with a rising burden of non-communicable diseases and

increased urbanization provoking budgetary pressures. The poorest segments of these societies will still be substantial.

In other low-income, and even some middle-income countries, the prospects for diminished instability and violence remain dim. Climate change and water shortages will engender political and social instability, if not conflicts, as well as significant refugee populations flowing into countries already burdened by large populations of poor people. Fostering a less violent and more stable political environment conducive to economic development in these countries will remain a daunting and complex challenge. Ongoing humanitarian problems will be faced, with negative externalities for neighbouring countries (see World Bank 2011).

While these scenarios do not suggest weakened growth prospects among the key emerging market countries, neither do they suggest a lessening of inequality or a significant reduction in the number of those in poverty (both absolute and relative). Moreover, even the *successful scenarios* are associated with the downside of increased carbon emissions (and an increased stock of carbon in the atmosphere), higher demand for energy and food supplies, intensified pressure on natural resources (particularly water), and diminished food supplies (especially if there is increased biofuels production). Such scenarios imply an even greater need for infrastructure investments and diminished prospects for staying within the bounds of a 2°C warming of the earth. Neither do the scenarios suggest a diminished need for resource transfers to finance the provision of global public goods (to respond to pandemics, to address fragile states within regions, to foster better water management, to protect biodiversity, to fund R&D, or to mitigate climate change).

The scenarios also offer little hope of an increased flow of aid resources, at least from industrial donor countries. Neither should continued real growth in these economies, albeit reduced, lead one to assume a significant positive quantitative step-up in the magnitude of resources provided or in the role that civil society, private philanthropies, and multinational corporations will play in the provision of private sector aid resources. Most scenarios do envisage continued growth in emerging market countries through 2025. This might suggest that their aid flows might continue, but without clarity as to any change in the focus of their aid efforts.<sup>6</sup> Perhaps these countries may join the DAC, but views differ as to whether countries will achieve greater intergovernmental co-operation or consensus on global public policy issues.<sup>7</sup>

These scenarios also do not consider whether ongoing aid efforts will have successfully promoted growth and development, achieved the MDGs, fostered stability, or contributed to the production of global public goods. They are not designed to be commentaries on the counterfactual. But implicitly, each of the scenario exercises is notable for the inclusion of a scenario which offers the *prospect of a transformation over time in the way that civil society organizations, governments, and international institutions interact and in the value systems that motivate them*. Such scenarios offer the clue that it may be as much a question of *how* aid is provided—in many dimensions

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<sup>6</sup> See the recent White Paper on Chinese Aid (People's Republic of China 2011) or the discussion in The Economist (2011) on India's new aid effort.

<sup>7</sup> As an example, China has sought to use the UN as a forum for aid discussion and strategy rather than the DAC, suggesting that if there is more co-ordination in future, it might be through some UN institution rather than the DAC.

of form, function, duration, and approach—that will prove critical to the world of aid in 2025, rather than the magnitude of aid efforts.

Finally, these scenarios provoke obvious normative questions as to the appropriate aid strategy for the next decade or so. These include:

- (i) How can donor and recipient countries pursue a strategy that is relatively risk averse—that seeks to be sustainable and appropriate regardless of which global scenario prevails? Does the prospect of a ‘fragmented world’ suggest that donors should prioritize some countries and issues relative to others in order to minimize downside risks?
- (ii) How can donors maximize the flexibility of their aid policies, in effect allowing them to adapt as it becomes clearer as to the direction the world is heading. Preserving flexibility also provides additional capacity to address the consequences of inevitable surprises (e.g., natural catastrophes, terrorist events) and limit the extent that such surprises shift the world on to the track of more adverse scenarios.
- (iii) Should aid seek to influence which scenario is likely to prevail? Or is aid only a secondary policy instrument that can only be responsive in its design to whatever scenario prevails? The answer to this may well be very region specific or even sub-region specific.
- (iv) Does the diversity of scenarios argue for giving greater pre-eminence to some goals rather than others? Are there some policy challenges that will be dominant in any case? Climate change? Energy sources? Water availability? Fragile states? Limiting violence and instability? Poverty reduction? MDGs achievement? What are the problems for which finding a solution would be most critical and beneficial to humankind, not only in the present but also over the longer term?
- (v) Given the diversity of actors in the world of aid—public and private—should there be a division of labour in terms of the primary focus of their respective aid efforts (assuming donors might find sufficient incentives to co-operate)?
- (vi) Given the budgetary pressures likely to confront industrial countries, should increased attention be given to innovative financing mechanisms that ‘lock in’ channels of resources earmarked for aid or other global public goods (providing insulation from short-term budgetary pressures)? Will they use these mechanisms instead to fund the budget in general rather than for aid?
- (vii) Should industrial countries enhance their efforts to achieve greater consensus on aid policy with new aid donors from emerging market countries?
- (viii) Despite the increasing economic weight of many emerging market and middle-income countries, should the industrial donors nevertheless consider resource transfers to these countries, recognizing that they have large numbers of poor



and that their policy efforts on climate change mitigation will have enormous effects on global climate sustainability?<sup>8</sup>

