

In Search of New Approaches to Japanese Development Assistance

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Foreword

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International development has entered a dynamic phase, as indicated by increases in funding at the onset of the 21st century following declines in the 1990's. An important contributing factor to this has been accelerating economic, political and social globalization. Assistance to the most fragile states has also been prompted by terrorism concerns in major donor countries. If development had ever been an issue to be treated in isolation, clearly that time is past. It has now become a process with a global context, global consequences and global ramifications.

Some donors have restructured their organizations to adjust to the changing trends. Noticeable examples include the UK, which established the Department for International Development (DFID), the US, which established the Millennium Challenge Corporation (MCC), and France, which established Agence Française de Développement (AFD). The UN aid agency, UNDP, shifted its attention away from technical cooperation to the provision of upstream political analysis and policy recommendations, and changes are also under consideration at the two Bretton Woods Institutions — the World Bank and the International Monetary Fund.

In Japan, two important international conferences are scheduled for 2008 — the G8 summit to be held in Hokkaido and the 4th Tokyo International Conference on African Development (TICAD IV) to be held in Tokyo. And in the fall of 2008 a significant new ODA organizational structure is set to be introduced. This is an opportune time, therefore, to review and examine the Japanese system as part of a search for a new Japanese approach to ODA.

That is the purpose of this fourth volume in the *Trends in Development Assistance* series: to analyze international trends, development assistance institutions and important development issues. This book describes and analyzes key modalities — loans, grants and technical assistance — and presents key issues facing the Japanese development community.

Takamasa Akiyama, senior advisor of IDRI, FASID and Yuichi Sasaoka, Professor, Graduate Institute for Policy Studies (GRIPS), are the co-editors. I want to express my gratitude to external contributors to this volume:

Yasutami Shimomura, Professor, Hosei University; Yasuhisa Ojima, Senior Advisor, Planning Division, Department of Development Operations, JBIC; Izumi Ohno, Professor, GRIPS; Koichi Miyoshi, Professor, Ritsumeikan Asia Pacific University; Koji Makino, Director, Human Security Team, Planning and Coordination Department; Yukio Sugano, Professor, GRIPS; and, Mikiko Nishimura, Associate Professor, Kobe University. Each contributor brings valuable insights from the academic as well as the practical perspective. I would also like to convey my appreciation to Hajime Sato, Junko Takeuchi and Nagashige Chou for their translation.

I hope this book will be useful to the on-going reform of ODA system in Japan.

Each chapter reflects the opinion of its author, not of their organizations. Titles are the ones used in the original version.

March, 2006

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Abbreviations and Acronyms

ADB	Asian Development Bank
AFD	Agence Francais de Development
AHSI	Africa Human Security Initiative
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association for South-East Asian Nations
AU	African Union AusAID: Australian Agency for International Development
BHN	Basic Human Needs
BOP	Bottom of Pyramid
BPD	Business Partnership for Development
BRICs	Brazil, Russia, India, China: CAS: Country Assistance Strategy
CDF	Comprehensive Development Framework
CDM	Clean Development Mechanism
CfA	Commission for Africa
CIDA	Canadian International Development Agency
CSR	Corporate Social Responsibility
DAC	Development Assistance Committee
DFID	Department for International Development
EC	European Commission
EFA	Education for All
EFA-FTI	Education for All Fast Track Initiative
EIF	European Investment Fund
E/N	Exchange of Note
EPA	Economic Partnership Agreement
EU	European Union
FAO	Food and Agriculture Organization
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
EU	European Union
GAVI	Global Alliance for Vaccines and Immunization
GDP	Gross Domestic Product
GNI	Gross National Income
GNP	Gross National Product
GTZ	Deutsche Gesellschaft fur Technische Zusammenarbeit
HIPCs	Heavily Indebted Poor Countries
HLF	High Level Forum DAC

IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IDTs	International Development Targets
IFAD	International Fund for Agriculture Development
IFC	International Finance Corporation
IFF	International Finance Facility
IMF	International Monetary Fund
JBIC	Japan Bank for International Cooperation
JICA	Japan International Cooperation Agency
KfW	Kreditanstalt für Wiederaufbau
LDC	Least Developed Countries
LICs	Low Income Countries
LICUS	Low Income Countries under Stress
LMCs	Lower Middle Income Countries
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
MGDs	Millennium Development Goals
MIGA	Multilateral Investment Guarantee Association
MTEF	Middle Term Expenditure Framework
NAFTA	North American Free Trade Agreement
NEPAD	New Partnership for Africa's Development
NGO	Non-Governmental Organization
NORAD	Norwegian Agency for Development Cooperation
NPM	New Public Management
NPO	Non-Profit Organization
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
OECF	Overseas Economic Cooperation Fund
OLS	Ordinary Least Squares
O&M	Operation and Maintenance
OOF	Other Official Fund
OPIC	Overseas Private Investment Corporation
PF	Private Fund
PFI	Private Financial Initiative
PFM	Public Finance Management
PPA	Participatory Poverty Assessment
PPP	Public-Private Partnership
PRBS	Poverty Reduction Budget Support

PRGF	Poverty Reduction and Growth Fund
PRS(P)	Poverty Reduction Strategy (Paper)
PSA	Public Service Agreement
PSD	Private Sector Development Strategy
PVO	Private and Voluntary Organization
RDS	Rural Development Strategy
SAP	Structural Adjustment Program
SIDA	Swedish International Development Agency
SSA	Sub-Saharan Africa
SWAp	Sector Wide Approach
TF	Task Force
TICAD	Tokyo International Conference on African Development
UMCs	Upper Middle Income Countries
UNDP	United Nations Development Program
UNCEF	United Nations Children's Fund
UNESCO	United Nations Educational, Scientific and Cultural Organization
USAID	United States Agency for International Development
UXO	Unexploded Ordinance
WFP	World Food Program
WHO	World Health Organization
WTO	World Trade Organization
ZSP	Priority Solidarity Zones

Recent Trends in International Aid and Their Impact on Japan

Takamasa Akiyama¹

In recent years, major political and economic events have had impact on the global strategies, policies and implementation of international development aid. This chapter reviews and analyzes these events and overviews the current situation. On the basis of that review and analysis, it examines more closely the implications for Japanese aid. As discussed in Akiyama et al. (2003), global trends in foreign assistance are greatly affected by discrete events, the economic climate, development theories and evaluations of aid activities on-the-ground. Furthermore, those factors mutually affect each other, rendering broader aid trends even more complex. Recognizing the complexity, this chapter ventures a first step toward a cinemascopic picture of trends. Section 1 outlines recent international aid trends as understood by the author. Section 2 analyzes political and economic events that have had significant impact on development assistance. Section 3 looks into aid trends related to international conferences and aid literature. Section 4 analyzes recent moves by major donors. Finally, Section 5 examines the implications of these for Japan.

1-1. Outline and background of recent trends in international aid

Perhaps the most important international event in the 1990s was the collapse of the Soviet Union. This had a significant effect on development aid strategies and an immeasurable impact on both political and military fronts. Development aid was distortionary during the Cold War in two ways. Firstly,

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many developing countries adopted the Soviet-style economic model. They did so not only to receive aid from the Soviet Union, but also because the Soviet style centralized political system was convenient for their ruling classes. Secondly, Western donors and the World Bank continued to assist developing countries during this period no matter how undemocratic their governance, so long as they remained in the anti-Soviet camp. Although not the intention, this assistance inequitably supported elites and ultimately delayed necessary institution building and reform. When the political and economic system of the Soviet Union crumbled in the 1990s, the objectives and strategies of United States and other donor foreign assistance lost their mooring.

