Re-inventing Aid

If the international development task must now consist primarily of helping developing countries to run successful market economies, the question is how this is to be done. International aid has mostly taken the form of financing governments and the change in the role of governments which the move to the market economy requires must also mean a change in the activities which aid finances. At the same time, if the private sector is to play the leading role in economic growth, much more attention needs to be focussed on aid to the private sector – a task which also needs careful definition. Aid needs to be re-invented.

Some conservative economists have argued that any development aid is inconsistent with the market philosophy. On this view, any development activities undertaken by governments or international organisations are ipso facto an interference in the market economy and therefore damaging to economic efficiency and growth. The interests of Third World countries, and of the donor countries themselves, would be served best if the whole aid and development effort were abandoned. The foremost proponent of this view has been the British economist Peter Bauer.¹

This simplistic and extreme position, based more on a priori arguments than on an examination of the evidence, unfortunately diverts attention from some real issues. It is true that international aid grew out of a period when there was a prevailing belief in the ability of the state to promote economic growth, through public investment, ownership of enterprises and planning, and, as I have argued, aid to governments encouraged many of them in such policies in the past. These beliefs are shared by few serious people now and clearly the acceptance of market principles must raise serious questions about the effects of a great deal of traditional aid activity.

The view that market economics completely invalidate the case for any kind of aid is altogether too sweeping. The question is: what kinds of aid can be consistent with a belief in market economics and what kinds are not? I believe Bauer
Re-inventing Aid

133

does us a service when he asks why the case for aid ‘has come to be taken as practically self-evident’. But he himself is open to the charge that he treats the case against aid as self-evident and does not distinguish between one kind of aid and another. The case for aid does indeed need to be argued and justified, both on the basis of principle and case by case.

I believe we need a new intellectual basis for the whole aid activity. This new basis must be fully consistent with, indeed built on, the market philosophy, so we might well start from the challenge of those who believe that the market philosophy invalidates aid in its entirety.

The extreme proposition that any form of development aid is inconsistent with the market philosophy fails on two counts. First, it ignores the important positive role the state must play in an efficient market economy – a role which I discussed in the previous chapter and which normally includes some public investment. This role of governments is a non-market activity – governments cannot be market operators because they do not operate in an environment of market risk – but necessary to create the conditions in which the markets can function well. In the Third World, many governments are not able to perform this role satisfactorily and can benefit from external assistance. Economic progress can be accelerated by selective and targeted assistance to help government perform these functions. But it is of crucial importance that any aid activities carried out under this rubric must assist the development of a healthy market economy and not hinder it.

Secondly, so far as the private sector is concerned, the extreme view fails to distinguish between a fantasy world in which market forces function perfectly and the world as it actually is. In the market economy, the private sector will be the driving force of growth, operating in an environment of market forces and subject to market risks and incentives. But the truth is that in most Third World countries, this environment is highly imperfect and market forces work less efficiently than in more developed countries. This retards the processes of investment and growth. (We could almost define under-development as a set of conditions in which markets can only work badly.) So certain aid activities which enable private companies and investors to cope with these conditions and facilitate markets in making sound investments can be