#### **4 A normative policy framework for aid looking forward to 2025**

What change in the course of aid policies would best take account of the potential scenarios for 2025, the problems that characterize the current world of aid, and recent developments in that world? In laying out a recommended course of action, my bias is towards the precautionary principle, that is to say it is best to be relatively risk averse, and not to assume that the more optimistic global scenario will prevail. I also start from a perception of the principal sources of inefficiencies and ineffectiveness that today characterizes aid. These start with the serious fragmentation both in the priorities of donors as well as in the source of resource flows. While the fragmentation in sources can be considered a strength, to the extent that it has led to an expansion in the volume of resource flows and new innovations in the way in which aid is delivered and results obtained, it has also entailed serious problems of prioritization, co-ordination, duplication, and lack of alignment with the interests of recipient countries. The ‘bang for the buck’ obtained from much of the resource transfer is low as a consequence.

Fragmentation in priorities extends beyond a developmental or social welfare focus. It partly reflects the significant share of aid flows and resource transfers that serve more political economy, donor national security, and mercantilist interests rather than developmental assistance, social welfare, or global public good concerns. And it partly reflects the relative narrow focus of the prevailing attempt at harmonizing aid priorities as embodied in the Millennium Development Goals. As noted in the recent report of the Advisory Council on International Affairs (2011) from the Government of Netherlands the MDGs, commendable as they are in terms of progress from the even less focused world of the previous half century, still exclude other policy objectives for resource transfers which might be considered as more important and of higher return than those of the MDGs. Efforts to consider what might be a desirable prioritization in the use of resource transfers has been relatively limited (the efforts of the Copenhagen Consensus are perhaps most notable) and largely ignored in the priority-setting process of donors (Lømborg 2009).

But I also question the appropriateness of the priorities revealed in the current trends in the allocation of resource transfers; specifically, the relative balance that tilts in favour of developmental assistance, social welfare-type expenditures, and transfers that are heavily of a consumption nature. While yielding some immediate benefit in welfare to recipients and addressing the undoubted inequities and hardships that afflict a large share of humankind, such allocations do not significantly contribute to improving either the long-term welfare of these populations nor stem the intensified depreciation and depletion of the world’s environmental capital, both with respect to climate change and biodiversity.<sup>9</sup> Neither, in an increasingly globalized world, do such allocations address

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<sup>8</sup> Such developments are already emerging, with the possibility that some World Bank lending on climate change will go to middle-income countries that would otherwise be graduating from Bank lending/grants.

<sup>9</sup> As Paul Krugman noted in a recent NY Times editorial ‘In fact, if you follow climate science at all you know that the main development over the past few years has been growing concern that projections of future climate are underestimating the likely amount of warming. Warnings that we may face civilization-threatening temperature change by the end of the century, once considered

the need for greater outlays on other global public goods, the challenges that are building from the growing population disequilibrium among the poorest regions of the world nor the high share of the world living in countries or sub-regions of countries subject to conflict or fragile governance. Neither do current aid allocations recognize the greater degree of interconnectedness that increasingly prevails on many policy issues.<sup>10</sup>

More pointedly, I thus argue for a reduced flow of aid for development assistance for income convergence and for social welfare-related services in order to channel more resources to addressing key issues in the global public goods debate. The principal DAC donors from industrial countries should essentially accept that social welfare and income convergence assistance is better suited to come from the efforts of private philanthropies and civil society (if not from budgetary reallocations away from unproductive expenditure in aid recipient countries). DAC donors should thus focus their budgetary aid on global public goods with a high externality content. Implicitly, this argument also means that emerging market and resource-rich countries should be expected to bear more responsibility for addressing the needs of their poorer citizens.

Implicitly, some of my suggested reorientation in priorities takes account of the thrust of the scenarios envisaged for the next several decades. Aid should be one factor, albeit among many, that can influence whether the path taken will be in a favourable direction. This explains my focus below on some key challenges, notably conflict resolution and governance; climate change; biodiversity; population disequilibrium; and technological innovations in the area of energy and medicine.