At the same time, the consensus Western aid strategy seemed to come to a dead end as it became apparent that structural adjustment loans — which had been a main pillar of international aid policy — were not producing good results. The United Nations had until then conceded leadership in aid to the World Bank, but now it urged the aid community to adopt more human-oriented development indices as the drivers of their development assistance strategies. During this period, many important international conferences were convened in such areas as education and health² and there was a movement to elevate social infrastructure building to a main development assistance theme. The OECD adopted these ideas and prepared International Development Targets (IDTs), which would later become the basis for the Millennium Development Goals (MDGs), and advocated that their achievement be the aim of development aid. The World Bank had at this time been advocating a strategy based on economic development and was initially reluctant to adopt the social infrastructure-based approach. Ultimately, however, the Bank gave its support, partly due to strong backing from the UK administration of Prime Minister Tony Blair. An important role in this was played by Clare Short, who became the first Secretary of State for the Department for International Development (DFID). She was an influential advocate of the strategy of IDT achievement through poverty reduction. In this way, poverty reduction strategy emerged as the main driver of global foreign assistance.

To increase international awareness, a goal for the contributions of developed countries was added to the IDTs, which were then adopted by the UN

2. Examples include the International Conference on Population and Development (1994, Cairo), World Conference on Women (1995, Beijing), Social Development Summit (1995, Copenhagen) and World Education Forum (2000, Dakar).

in September 2000 as the MDGs. Recognizing that ODA would have to be increased substantially to achieve the MDGs, the United Nations International Conference on Financing for Development (FfD) was held in Monterrey, Mexico, in March 2002³. At this conference the Western donor countries announced plans for substantial increases in their ODA. Poverty reduction with an emphasis on achieving the MDGs then became the main theme of the aid community. Parallel with this, the fundamental responsibility of developing countries themselves, not their donors, for their development was endorsed. As a result, institutional issues such as governance and fiscal management came to the fore as major challenges.

In the US, which was now the sole economic and military superpower, neither the Clinton nor Bush administrations initially paid much attention to the problems of developing countries. The terrorist attacks of September 11, 2001 changed this. President George W. Bush, who had narrowly won the 2000 election, adopted the persona of “terrorist fighter” and his approval ratings rose dramatically. Recognizing that to fight international terrorism even a superpower needs international support, the US government at this time adopted development as a diplomatic priority to win over the UN and the UK, which regarded it as extremely important. This foreign policy shift may also have been influenced by Prime Minister Blair’s argument that poverty in developing countries breeds terrorism⁴ and by a judgment that help from other developed countries would be needed to rebuild Afghanistan and Iraq. In addition, President Bush may have wanted to display a softer diplomatic side, not only terrorist fighter, but also development advocate.

The 9.11 attacks shocked the US to the core, and the threat of terrorism and violence bore down also on Europe in 2005. Terrorists attacked London during the G8 Summit Meeting in Gleneagles, Scotland. In France, the children of immigrants from its former colonies rioted throughout the country, expressing their discontent over unemployment and other problems and revealing a huge social problem for the French. As a consequence of these events, not only did poverty reduction with a focus on social infrastructure become the dominant international aid trend, but also — for the first time

3. For details, see *Report on Latest Trends in Development Assistance No. 2* (in Japanese) found on the FASID DAKIS website.

4. See Prime Minister Blair’s speech at the Labor Party’s annual conference held in Brighton on October 2, 2001.

since the first oil shock in 1973 — the issue of development came under the spotlight as a major international problem. It is regrettable that development seems to get little attention unless Western society and industrialized economies are threatened by oil shocks and terrorist attacks.

International political and economic events in recent years reflect the progression of globalization, economically, politically and socially. Terrorism is part of that globalization. The problem of development is no longer a problem of faraway, troubled countries. It has now become a domestic problem of donor countries as well. It is safe to say that the links between international issues — including those of developing countries — and domestic issues have strengthened since the new millennium began. The main political issues in the US since the Iraq invasion, for example, have included the pros and cons of the invasion itself, the situation in Afghanistan, the ability of the CIA and other agencies to analyze information accurately, counter-terrorism measures, nuclear proliferation in Iran and North Korea, the federal budget, debt and taxation (significantly related to the invasion of Iraq), soaring energy prices (due to political and social instability in the Middle East and to increased demand from India and other countries), and the trade deficit (largely due to imports from China). Many of these are related directly or indirectly to developing countries. As will be discussed later, the UK recognized the strategic importance of development several years ago and has worked to increase its ODA and enhance related research. The US also has implemented organizational reforms to address issues more efficiently and effectively. The establishment of the Millennium Challenge Account (MCA)⁵ is one tangible example of this.

Since taking the reins of the British government in the late 1990s, the Blair administration has accorded the issue of development a high priority, leading the international aid community in this area. The UK established a poverty reduction strategy focused on the overarching objective of achieving the MDGs, and has been aggressively promoting new ideas such as results orientation, aid coordination and budget support, which have now become mainstays of the international aid community. The UK also urged all donors at the 2005 Gleneagles Summit to increase their ODA substantially.

5. The MCA refers to the new aid program of the US. The MCC (Millennium Challenge Corporation) is a new government agency which administers the MCA.

The centrality of development in the politics and economy of industrialized countries benefits poor countries because it means that rich countries are taking the problem seriously. However, if donor countries insist on putting their own interests first when assisting poor countries, necessary institutional reforms might be delayed and in the long term the development of many countries might be hampered. Such an outcome would lay waste to the lessons learned from the Cold War era. When the Cold War ended in the early 1990s, there was hope that development aid would now be implemented with a clear focus on the developing countries themselves. It seems, however, that the mistakes of the Cold War may still be repeated.

It is also alarming, as Ishikawa (2006) notes, that poverty reduction strategies have not yet produced a definitive development model. The reason why economists have not proposed definitive models may be because poverty reduction strategies, unlike previous strategies, were not formulated by structuralists, that is, by economists who believe in structural adjustments. Without rigorous examination based on sound economic theory, however, this approach might whither. Ishikawa (2006) observes that DFID seems to rely on hope that the “patrimonial political system” will simply collapse as the governments of developing countries adopt poverty reduction strategies. But political systems are deeply rooted in history and culture (North 2005), making it doubtful that political system reform through poverty reduction efforts will be sufficient to put developing countries on a secure path to prosperity.

1-2. Recent factors in international politics and economy that have had impact on development aid

This section lists and attempts to analyze the main political and economic factors of recent years that have had significant impact on international aid trends. These include terrorism, increases in oil and other natural resources prices and the rapid economic development of China and India. In addition to having a direct impact on developing countries, these events also have had significant influence on developed countries. This trend will gain momentum as political and economic globalization continues.

Terrorism

The terrorist attacks of September 2001 in the US not only gave the world a jolt but also caused a fundamental shift in the Bush administration’s foreign

policy. After the attacks, the US took military action in Afghanistan and Iraq. The justification for these interventions and the “war on terror” became the paramount issue for the US, both domestically and diplomatically. Although the war on terror exacerbated the US government’s debt problem, these attacks prompted the government to pay more attention to developing countries and to increase aid that would promote poverty reduction and democratization. Historically, the US has sometimes shown a tendency to draw away from diplomacy and that tendency did resurface after the end of the Cold War. But the globalization of terrorism swallowed the US like a tidal wave and diplomacy became an important part of the country’s political agenda.