Also underlying my argument is a strong assumption on the relevant social discount rate. The degree to which the welfare of the current generation of adults should supersede the prospects of the youth of today or unborn generations of the future has been largely a matter of neglect, with the bias overwhelmingly in favour of the former. In effect, we are underinvesting in the future relative to the present. The nature of the world being bequeathed to our grandchildren's generation and their children remains an extraordinary unknown in many respects. The consequences of the likely loss of biodiversity, the warming of the oceans, the effects of global warming, while highly indeterminate, are certainly worrisome. Were any serious effort to be made at considering the priorities for aid flows, the issue of whether to adopt Nicholas Stern's assumption of a very low social discount rate would be highly relevant (Stern 2006).

Another argument for redirecting aid resources is essentially a negative argument. It reflects the recognition by informed economists (Spence et al. 2010) that *policies* are what tellingly matter in explaining whether a country is able to accelerate its rate of economic growth. While this could be seen as mirroring the Dollar and Burnside (1997) argument that aid should only be provided to countries that demonstrate a strong policy commitment—and thus a more selective approach as to the conditionality that should accompany aid—the other sources of inefficiency of aid diminish the overall return and

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outlandish, are now coming out of mainstream research groups'. ('Republicans Against Science', *New York Times*, 28 August 2011).

<sup>10</sup> In this regard, I share the view of NematShafik (2011), who emphasizes in a recent paper that 'if we get this right, the future of aid will be to serve as the major tool for addressing the global challenges of our time—peace, poverty and environmental sustainability'.

argue for other policies that benefit low-income countries in different ways—for example, trade.

My prescription for a desirable evolution of an aid policy framework for the coming two decades is focused principally on the community of DAC donors. It does not seem likely that any agreement on pooling funds for agreed priorities could be reached which extends beyond DAC donors. My reading of the scenarios suggests that the kind of fragmentation in sources of aid and other resources described by Severino and Ray (*ibid.*) will only continue and the likelihood of a grand agreement including new emerging market donors or private donors is low. Moreover, one would want to encourage continuing independent initiatives by the non-governmental social sector (*viz.*, private philanthropies and civil society), which are likely to be heavily tilted towards social welfare-type expenditures. Tax incentives provide one outlet for public financial support for these priorities and initiatives.

In contrast, there would appear a greater prospect that the community of DAC donors might be able to move towards some consensus on a revised agenda in the use of aid resources. While I believe that the current DAC donors should be the entity which seeks a revised aid policy framework for the budgetary resources under their control, I would also pursue Severino and Ray's (*ibid.*) proposal to keep the DAC but change it to a 'Global Policy Funding Forum,... allowing other countries and organizations to fully access a forum where global policies are debated, standards set, and evaluations processed'.

In particular, my proposals relate to a *broadened pool of resources* that would encompass both aid flows (presently subsumed under the 0.7 per cent target) as well as those resources contemplated for climate change adaptation and mitigation (see below). There is a need for greater realism as to the size of the pool of resources likely to be available for all of these transfers. This underscores the importance of an enhanced prioritization. The 0.7 per cent target for aid—so rarely realized by any donor country—remains more of a fixed hope than a reality likely to be realized. To protect this target, assistance for climate change mitigation and adaptation has been treated as requiring separate initiatives. But these too remain grossly underfunded relative to the estimated need. This artificial separation should be dropped. As argued by Gupta and myself in 2002, questions could even be raised about the appropriateness of the 0.7 per cent target, as the number of LICs is gradually diminishing and the amount of resources associated with meeting the 0.7 per cent target would be large relative to their needs. Only if the objective of aid were extended to address the problems of poverty in middle-income countries would the amounts of aid mobilized from a 0.7 per cent target not become excessive in macroeconomic terms. Looking forward to 2025, these issues would *a fortiori* become more relevant. It is far more realistic to recognize the multiple objectives of resource transfers as noted above, and to seek to utilize them in a prioritized way to address them.<sup>11</sup>

In addition to a refocused set of priorities, aid flows from the DAC should maximize the comparative advantage of donors and increase the return from the resources that are allocated. This means seeking ways of achieving desired results while minimizing the

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<sup>11</sup> I recognize that this might effectively dilute the political economy argument that having an enshrined aid target of 0.7 per cent serves, and the value of quantifying assistance for climate change on its own terms and as additional to the 0.7 per cent target.

leakage in funds associated with fungibility and rent-seeking and limiting the adverse effects that budgetary resource transfers entail in terms of their macroeconomic effects. Maximizing the comparative advantage of donors means to draw on their greater capacity for technological innovation and their richer pool of highly skilled human resources. The problems confronting the globe, and the poorest countries in particular, require a quantum leap in the development of suitable low-cost technologies and here the industrial countries as well as some emerging market countries constitute the obvious source.

In effect, this calls for utilizing a substantial part of aid resources to finance a dramatic upsurge in investments in R&D *in donor countries* on areas of benefit to low-income countries. These should include investments in: renewable energies for power and transport; for solar energy; for low-energy water desalinization; for carbon sequestration; for new green revolution-type agricultural technologies for crops that will have to flourish in very different climatic environments; for drugs to combat the major disease scourges afflicting the populations of poor countries; for low cost medical devices (e.g., portable MRIs) that are adapted to limited budgetary environments; and for low cost drip irrigation systems that maximize the efficiency of water use.<sup>12</sup>

The objective would be to dramatically expand the production possibility frontier of LICs by making available, at significantly reduced prices, new technologies in all these domains but most particularly in domains that contribute to the realization of global public goods objectives. The more that LICs and MICs can be incentivized and benefit from low-cost solutions that limit damage to the environment, the more they are likely to opt for them and afford them. Such a refocusing of aid can lead to a far greater targeting of expenditures without fungibility to unproductive expenditures in recipient countries and without giving rise to Dutch Disease effects. By spending more of aid resources on their own domestic R&D sectors, industrial countries may be able to buy continued political support for aid.<sup>13</sup>

The refocusing of the aid agenda should principally concentrate on the following issues:

- (i) **Climate change mitigation:** the goal of limiting the average degree of warming to 2°C within this century (and thus much *higher* warming in many parts of the globe) is probably already beyond reach. But the IPCC studies highlight the progressively more adverse effects that we know will come about from a greater degree of warming, and perhaps more important, the increased uncertainty as to the consequences that can only be speculated upon (in terms of the loss in biodiversity). While many parts of the world may seek to insulate themselves from the loss in economic welfare that such a climate change may imply, most studies suggest that at higher levels of warming this may not be so easily

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<sup>12</sup> Efforts would be needed to ensure that the intellectual property rights associated with such aid-funded innovations allowed developing countries to access such technologies at a low price.

<sup>13</sup> In addition to the intellectual property rights issue noted above, one further challenge that would emerge with such a shift in strategy would be to prevent the inevitable rent-seeking that might arise in the allocation of such funds, which could distort the R&D away from investments of true benefit to developing countries. Consideration might be given to the type of prize competition that was initiated by the Gates Foundation (The Grand Challenges) and which is being considered by other donors such as USAID.

achieved. Realizing the 2°C objective will require a path of increasingly dramatic reductions in emissions over the course of the century, particularly for industrial and emerging market economies. The technologies to achieve this goal, and the infrastructural investments to implement such technologies, will be costly.

Note that I have not attached as high an objective with regard to climate change to adaptation. In part, this is misleading, because in some spheres, adaptation (particularly with regard to some issues—limiting drought and soil erosion, protecting forest resources) may be vitally important for mitigation. But this lower priority reflects both the assumption that such adaptation will be an inevitable component of any country’s infrastructural investment agenda and the expectation that R&D initiatives would include efforts at developing new technologies that would facilitate adaptation, particularly in agriculture and forestry.

- (ii) **R&D investments in the pursuit of many global public goods:** as noted earlier, in energy, agriculture, and medicine.
- (iii) **Promotion of more financially sustainable models for addressing poverty problems:** beyond technical R&D, a set of impact-focused private companies known as ‘social enterprises’ are innovating models to provide energy, health care, clean water and other goods which are designed to cover their own costs or even generate enough of a return to attract private capital. Adoption of these models can help aid dollars go farther and attract different pots of capital to areas previously only addressed by government and aid dollars.
- (iv) **Protection of biodiversity:** ecologists and biologists continue to warn about the extraordinary pace at which species will be extinguished during this century, and the dramatic uncertainty that characterizes our understanding of the ecological impact of such losses, particularly as relates to many of the more elemental species low on the food chain.
- (v) **Responding to the increasing challenge of limited water availability** for a substantial segment of the world’s population.
- (vi) **Defusing major sources of conflict and instability in many parts of the low-income world and the rebuilding of failed and fragile states.** The scenario exercises support the argument of the World Bank’s World Development Report (WDR) 2011 that such problems will be a major source of instability and welfare loss in coming decades. The WDR also highlights both how the skill set and policy initiatives that are required to address these issues differ from those of the traditional development agenda as well as the longer time frame over which such initiatives need to be mounted.<sup>14</sup>

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<sup>14</sup> Thus, arguably the World Bank might not be the right place to manage conflict issues, and the UN might need a major strengthening to play this role.