The link between terrorism and development aid was dramatically highlighted by the London attacks during the G8 Summit meeting, which was being held in Gleneagles, Scotland. The links are very complicated, however. Many terrorists are Muslim, and as can be judged from the policies of the Taliban in Afghanistan, Al-Qaeda and other terrorist groups, they want to destroy the American cultural system and to be isolated from its influences. The conflict between Israel and Muslim countries and the fact that the world’s largest oil producers are Muslim countries in the Middle East are relevant here, but the connections are vague and subject to interpretation. With these complications, there is a risk that the fight against terror may escalate into a war on natural resources, civilization and religion⁶. During the Cold War, the US tended to categorize other countries by a single criterion: whether they supported the Soviet Union or not. The US seems now to be doing the same thing with a different criterion: whether they support terrorism or not. This is symbolized by its massive economic assistance to Pakistan⁷ and friction with Germany and France, among other things.

The categorization of aid recipient countries by their stance on terrorism is not the only outcome of the emphasis on terrorism. The content of aid has also been influenced. Assistance for building democratic institutions in developing countries is becoming important in policies and programs⁸, a trend which has the potential to undermine the policy of respect for the ownership of developing countries.

6. This impression is reinforced by the uproar in early 2006 caused by a publication in Denmark of a satirical cartoon of Mohammed.

7. In addition to direct instructions from the US, there were instructions through the World Bank and IMF.

8. See US Department of State and USAID (2003).

Energy

The significant increase in international energy prices in 2005 has not only had a direct impact on developing economies but has also affected donor aid policies. Since economic growth requires energy, the rapid increase in oil and other energy prices which began circa 2005 is a serious problem for developing countries. On average, net oil importer countries spend about two percent of their GDP on imported oil, and the total amount in 2003 was about \$80 billion. As the international oil price rose at least by 50% between 2003 and the latter half of 2005, many oil-importing developing countries will have to spend much of the additional ODA they receive to pay for the increased cost of oil⁹. Since the US and China are both major oil importers, securing the oil supply has been a strategic pillar of their foreign policies, and they make a point of providing aid to oil producing countries including those in sub-Saharan Africa (SSA). In light of donor country interests, the oil price trend will continue to have significant effects on ODA as long as the trend remains upward.

One of the best illustrations the difficulties of large-scale projects in the natural resources sector is the Chad Oil Pipeline Project¹⁰. The World Bank was initially reluctant to underwrite this project because of corruption in the Chadian government. It finally agreed to provide financing and guarantees only after the government signed an agreement to spend most of the proceeds from oil exports on poverty reduction measures. Almost immediately, however, the government moved to modify the deal, insisting that it needed the money to suppress antigovernment forces. The Bank suspended at least temporarily its involvement in the project.

It should be noted that price increases of natural resources do not necessarily bring long-term economic benefits even to producer developing countries. In fact, resource revenues tend to contribute to corruption and environmental problems as well as to the so-called “Dutch disease” whereby currency appreciation makes other exports less competitive. The negative correlation between the occurrence of natural resources and economic develop-

9. As the energy efficiency of many developing countries is significantly lower than that of industrialized countries, thought should be given to improving it through aid. This kind of aid will benefit donor countries as well by improving global energy efficiency and reducing global demand for energy, energy prices and pollution.

10. GRIPS/CSIDS (2006a)

ment, termed the “resource curse,” has been proven statistically¹¹.

Rapid growth of China and India

In 2005 China became the third largest economy in terms of GDP. This is the sort of milestone that has attracted attention over the past few years to the economic performances of the large emerging economies referred to as BRICs (Brazil, Russia, India, China). The international political and economic order built by organizations such as the UN, the World Bank and the WTO can no longer be maintained without the two largest BRICs, China and India. These countries have acquired influence with other developing countries as well as with donor countries for a number of reasons. First, the BRICs have a significant impact in the global political and economic arena, affecting trade, investment and international commodity prices. They also provide fresh development and business models based on their comparative advantages in human resources and sometimes their policies of protecting industrial growth. India and China, in particular, have become important export markets for other developing countries. But the picture is not all rosy. While they buy goods from developing countries, they also compete with their producers in the global marketplace. Furthermore, the trade regime strongly advocated by Brazil and other emerging economies in WTO meetings may not be beneficial for the least developed countries (Abe 2005). Additionally, the economic development of the BRICs may contribute to increases in the prices of oil, copper and other primary commodities essential for industrialization; this, in turn, may hinder the industrialization of other developing countries.

China, meanwhile, has begun to provide development assistance to countries in Africa and other regions. However, since China is not a member of the Development Assistance Committee (DAC) of the Organization for Economic Cooperation and Development (OECD), lack of coordination with other donors may become a serious problem. The *Financial Times*¹² points out the importance of understanding that China’s intentions are focused on securing natural resources for itself and that its standards for governance and other issues are quite different from those of Western donors.

11. Sala-i- Martin and Subramanian (2003), Sachs and Warner (2001)

12. *Financial Times* (2006d)

1-3. Trends of international aid found in major international conferences and literature

In 2005 several important development aid-related international conferences were held. These included the OECD/DAC High Level Forum (HLF), the Gleneagles G8 Summit and the United Nations MDG mid-term review meeting. Based on discussions at these meetings, actions by major donors and research papers, this section examines the trends and issues that have drawn attention. Important issues include an emphasis on sub-Saharan Africa, substantially increased ODA, debate on social and economic infrastructure, results orientation, aid coordination, trade and investment and institution building/reform.

Development in sub-Saharan Africa (SSA)

Development in sub-Saharan Africa has been a major issue for the aid community for at least 20 years. More recently there has been a recognition that as India has gotten on track for economic development and as Latin America has made a comeback, SSA is the only region with almost no prospect of development¹³. It is generally understood that the fundamental problem is the lack of institutions that promote development, but how to build such institutions in SSA is not understood (This topic will be discussed in more detail in Chapter 9).

This very problem was a subject of discussion at the 2005 G8 Summit. UK Prime Minister Blair and Chancellor of the Exchequer Gordon Brown addressed the issue of SSA as if they were competing against each other to urge that other donors support Africa more aggressively. Mr. Blair had established the Commission for Africa 18 months earlier partly for the purpose of preparing a paper that would serve as a basis for discussion at the Summit. With broad support from the international community, the 17-member Commission published a 400-page report entitled *Our Common Interest: Report for the Commission for Africa* (Commission for Africa 2005). The United Nations MDG mid-term review meeting of September 2005 also focused on SSA which it evaluated as having the most difficulties in reaching the MDGs. A report prepared by Jeffrey Sachs of Columbia University for the mid-term review meeting (Millennium Project 2005) devoted many pages to

13. Even scholars who have long studied the issue of development in Africa have difficulty identifying the problems. For example, see Collier and Gunnings (1999).

SSA. According to this report, one of the most significant problems in SSA is declining capital accumulation. This means that capital depreciation is greater than investment and the productivity of cropland is declining. The report warns that significant investments are required to reverse this trend.

The World Bank also began to emphasize SSA after Paul Wolfowitz took office as President in May 2005 and it is now more deeply involved with the issues of SSA than before¹⁴. The Bank is set to enhance assistance to SSA as it increases the share of its grant aid. There was also a significant increase in the International Development Association 14th Replenishment (IDA 14). This will be discussed later in more detail. Western European donor countries have been assisting SSA through fiscal support in a major way. In the past few years, they provided fiscal assistance to Uganda and Ethiopia. Now, however, they face severe difficulties coping with the undemocratic behavior of both governments. The examples of these two countries illustrate a problem with fiscal assistance which is directly linked to political agenda¹⁶.