- (vii) **Addressing the substantial disequilibrium that will characterize the world's population structure in coming decades.** We have noted earlier that a substantial population increase will occur in regions characterized by low per capita income, diminished resource availability, already high rates of unemployment, and gender inequity. It is difficult to foresee how such imbalances will shake out in political, security, and welfare terms, but seeking policies that minimize potential adverse effects should be high on the agenda of industrial and emerging market countries. Fostering of immigration that can meet the needs of aging countries, and facilitating circular migration that can limit the impact of brain drain on high population regions will be a contentious but important challenge.
- (viii) **Ensuring a contingent share of aid resources that is available to respond to humanitarian relief needs.** These will continue to be costly and necessary, as natural disasters (in part a function of climate change) and security challenges inevitably occur and some public assistance will necessarily complement private sector relief efforts.

In addressing these issues, the DAC community will need to recognize some difficult truths:

- (i) It will be necessary to **mobilize and convince public opinion** on the importance of this shift in direction in priorities for publicly funded aid resources.
- (ii) The **solutions to many of these issues still remain to be developed.** Many of the needed technologies are not even well recognized. Equally, achieving solutions to other challenges will be hard, with no easy solutions readily apparent (e.g., with respect to global population imbalances). Some technological solutions may be easier to achieve than is typically recognized, but may require reconsideration of the incentive mechanisms that can be adopted to induced private sector agents to innovate towards low cost technologies (advanced market commitments as a model).
- (iii) **Some issues will require the development of new multilateral institutions,** most likely of the vertical kind. WDR 2011 convincingly raised questions as to whether existing multilateral agencies have the skill mix, the time horizon, and the organizational flexibility to adequately engage in conflict resolution and the rebuilding of governance systems. While the present inefficiency of many multilateral aid agencies, and their persistent longevity, remains a troubling and costly phenomenon, one cannot assume their capacity to reinvent themselves.
- (iv) **Some issues will entail transfers of financial resources to emerging market countries that would seem inappropriate for financial assistance.** In particular, addressing climate change mitigation or biodiversity will require policy and resource initiatives by some of the larger emerging market countries. Any scenario on climate change

recognizes that the principal source of growth in emissions will come from many of these countries, given their large populations, their still youthful point in the demographic transition, their aspirations for higher per capita income levels, and their rapid rates of growth. Yet these countries have high reserve levels, are presently running current account surpluses, and are now themselves increasingly active aid donors.

On the one hand, it seems illogical to channel aid resources to countries already awash with reserves. Yet for these countries, compromising their growth prospects through the implementation of measures to contain emissions or shelter biodiversity is likely to be a high cost policy initiative. Indeed, these countries already demonstrate a limited willingness to compromise their growth prospects by addressing prevailing inequities or inadequacies in social service provision. In effect, if these negative externalities are indeed a source of global concern, then these countries may need to be financially induced to pursue domestic policies that would ‘internalize these externalities’.

- (v) Finally, **the reordering of priorities needs to allow for some degree of flexibility**, recognizing that the scenario path that the world will proceed upon cannot be readily assumed and that a path that had not been anticipated might entail a revision of priorities for aid allocations.

#### **4.1 Issues in implementation**

The change in aid priorities will need to be accompanied by a revisiting of the institutional framework through which aid is financed and delivered, and a gradual movement toward a new implementation framework. Some of these issues have been discussed above, including: the need to reconsider the ‘target for aid’ in an environment where prioritization in aid must include many previously excluded global public good objectives; the reconsideration of the roles to be played by DAC countries vis-à-vis private sector actors and non-DAC donor countries coupled with an embracing of the diversity of actors and their different priorities and forms of involvement; and the possibility of using tax deductions or credits as leverage mechanisms to both encourage private sector financing efforts and to steer such efforts on behalf of favoured objectives. But other implementation challenges remain:

**Facilitating a prioritization process:** We have argued that the global aid process lacks an adequate mechanism for prioritization among aid and global public good objectives. This is not surprising, given the conceptual, empirical and value issues that make such a process so difficult. But this does not mean that the institutionalization of a prioritization process is not needed. Two initiatives in this direction are worth noting. One—the Canadian Priorities Agenda, conducted under the auspices of the Institute for Research on Public Policy (Leonard et al. 2007)—represented one such effort to initiate

a broad-based and informed public debate on policy priorities for Canada over the medium term. The project’s central theme was scarcity of public resources and the need for governments to make sound policy choices for the future. It brought together 45 of the best policy minds in the country to examine and deliberate on choices and priorities in the context of the following eight broad policy challenges identified by the CPA agenda setters: human capital, climate

change, natural capital, population aging, economic security, health outcomes, productivity and trade, and globalization. The process and substance of the project generated widespread interest and led to high-level meetings at the Bank of Canada and the Department of Finance (<http://www.irpp.org/cpa/>).