Japan has announced an intention to significantly increase its aid to SSA¹⁷; however, it still lacks a long-term and consistent aid policy towards the region. Presently Japan does not have the institutional capability to provide effective aid to SSA because there are too few Japanese SSA experts. Japan also finds it difficult to provide ODA loans to SSA because of the HIPC (heavily indebted poor countries) Initiative. Japan will host the fourth TICAD (Tokyo International Conference on African Development) in 2008.

Significantly increased ODA

It is widely accepted that ODA must be significantly increased if the MDGs are to be achieved. The World Bank and UN agencies have estimated the funding requirement. Based on those estimates, developing countries have

14. At the G8 meeting, the World Bank strongly resisted the idea of forgiving debts owed it by the least developed countries. The problem was that if this were implemented, the amount of funds returned to the Bank as reflow and used to provide new loans would be significantly reduced. It was finally resolved by an agreement that essentially makes developed countries responsible for bearing that cost.

15. At the G8 meeting, the World Bank strongly resisted the idea of forgiving its debts owed by the least developed countries. What became an issue was that, if this is implemented, the amount of funds that returned to the Bank and then used to provide new loans will be significantly reduced. However, it was resolved by an agreement that essentially makes developed countries responsible to bear that cost.

16. GRIPS/CSIDS (2006b)

17. According to a summary of Prime Minister Koizumi's press conference at the Gleneagles Summit (found on the MOFA's website), he "announced a plan to increase the total amount of ODA by \$10 billion over the next five years and to double the amount of aid to Africa in three years."

insisted that global ODA should be doubled from US\$50 billion (at the time of the FfD Conference) to US\$100 billion. During the 2002 Conference, the majority of the participants agreed that each donor country should set a target of spending 0.7% of GNI for ODA. The US, which before the 9.11 terrorist attacks had been somewhat reluctant to increase its ODA, began to focus on the link between terrorism and poverty in developing countries. Immediately before the FfD Conference, the Bush administration created the MCA and announced a plan to significantly increase aid. The UK and France, partly because many countries in SSA are former colonies, not only declared their intentions to increase ODA but also urged other EU nations, including Germany, to do the same. Germany was hesitant due to fiscal problems, but eventually gave in to the pressure and pledged an increase¹⁸.

This wave of significant ODA increases had a big effect on the World Bank's IDA 14 replenishment as well as on the main agenda of the 2005 G8 Summit¹⁹. Typically the challenge in IDA replenishment negotiations is to persuade reluctant donors to pledge, but in the case of IDA 14, the negotiation took on a quite different tone as the UK and France proposed significant capital increases. In IDA 14 also, the share of the IDA grant facility, established in the IDA 13 negotiations with US backing, was increased from about 20% to 30%, making it more beneficial for the least developed countries.

The Gleneagles G8 Summit emphasis on SSA and the wave of significant ODA increase are connected. The UK, the Gleneagles host, in particular stepped up pressure on other industrialized countries to provide more assistance to Africa, pushing for the 0.7% of GNI goal for ODA and for debt forgiveness by donors, including the international financial institutions. As a result of all this, the amount of global ODA, stagnant until the latter half of the 1990s, has increased since. Countering this international trend, the net amount of Japanese ODA has declined continuously in recent years. While the Japanese government's fiscal problems are a factor, the most significant cause of this decline is increased ODA loan repayments from recipient countries. In FY2004, JBIC's operational budget was ¥700 billion but the net transfer was only ¥288.6 billion²⁰. This elevated level of loan repayment will contin-

18. In early 2006, Germany stated that it could not increase its ODA significantly because of fiscal problems (Financial Times 2006a).

19. For details of the IDA 14, see FASID (2005).

20. Nakao (2005)

ue for at least a few more years, so that a significant increase in gross ODA is required to stop the decline on a net basis. With the UK, France and Germany increasing their ODA significantly, Japan may soon end up in fifth place in world ODA rankings.

There was an earlier period, in the 1960s and 1970s, when the amount of ODA was increased significantly. At that time, developing countries in UNCTAD and other fora insisted on the increase based on the concept of the New International Economic Order (NIEO). What is different about the current movement is that Western countries, such as the UK, also are calling for increases. The aid community learned throughout the 1980s and 1990s that — as the institutional school insists — policies and institutions of developing countries must be changed and made development-friendly. The UK seems to believe that to do this what is needed is funds to implement accumulated research findings on the mechanism of development; this view, however, may be too optimistic. Some scholars, in fact, are critical of the recent increase in the amount of ODA²¹.

Social and economic infrastructure

As explained above, the poverty reduction strategy approach — oriented toward achieving the MDGs and building social infrastructure in line with Poverty Reduction Strategy Papers (PRSPs) — became a dominant trend because the UK and other countries strongly promoted it and convinced UN agencies, including the UNDP, and the World Bank of its merit. The UK and other Western European countries seek to build social infrastructure and emphasize achievement of poverty reduction based on the following rationale:

- (1) The medical, educational and gender conditions in the least developed countries are very bad, a situation which needs to be addressed from a humanitarian perspective.
- (2) Development will remain difficult until these conditions have improved.
- (3) Changes in social infrastructure are relatively easy for the citizens of donor countries to see, making it easier to solicit their support (i.e., public relations through the mass media becomes easier).
- (4) Western European countries are situated much closer to SSA than is

21. For example, Rajan and Subramanian (2005a), (2005b), Birdsall, Rodrik and Subramanian (2005) mentioned in the DAKIS Literature Introduction No. 55, which can be found on the FASID website.

Japan or the US so that their social problems are more readily linked to problems in Africa, such as illegal immigration, drugs and terrorism.

- (5) The past experience of most donors indicates that governments of developing countries are not trustworthy, thus ODA should be provided in such a way that it most directly benefits the poor.
- (6) If governments are encouraged to implement policies and spending measures that benefit the poor, they become accountable to the majority, not just to the few elite, effectively making them more democratic.

From a different perspective, India and China have pointed out that donors overemphasize social infrastructure to the neglect of economic infrastructure. As a response to this view, the World Bank shifted somewhat back to an emphasis on economic infrastructure (Fay and Yepes 2003). However, none of the MDGs are directly related to economic development, and PRSPs, as the name suggests, are plans for reducing poverty in a particular country²². When this strategy is applied to the least developed countries — in SSA and elsewhere — the HIPC Initiative in particular makes it difficult to build economic infrastructure because they often require loans.

Potential non-loan funding sources include the International Finance Facility (IFF), the MCA (infrastructure building is possible because the aid amount for one project is large), and IDA grants and fiscal assistance contributions. Useful loan resources include the IDA and the European Investment Fund (EIF)²³. The Japanese government appears also to be considering offering ODA loans to several SSA countries in conjunction with the African Development Bank and other donors.

Results orientation

Reflection on past experiences has given rise to a new aid methodology: deadlines and concrete goals are clearly defined and the effects of aid are monitored and evaluated against them. This marks an application to aid of the New Public Management (NPM) methodology used by the UK and other countries to evaluate the activities of government agencies. This methodolo-

22. Second generation PRSPs are beginning to emphasize growth as well. For details, see Chapter 9 of this volume.

23. The EIF announced that it would begin to provide loans to developing countries in the summer of 2006 (GRIPS/CSIDD (2006b)).

gy was incorporated into the PRSP approach of the late 1990s as well as into the MDGs adopted in 2000. NPM establishes concrete goals for the government and other public institutions whose objectives and activities are often ambiguous and difficult to evaluate. It then seeks to clarify to the extent possible how these goals affect achievement and to measure cost effectiveness. This approach also addresses criticism that the achievements of past foreign aid are unclear and the feeling among donors that their efforts may have been in vain (“aid fatigue”).

This methodology — establishing measurable goals and achieving them within a pre-determined time frame — presents its own problems. Many development issues — for example, building and reforming institutions — are complex, not readily reduced to simple indicators. There is a concern, also, that assistance may be unduly directed toward areas where indicators are more easily established. The UK and others argue that all assistance should contribute to the achievement of the MDGs and that all aid activities should be evaluated in terms of their contribution to this overarching objective. Their basic aid philosophy reflects the following two positions: First, the purpose of aid should be to help developing countries rather than for the political or economic gain of donors. Second, evaluation of individual projects should not be conducted in isolation, their macro-level impacts should also be considered.

The first position relates to the quality of aid. ActionAid, an influential British NGO, discussed this in its June 2005 publication *Real Aid* (ActionAid 2005). *Real Aid* points out that currently more than half of all assistance goes directly to the political or economic gain of donor countries and their citizens. This is largely because consultants from developed countries implement many projects. Unfortunately, their contributions to the economic development and poverty reduction of developing countries are small. This situation is also mentioned in the Millennium Project Report by Jeffrey Sachs (Millennium Project 2005). DFID and OECD/DAC have disputed this claim, but it highlights various problems with foreign assistance and cannot be ignored.

The second position is an argument that ODA should be evaluated by whether the developing country has achieved economic growth and poverty reduction, not by the success or failure of individual projects. Western

European countries, the UN and the World Bank have come to accept British ODA strategy. The US, however, has not entirely agreed because the main objectives of its foreign assistance are different from those of other donors.

Aid coordination

Aid coordination was first advocated by James Wolfensohn, the former President of the World Bank. He was surprised when he took office at the lack of collaboration among the World Bank and the regional development banks: the Asian Development Bank (ADB), the Inter American Development Bank (IADB) and the African Development Bank (AfDB). To correct this, the World Bank introduced the Comprehensive Development Framework (CDF) — reportedly created by Mr. Wolfensohn, himself — as a mechanism to facilitate coordination among donors. The PRSP approach was established along a similar line of thinking and donor coordination gradually improved. With regard to harmonization of procedures, High Level Forums were held in Rome in 2002 and in Paris in 2005. The Paris HLF adopted 12 measurable goals for harmonization and participating donors approved a target of achieving five of them by 2010. This is another example of donors agreeing to reach numerical targets within a specified timeframe; i.e., the NPM methodology.

Few were opposed to the concept of aid coordination. However, when aid organizations try to actually coordinate their work, more meetings are required among donors and between donors and recipient governments, leading to increased transaction costs instead of reduced ones. This is a particular problem for Japan, which has relatively few aid professionals stationed in recipient countries²⁴.

Trade and investment

After the adoption of the MDGs in 2000, the idea of promoting development through social infrastructure building became dominant in the aid community. Nonetheless, it remained true that without concomitant economic development, cash-strapped developing countries would not be able to operate and maintain (O&M) the medical and educational facilities built with the help of ODA. The Japanese government's position is that social infrastructure built with ODA cannot be maintained if government revenue is not generated

24. This point is also discussed in Chapter 2.

through economic growth²⁵.

In East and Southeast Asian countries, poverty reduction and economic development were achieved simultaneously. These countries followed a pattern whereby exports and foreign direct investment (FDI) increased as the private sector was developed. Japanese ODA has been aimed at promoting such exports and FDI. In the last few years the World Bank also has begun to emphasize the promotion of the private sector and it has created indicators environment for private sector development that it publishes annually. These indicators allow objective evaluation of investment climates in developing countries and help those countries understand what they must do to nurture and promote their private sectors. This is a positive step for development assistance.

With regard to trade, the still uncompleted Doha Round of negotiations is not going well. Unlike the situation a few decades ago, many developing countries are now members of the WTO and it has become much more difficult to build a trade regime on which all members can agree. One major problem in the Doha Round is liberalization of agricultural products by industrialized countries. Even if the liberalization occurs, however, most of the benefit would flow to countries whose large scale farms are managed efficiently such as the US, Australia and Brazil. Many least developed countries including those in SSA would actually be expected to lose market shares (Abe 2005). In addition, global trade liberalization would strip the least developed countries of the preferential treatment they now receive. Furthermore, it would become more difficult to adopt such industrial protection policies as East Asian countries were able to use under current WTO provisions.

If the Doha Round fails, there will be more proliferation of bilateral trade agreements, such as free trade agreements (FTAs) and economic partnership agreements (EPAs), favored by the developed and semi-developed countries. The concern is that as this happens the export markets of many developing countries, including least developed countries, will shrink because they are seldom involved in these agreements (Abe 2005).

25. UNCTAD (2004) suggests that it also has a similar stance.

Institution building and institutional reform

The main theme of development has changed over time. It was economic infrastructure until the 1970s and then structural reform from the early 1980s to the early 1990s. Thereafter, poverty reduction took over. Recently the role of institutions, as explained by North and Stiglitz, is attracting considerable attention. (This may be due partially to these academics' status as Nobel laureates.) Categories of institutions are many and very diverse, covering politics, the economy, commerce, justice and civil society. The scope and policy measures related to institution building and institutional reform are quite different from donor to donor. The World Bank focuses on anticorruption and improving laws related to the economy, such as foreign trade laws, financial laws and commercial laws. The US concentrates its efforts on building institutions that contribute to the democratization of developing countries rather than on economic institutions. The core of the British strategy is achieving the MDGs and the British government is significantly increasing its investment in fiscal assistance. The UK is pressuring developing country governments to allocate their budgetary maximums to activities that benefit the poor, such as health care and education, and is trying to establish pro-poor political systems. The World Bank and the UK's DFID also seem to be trying to reform public finance management systems through fiscal assistance²⁶.

Poverty reduction — the current focus of the aid community — is closely related to the issue of political systems. As Bates (1981) and others point out, the governments of many developing countries give preferential treatment to their elite including the military, for political purposes, paying little attention to the general public including the poor. Since 1980, the World Bank and others have tried to change this attitude through structural adjustment loans, but the impact of their efforts has been limited due partly to conflict with “ownership.” As now conceived, it is essential that a poverty reduction strategy be “owned” by its government; that is, the government itself must generate and implement policies and allocate budgetary resources to activities that reduce poverty. Since the majority of citizens in least developed countries are poor, a government that adopts policies targeting poverty is defined as democratic regardless of other policy attitudes. The UK is one donor providing fiscal assistance to induce governments to adopt pro-poor policies. While the concept of ownership is accepted, the definition of the term and how it

26. Ishikawa (2003)

should be used is unclear²⁷. Is ownership at play when donors decide that ODA will be provided only when the government of a developing country proposes an agreeable set of policies? Is it ownership when, as now, donors seem to undertake quite rigorous monitoring and evaluation²⁸? While the inferred intent of a recipient country government is currently an accepted indication of ownership, how does this work in the case of a blatantly undemocratic government? With such unanswered questions, ownership by recipient countries is rife with ambiguity.