Another model arose from the Copenhagen Consensus initiative in 2004 (jointly financed by Denmark and the Tuborg Foundation).

The exercise started as a simple but untested idea of prioritizing global opportunities. In 2004, the process was carried out for the very first time and ended with a successful list, compiled by some of the world's top economists, attracting attention from all over the world ... The ambition is to carry through a global Copenhagen Consensus exercise every fourth year similar to the Olympics. This ensures that new, important challenges and solutions are included in the process and that research is updated ... The basic idea is: Imagine you had US\$75bn to donate to worthwhile causes. What would you do, and where should we start? (See Lømborg 2009 <http://www.copenhagenconsensus.com/About%20CC08/The%20Basic%20Idea.aspx>)

How might such an exercise be organized, under whose auspices, and with what frequency such that it yields adequate credibility and cover for DAC donors on which to base their aid allocation decisions?<sup>15</sup> In principal, one could envisage such a process either under the direct auspices of the DAC or even of the G20. Alternatively, one could imagine that a politically neutral body—perhaps funded by a private foundation—could organize such an initiative in a way that would not be tied to the political interests of specific donors. The G20 or DAC might then consider the recommendations of such a neutral body and seek a political consensus on their proposals.

**Looking forward: the role of bilateral and multilateral aid agencies:** The world of aid in 2025 is not likely to see a reduced number of official actors. In part, this reflects the difficulty of closing ineffectual multilateral agencies, some of which have roles that are no longer terribly relevant and which have failed to reinvent themselves. More likely will be the strengthening of the more competitive general multilateral agencies that continue to have an important role to play as well as the emergence of new dedicated vertical funds that are inherently more specialized and nimble in their ability to finance initiatives for global public goods that need a dedicated champion organization. The World Bank and other regional development banks will continue to play an important role, given their capacity: to provide an informed perspective to low-income and emerging market countries on country development strategies; to serve as a vehicle for infrastructural and programmatic lending; to provide an important perspective on the interconnectedness of many structural policy issues and to highlight the next that need to be addressed; and to provide macro policy guidance.

But the evolution of many of these multilateral agencies over the years has tended to dilute the specialized capacity and the institutional memories of their staff, making them a world of informed generalists as opposed to highly specialized experts. Increased mobility and some politicization of their bureaucracies have also limited their overall

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<sup>15</sup> For example, the Copenhagen exercise was criticized by some for lacking consistency in the cost benefit analyses used to assess alternative interventions.



effectiveness. Their increased bureaucratization has also limited their capacity to play a nimble and flexible role in providing policy advice in many specialized domains. The vertical fund model will thus need to be elaborated further with regard to global public good issues. For example, it is not clear that the UNEP or the UN secretariat dealing with climate change have the capacity to forcefully lead the global effort in relation to climate change. It also remains unclear whether the World Bank staff can play this role, given the relative balance of generalists vs. specialists in many of their departments. Equally, the *World Development Report 2011* indirectly makes a case for a vertical fund that has the particular specialized skills and capacity (most of them non-economic in nature) to address the problems of countries or sub-regions in conflict or in the long-term process of rebuilding governance.

**Pursuing the objective of developing independent revenue sources:** The budgetary challenges that will confront industrial country donors in the decades ahead argue for continued efforts to provide independent, earmarked revenue sources that can contribute to the funding of global policy initiatives (e.g., as with the airline solidarity fee and RED) and that are somewhat immune from the exigencies of budgetary pressures (if not from the effects of recessionary forces). The appeal of a carbon tax or a cap and trade scheme for emissions auctions is that it offers the possibility that in addition to a price for carbon closer to its real economic cost, revenues could be generated which could be allocated for mitigation and adaptation efforts. This is not the place to survey the various other revenue mobilization initiatives that are often proposed (e.g., the Tobin Tax) but continued initiatives to implement mechanisms that earmark revenues is an important policy direction for aid. Mechanisms such as the IFFIm, that seek to front-load future aid allocations for high return investments on global initiatives are valuable to the extent that the resources can be genuinely dedicated and so used (see Atkinson 2005).