PRSPs have been prepared by many least developed countries. One of the important factors in the PRSP preparation process is the participation of as many stakeholders as possible. So far, the participants in PRSP consultations have come mainly from civil society groups. Driscoll and Evans (2004) say that a future challenge is to promote wider participation by the poor themselves.

IDA and MCA allocate their aid resources based mainly on governance indicators established with regard to institutions, policies and corruption. Again, this is a methodology that works smoothly only if it is compatible with the national interests of the donor. Debate on aid to Kenya, which was featured in the pages of the *Financial Times* (FT) in February 2006, clearly shows the difficulty of this problem. The debate started when Michael Holman, former FT Africa Editor, asked why the World Bank and DFID continue to provide aid to Kenya in the face of the government's rampant corruption. Answering his own question, Holman suggested that the US government pressured the Bank and other donors because the Kenyan government was cooperating in the war on terror (Financial Times 2006b). Jeffrey Sachs of Columbia University and Hilary Benn, the current British Secretary of State for International Development, countered this suggestion on the same pages by arguing that even corruption is no justification for ignoring the poor and furthermore that their aid reaches the poor directly (Financial Times 2006c).

Many donors argue that a democratic political system is essential for a developing country to succeed²⁹, but an interesting analysis of aid and institu-

27. Buiter (2005)

28. The NPM is becoming popular in donor countries as well, requiring stronger accountability from aid agencies.

tions published by Moss, Pettersson, and Walle (2006) questions this. According to their analysis, as the share of received aid in GDP increases and the share of tax revenue decreases, a government may become less accountable to its citizens and more accountable to its donors. In such cases, the government will blame failure of development efforts on insufficient aid quantity to avoid the politically difficult act of increasing taxes. This places the government in a systemic fiscal dependency on aid and suggests, in effect, that massive amounts of aid may actually work against the establishment of sound and democratic political and fiscal systems. At a time when aid to SSA is about to be increased substantially, attention should be paid to this scenario.

The International Monetary Fund (IMF) has found interesting results through statistical analyses of the factors of institutional changes in aid recipient countries³⁰. IMF analysts selected for their sample developing countries that had experienced significant changes in institutional indicators and conducted regression analyses on them using various explanatory variables. Their results show that institutional indicators improved in those countries where market-oriented economic reform had taken place, political accountability had been established, citizens were better educated, and neighboring countries had better institutions. However, they could find no correlation between aid itself and institutional improvements.

While the importance of institutions in development is recognized, it is not well understood and exactly what should be done to build them or how remains unclear.

1-4. Recent moves by major donors

This section provides an overview of recent moves by major donors: namely the World Bank, the US and the UK. The World Bank focus is on the possibility of a strategic shift due to the change in top management. For the US, the focus is on the development of aid strategies after 9.11. With regard to the UK, at the focus is on its achievements during the 2005 G8 Summit and its moves thereafter.

29. A summary can be found on the website of the GRIPS/CSIDS (www.grips.ac.jp/CSIDS/Index.html).

30. IMF (2005)

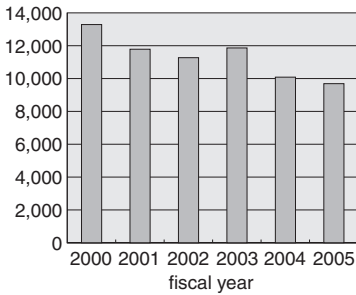
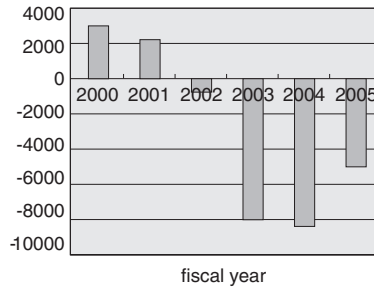
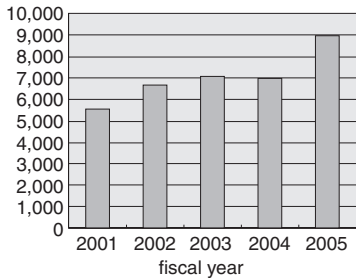
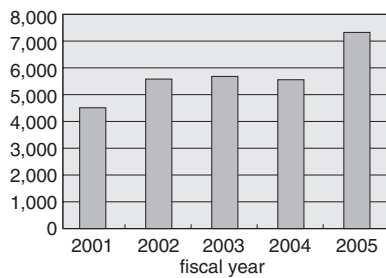
The World Bank

In May 2005, former US Deputy Secretary of Defense Paul Wolfowitz took over the post of President of the World Bank. When his predecessor President James Wolfensohn took office a decade earlier in 1995, he immediately declared that the Bank was in a crisis, advocated an organizational reform, introduced the CDF and strongly urged developing countries to prepare PRSPs. Mr. Wolfowitz has not displayed any dramatic initiatives or theatrics of this kind. One suggested explanation is the aid community's unease over his involvement in the invasion of Iraq and his strong ties with the Bush administration. It seems also that Mr. Wolfowitz decided to give himself time to study the lay of the land, since he had never been directly involved with issues of development and international finance. His arrival did prompt significant personnel change, however. Many managerial staff left the Bank and others who were trusted by Mr. Wolfowitz — mainly from his former US government staff — began to take their positions. This created friction between the existing staff and the newcomers³¹.

Considering that with the exception of Messrs. McNamara and Wolfensohn past Bank Presidents kept rather low profiles, it may be reasonable to expect that Mr. Wolfowitz will not pursue drastic changes in the organization or in aid modalities. On the other hand, the very high profile James Wolfensohn brought change to critical areas of the Bank. While his tireless efforts to make the Bank relevant were boosted by the 9.11 terrorist attacks and the hard work of the UK, it is important to remain mindful that development assistance tends to shrink when it is out of the spotlight because it has few direct beneficiaries in donor countries.

After taking office, President Wolfowitz delivered speeches in several countries including Japan. The contents of those speeches did not disclose whether or not he held strong beliefs with regard to development or Bank strategies. His topics generally covered such issues as SSA, enhanced infrastructure building, private sector development and the importance of trade and rural development; but these were nothing new. As discussed above, the problem of SSA is the subject of much advocacy by the UK and by UN agencies in conjunction with the MDGs. Other challenges are probably based on a reflection that the aid community including the Bank placed too much

31. GRIPS/CSIDS (2006c)

Figure 1-1. Gross Disbursement**Figure 1-2. net disbursement****Figure 1-3. Gross Disbursement
(million dollars)****Figure 1-4. net disbursement
(million dollars)**

Source: World Bank (2005c)

emphasis on social infrastructure. This reactionary move may represent the will of senior officers of the Bank who did not agree with the policies of Mr. Wolfensohn but could not openly criticize him. They might be hoping to use the change in top management to shift the Bank's focus back to economic development and economic infrastructure building. One of the factors that contribute to this sort of policy shifts is perhaps the recent trend in the net amount of the World Bank's loans.

As is evident in Figures 1-1 through 1-4, the gross disbursement of the IBRD (International Bank for Reconstruction and Development), at one time the most important branch of the World Bank Group, has been declining in recent years. The net disbursement has been negative since FY2002, and the net negative flow in FY2003 and FY2004 was a massive US\$8 billion. Both the gross and net disbursements of the IDA, by contrast, have been increasing. At the beginning of FY2000, IDA's gross disbursement was about half that of IBRD; for FY2005 it was about the same; for FY2006 IDA gross disbursement

was expected to surpass that of IBRD.

The IDA disbursement amount is increasing in the context of increased aid to SSA. Since many of the SSA countries are in the least developed country category and most of the least development countries are in sub-Saharan Africa, the vast majority of the World Bank's loans to that region are provided by IDA³². This means that if IDA resources are increased, loans and grants to SSA will automatically be increased. For these reasons, the IDA 14 replenishment was expected to be 30% larger than the IDA 13. Sources of IDA funds include contributions from donor countries, loan repayments and net profit transfers from IBRD. Donor contributions will be increased by 25%. European donors in particular have increased their contributions substantially. For IDA 14, Sweden is contributing about 220% of what it did for IDA 13. France and Spain are increasing contributions by 70%, while the UK is increasing its contribution by 83%. This has raised the British ranking in both total amount and share from fourth place to second place, surpassing both Germany and Japan. The US was the only country whose contribution to IDA decreased, by 14%. The US is still the number one donor in terms of share in total amount, but its share has declined significantly from just over 20% in IDA 13 to slightly under 14%. Japan barely managed to increase its contribution, by 8%.

In the negotiations for the IDA 13 replenishment, the US and Western European countries were at odds over whether or not IDA should provide grant assistance. The UK was particularly concerned that grants requiring no repayment would lead to a reduction in IDA resources and maintained that the World Bank should always remain a provider of loans. For IDA 14, however, Western European donors did not object to increasing the share of grants in IDA financing because they had to frontload ODA to achieve the MDGs.

Another feature of IDA 14 was the adoption of a grant allocation method based on recipient debt risk. In other words, to provide aid more efficiently, grants were given in consideration of recipient countries' ability or potential to meet debt obligations. In order to provide needs-based grants, the Bank and IMF jointly proposed a framework for measuring the debt distress levels

32. In the past few years, more than 95% of the Bank's financing for SSA has come from the IDA. In FY2005, 45% of the total IDA financing went to SSA. (World Bank 2005)

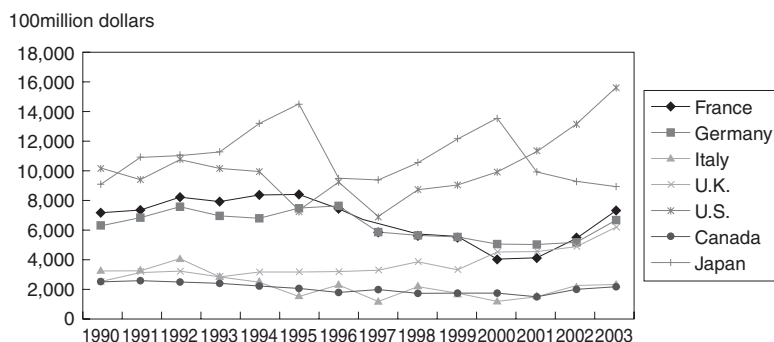
of IDA beneficiaries. In this framework, debt distress levels are categorized as low, moderate and high. Assistance to countries in the “low” category would be 100% loans, for the “moderate” category it would be half loans and half grants, and for the “high” category it would be 100% grants. This system is designed to prevent the debt of IDA recipients from accumulating to unsustainable levels. With the adoption of this allocation method, about 50 countries became eligible to receive IDA 14 grants.

The World Bank has a large body of publications and databases which are widely used by the aid community. A few of them are commented below. The Bank has always emphasized private sector development. Since 2004, the Bank and its private sector arm, the International Finance Corporation (IFC), have been publishing global business environment data on the Web under the rubric “Investment Climate Indicators” and in print through the “Doing Business” surveys. Indicators of policy, corruption, the judiciary, crime, regulations and tax systems, finance, electricity and labor are derived from raw data obtained from more than 26,000 companies in more than 50 developing countries. The *World Development Report 2005* (World Bank 2005a) also emphasized the importance of investments for growth and poverty reduction in developing countries and analyzed the relationship between the indicators and development. A lot of financial, human, tangible and intangible resources are required to create these databases, so that they reflect the importance the Bank places on this information.

As aid to SSA was attracting attention, the World Bank also declared a focus on Africa in September 2005 by publishing the *Africa Action Plan* (World Bank 2005b) which set forth the Bank’s comprehensive aid policy for the region. The Action Plan assumed substantially increased aid to SSA over the next few years and stated that the Bank would take the lead in supporting Africa³³. The Plan also emphasized the importance of achieving the MDGs, the PRSPs, infrastructure, results orientation and the evaluation methods for it.

The aid trends of major bilateral donors are examined below. Figure 1-5 shows the net amount of bilateral ODA by major donors since 1990. According to Figure 1-5, the US, UK and France have increased their ODA

33. On the other hand, the EU insists that it will provide aid to SSA without going through the World Bank. (GRIPS/CSIDS 2006b)

Figure 1-5. Transito of ODA disbursements among DAC major countries

Source: MOFA (2004)

substantially over the last few years. Japan's reduction of ODA since 2000 stands out by contrast. This trend is expected to continue for some years, so that by FY2008 Japan may descend to fifth place in the ranking of bilateral donors after the US, UK, France and Germany.

The United States

After the 9.11 terrorist attacks, the Bush administration made eradication of terrorism its highest policy priority. The Millennium Challenge Corporation (MCC) was established as a major development aid agency — separate from USAID and the Department of State — to manage the newly created Millennium Challenge Account (MCA). It was charged with providing aid in the order of US\$50 billion³⁴. This would have increased American ODA by 50%, but the Congress has been reluctant to approve such an increase in view of the federal deficit problem. The establishment of the MCA was said to have been proposed by Secretary of State Condoleezza Rice in her previous role as National Security Advisor.

Learning from the bitter experience of USAID, the MCC has adopted an entirely new aid method. The MCA seems to have been built as a mechanism for selecting countries with high potential for growth and supporting their development. While its features are many and varied, the most important ones are as follows.

(1) The basic stance of MCA assistance is characterized as poverty reduc-

34. See DAKIS Report on Latest Trends in Development Assistance No.18, which can be found on the FASID website.

tion through economic growth. The focus areas include agriculture, education, private sector development and capacity building.

- (2) Using indicators for governance, market-oriented economic policies and other factors, countries are selected to receive focused grant assistance based on their performance.
- (3) Recipient countries plan how to use MCA aid and submit their proposals to the MCC.
- (4) The MCA supports activities whose results can be clearly evaluated.

Underlying the establishment of the MCA were the following factors and judgments: Firstly, it is difficult for USAID to implement the policies and goals of the executive branch due to extensive Congressional interference; Secondly, ODA will be more efficient divided into two categories: one in line with the US foreign policy or national interests, the other aiming for the development of poorer countries ; Thirdly, there is a need to establish a new method that maximizes the efficiency and achievements of aid. These three points are explained in brief.

USAID was understandably opposed to the creation of a major new aid agency. When USAID was first established by President Kennedy in 1961, Congress did not interfere with it excessively. But over the course of more than 4 decades, various regulations came to be imposed on it. In the words of former USAID Administrator Andrew Natsios who resigned at the end of 2005, most of USAID's budgets are regulated or earmarked by Congress, staff moral is low, and the budget is not used effectively³⁵. These facts are well-known in the US aid community, and many lawmakers admitted as much when they approved the establishment of the MCA.