**Embarking on a new framework of relationships with potential recipient countries:** Perhaps the most difficult and challenging element in the reprioritization advocated above is the implication of some gradual disengagement by donors from current allocations for social welfare and developmental purposes to low-income country recipients. This becomes even more controversial to the extent that it is associated with transfers to high-growth emerging market countries in relation to addressing global public good initiatives. Obviously, this is a disengagement that would have to be gradual in order to allow recipient countries to enhance their own domestic revenue mobilization efforts and to reorder their own budgetary priorities to replace some of the lost aid revenues.<sup>16</sup> Private sector and emerging market donor involvement would presumably continue, so that the loss in aid revenue would not constitute as large a fiscal hit. Despite the recent financial crisis, the last decade has also demonstrated that private capital markets can be tapped for well-planned and well-governed infrastructural investment initiatives, either by governments directly or through public private partnerships.

DAC donors would continue to be involved in relation to development programmes that embodied the revised aid priorities. Thus, one might observe aid efforts to foster climate

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<sup>16</sup> Eurodad, in a recent policy paper on whether foreign aid, emphasizes that more effective domestic resource mobilization is central to any effort by low-income countries ‘to recapture policy space’ and ‘emancipate them from heavy reliance on external development finance, concessional and otherwise’ (see van Waeyenberge and Powell 2010).

change mitigation and adaptation; or human capital investments that might facilitate short-term emigration or circular migration efforts; and new initiatives to foster improved institution building and enhanced governance. But implicit in this reordering of priorities is the argument that after more than a half century of aid assistance to many low-income countries, the responsibility for addressing the welfare of their populations and energizing growth lies with their governments. This would be even more the case if industrial countries were to fully remove many of the subsidies that currently disadvantage many low-income countries. The possibilities of rapid growth have been demonstrated here for many poor parts of the world and the responsibility of global donors must now be to address the ever-pressing global storms that these donors themselves, in part, have engendered. The reorientation of donor priorities also carries the emphasis on an alternative approach to assisting potential recipient countries. In part, the effort to pioneer new innovations in technologies of benefit to them should be recognized as facilitating an increase in their productivity by expanding their production possibilities and lowering the price and increasing the quality and value of many essential inputs and consumption items.

## **5 Concluding remarks**

The world is changing in many ways and the prospects for further dramatic changes only deepen when one looks to the rest of the twenty-first century. After sixty years of foreign aid efforts and dramatic change in the world of aid recipients, it is time to reconsider the role that aid should play in coming decades. This reconsideration should extend: to the priorities that aid should be used for; to the ways that donors can contribute to these different policy objectives; and to the roles that different current aid actors (donors and recipients) should play.

This paper has sought to apply the optic of scenario analysis to frame the potential contexts in which resource transfers can play a role in the global economy, and to ask whether the traditional priorities for aid—particularly that derived from industrial country donors—are serving the appropriate purposes. In essence, it argues that after sixty years of a moral commitment to those countries that were far behind in the global economy at the time of decolonization and the turbulence of the Second World War, the pressing needs of humankind call for a different focus. Globalization (with far reaching forms of interconnectedness across countries), global warming, dramatic biodiversity loss, and geopolitical turbulence suggest that responding to the imminent threats to economic, political, and ecological stability call for no less of a resource commitment by industrial countries, but with a focus that is principally directed to addressing the need for global public policy initiatives and the provision of global public goods.

This is not an argument that diminishes the moral importance of addressing global poverty, neglect, gender discrimination, and in this twenty-first century, needless suffering from treatable diseases. It is an argument that says that underemphasizing other large challenges facing humankind will only result in the latter problems continuing and indeed, becoming potentially even greater. Moreover, the environment of aid has changed dramatically, even in the last decade, with many more players, far greater economic and political sophistication at the level of aid recipient countries, and far richer modalities through which the policy possibilities of the latter can be enhanced.

Private philanthropies and emerging market donors are now playing an increasingly active financial role in supplying aid resources to the poorest countries and for vital

social services. Many low-income and middle income countries have made much progress in their development; some, with large natural resource endowments, have the potential to seriously address problems of poverty if there is the commensurate political will. Other middle-income countries with significant populations of poor, are well aware of the policy tradeoffs as between growth and poverty reduction. Good policies can do as much for growth as additional aid resources, which often come with price tags that sap development initiatives as much as they support them. And industrial countries, by dramatically enhancing the technologies available to low-income countries, can lower the price of interventions that can significantly improve productivity in many sectors, both economic and social. Their removal of trade barriers and subsidies that unfairly bias the playing field against LIC products and services is equally necessary.

In short, as the resources available for aid from aging industrial societies stabilizes and potentially even shrinks, the task must be to identify the policy challenges that most imperil the global economy and polity looking ahead, and to allocate aid resources to grappling with them and diminishing the threats that they pose, and to maximize the impact of these resources by allocating them to fit the comparative advantage of donor countries.

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## Appendix

### I. The NIC scenarios for 2025 and the Tellus scenarios for the twenty-first century

#### Box 1: NIC Scenarios for 2025

**Borrowed Time** describes a world following a path that, without major changes, leads to an unsustainable future. Ignoring, or giving insufficient credence to, the long-term consequences of their policy decisions, leaders leave an ‘imperfect’ or ‘flawed’ legacy for future generations. The result is a world that is ill-equipped to deal with complex global dilemmas.

**2013-2021:** Lack of harmony in regulatory frameworks in combination with global leadership vacuum results in difficulties in the West’s adjustment to new geopolitical realities. The rules of the game are shifting and cracks appear in the system (e.g., OPEC falters, immigration clampdowns).

**2022-2025:** Future generations are now set to inherit the many problems that have been allowed to fester. Economic swings, rising protectionism, and clear winners and losers (i.e., inequitable growth) characterize this world.

**Fragmented World** describes a world struggling to manage problems against a backdrop of constrained growth combined with a lack of multinational solidarity. Neither nations nor the international system can keep up as the problems leave the solutions behind.

**2013-2021:** The dream of the BRICs fades somewhat and global insecurity increases (e.g., natural resource and ethnic conflicts, Middle East arms race). Technology diffusion dries up. International co-operation is absent.

**2022-2025:** Poor economic performance, failed leadership, increased tensions, and an absence of multilateral co-operation define this world. An overwhelmed international system is collapsing under its own weight.

**Constant Renewal** describes a world in which nations realize that the international community must work collaboratively on a sustained basis to affect real change at the global level. Leaders systematically adjust policies and frameworks as needed in support of shared global priorities. While the transition is not without difficulties, the world moves in the right direction.

**2013-2025:** A world in which societies reconnect with each other on local and global levels to tackle global problems. Although problems persist, global community comes together (albeit with some hiccups) and sets itself on a path towards economic growth and shared responsibilities.

## **Box 2: The Tellus Scenarios**

*Market Forces: Market-centered Development:* a future in which free market optimism remains dominant and proves well founded. The global economy expands over three-fold by 2050, eightfold by 2100. The availability of sufficient resources and the means of maintaining ecological resilience in such a huge economy are critical uncertainties. The challenge compounded by the need to maintain social and economic sustainability in a world of profound inequalities between rich and poor countries, and within each country. Instability and conflict are major risks.

### *Policy Reform: Directing Growth*

Policy Reform assumes the emergence of a massive government-led effort achieves sustainability without major changes in the state-centric international order, modern institutional structures, and consumerist values. Strong and harmonized policies are implemented that are able to achieve internationally recognized goals for poverty reduction, climate change stabilization, ecosystem preservation, freshwater protection, and pollution control. The scenario halves world hunger between 2005 and 2025. Implementing this grand policy programme in the context of Conventional Worlds values and institutions would not be easy: intergovernmental efforts to address sustainability challenges over the past two decades have not succeeded. The Policy Reform path would require unprecedented political will for establishing the necessary regulatory, economic, social, technological, and legal mechanisms.

*Fortress World: An Authoritarian Path* explores the possibility that powerful world forces, faced with a dire systemic crisis, impose an authoritarian order where elites retreat to protected enclaves, leaving impoverished masses outside. In our troubled times, Fortress World seems the true—business-as-usual scenario to many. In this dark vision, the global archipelago of connected fortresses seeks to control a damaged environment and restive population. Authorities employ geo-engineering techniques to stabilize the global climate, while dispatching—peace-keeping militia to multiple hotspots in an attempt to quell social conflict and mass migration. But the results are mixed: emergency measures and spotty infrastructure investment cannot keep pace with habitat loss and climate change, nor provide adequate food and water to desperate billions.

*Great Transition: A Sustainable Civilization* envisions a values-led change in the guiding paradigm of global development. The transformation is catalyzed by the push of deepening crises and the pull of desire for a just, sustainable, and planetary civilization. A pluralistic transnational world order coalesces as a growing cultural and political movement of global citizens spurs the establishment of effective governance institutions. Less consumerist lifestyles turn toward qualitative dimensions of well-being: creativity, leisure, relationships, and community engagement. Population stabilizes more rapidly than in other scenarios as more equal gender roles and universal access to education and health care services lower birth rates in developing countries. The world approaches a steady-state economy with incomes reaching about US\$30,000 per person by 2100, three times the current average.