The administration of George Bush came to see development aid as an important part of its fight against terror. This prompted a decision to strengthen coordination between USAID — which had problems as described by Mr. Natsios — and the State Department, and to provide assistance aligned to US national interests. In January 2006, on the departure from USAID of Mr. Natsios, Randall L. Tobias³⁶ assumed a newly created post of Director of United States Foreign Assistance with the rank of Ambassador

35. GRIPS/CSIDS (2005)

36. Before joining the US government, he worked for AT&T (a US telecommunication company) and Eli Lilly (a pharmaceutical company).

reporting directly to the Secretary of State. He was also appointed to serve concurrently as USAID Administrator. He is expected to be in charge of foreign aid policies throughout the entire US government. Mr. Tobias formerly served as US Global AIDS Coordinator.

The system of development assistance in the US was also enhanced by President Bush's announced intention, in December 2005, to strengthen the political management of ODA³⁷ and the unveiling by Secretary of State Rice of a new concept, "Transformational Diplomacy"³⁸. Transformational Diplomacy means that US diplomats will work together with foreign citizens, assist in the democratization of developing countries such as China, India and Nigeria and promote antiterrorism activities. This is also an acknowledgement that the previous allocation of human resources to US diplomacy and defense, designed during the Cold War, was not suited to the realities of the modern world where the importance of developing countries is growing.

USAID is displaying some confusion about the division of roles between it and the MCC but one of its important tasks is to fight terrorism by promoting the democratization of developing countries — especially the so-called fragile or failed states³⁹. It seems that USAID will provide assistance to countries with many serious problems that prevent them from meeting MCA standards. In other words, the USAID will handle the major challenge of dealing with problematic countries that the MCC cannot handle. Congressional interference is unlikely to be reduced.

The United Kingdom

In recent years, the UK has played a leading role in the aid community, not only by increasing its ODA rapidly, but also by advocating the importance of aid designed to achieve concrete results, such as the MDGs. At the 2005 G8 Summit, which it hosted, the UK indicated that it considered the issue of SSA and other developing countries to be the greatest challenge of its foreign policy. Prime Minister Blair himself took initiative in organizing the Commission for Africa and publishing its hefty report. Chancellor Brown — the number two in the Blair administration — established the IFF and advocated the front-loading of ODA. The 2005 G8 Summit itself suffered a loss of

37. GRIPS/CSIDS (2005)

38. GRIPS/CSIDS (2006b)

39. USAID (2005)

global attention due to the concurrent terrorist attacks in London, but the pressure that the British government put on other donors to increase ODA was considerable.

Following are reasons why the UK has such a strong interest in developing countries.

- (1) The Labor Party took power in 1997 and has been working since to strengthen the UK social security system as a policy priority. This strategy has affected the government's stance toward developing countries⁴⁰.
- (2) Politically influential Ms. Clare Short became the first Secretary of State in charge of DFID and advocated both at home and abroad the importance of reducing poverty in developing countries. Her policy had an effect on both Prime Minister Blair and Chancellor Brown.
- (3) The UK places special importance on reducing poverty in South Asia and SSA. Many countries in these regions are former British colonies and the UK has a sense of guilt toward them. Also, these countries kept close ties with the UK after independence and their poverty-associated problems are recognized by many British politicians and bureaucrats.
- (4) The British government recognizes that poverty in SSA, which is geographically close, might breed terrorism and illegal immigrants.
- (5) Many celebrities, including rock stars, support and cooperate with the government in publicizing development policies. The general public also supports the government's policies.
- (6) With cooperation from universities and research institutes⁴¹, the government is promoting research on development aid theories and stressing to both domestic and foreign agencies and to media organizations the importance of the development issue.

In addition to these factors connected with the Blair government, the NPM method and merit system adopted by the Thatcher administration for all government agencies caused DFID officials to work very hard — too aggressively to some — to persuade international organizations and other donors. The DFID operational plan is clearly stated in its Public Service Agreement (PSA)⁴², which each department signs with the Treasury on a

40. Ishikawa (2006)

41. The Overseas Development Institute (ODI) is especially influential.

three year cycle. Six objectives are stated in the 2005-08 PSA: (1) Reduce poverty in Sub-Saharan Africa; (2) Reduce poverty in Asia; (3) Reduce poverty in Europe, Central Asia, Latin America, the Caribbean, the Middle East and North Africa; (4) Increase the impact of the international system on reducing poverty, preventing conflict and responding effectively to conflict and humanitarian crises; (5) Develop, support and promote policy that assists poverty reduction and the achievement of the MDGs; and (6) Improve the impact and effectiveness of DFID's bilateral programs. Each objective contains several concrete targets and indicators. These objectives, targets and indicators are evaluated semiannually and more detailed evaluations are conducted triennially.

One of the features of the UK aid system is that there are concrete action plans, an organizational structure to implement them and a system to evaluate them. Another feature is a results orientation: For countries on which the British aid has an impact, development indicators are included in DFID's objectives and targets and the department must show improvements in these indicators. As can be seen in the PSA, DFID is likely to become the lead donor in the developing countries that it focuses on, promoting the achievement of development targets such as the MDGs and acting as the linchpin of aid coordination. It is vigorously requesting the World Bank, the UN agencies and the EU to cooperate with its aid strategy. In other words, DFID's development goals for these countries do not mean simply that the British aid will be implemented effectively; it means that all donors and the recipient country will work together to achieve the same development goals.

1-5. Implications for Japan of recent trends

As explained above, international economy and politics have seen dramatic changes over recent years. Reflecting these changes, the development assistance programs of major donors are changing, not only in terms of strategies, policies and methods but also their positioning vis-à-vis donors' diplomacy and national interests. In Japan, serious ODA discussions began at the end of 2005, partly in the context of reform of government-affiliated financial institutions including JBIC. The discussions are proceeding under the slogans "aid with a human face" and "spread the experience of Japan and Asia to the

42. DFID (2005)

world.” At several venues, including the G8 Summit, UN conferences and WTO meetings, the government has announced various initiatives and plans to increase ODA. Despite this, it does not seem to have attracted much attention, even that of developing countries. The best explanation for this is probably that internally Japan is finding it difficult to formulate and launch coherent strategies and policies that satisfy the diverse interests of all the ministries involved in ODA.

As of early 2006, a plan was under consideration to create a new council of ministers within the cabinet to prepare a comprehensive aid strategy under political leadership. With regard to implementing agencies, too, the former OECF portion from JBIC would be integrated with JICA and add the grant assistance function which is currently administered by the Ministry of Foreign Affairs (MOFA). These moves were welcomed as motivated by a desire to improve the Japanese ODA structure, but the details are critically important. Construction of a new system must be considered both cautiously and boldly.

The theme of this chapter is the reality that development assistance has ceased to be a problem of far-away, low-income countries. It has become a very complex matter, entangled with issues of security, terrorism, natural resources, environment and trade. It is now linked with almost all the external and domestic issues of donor countries. When this reality is understood, the need for drastic alternation in the way aid is handled becomes clear. Until now, Japan has been rather passive in this regard. As the request-basis principle illustrates, Japan has reacted to challenges posed by other donors and developing countries. That approach is no longer suitable for a Japan that promises “aid with a human face” and “dissemination of information from Japan.”

It is still unclear how Japan’s aid system will change as a result of the organizational reforms under consideration. It is important to recognize that what has been lacking is an apparatus that systematically analyzes international affairs, conducts studies and research on development and formulates aid strategies and policies. Although it would be difficult to create such an apparatus within an existing ministry, it is urgently needed. Flaws in the current system compromise continuity and scale, resulting in inefficiencies. MOFA, JICA and JBIC have all preferred to outsource studies and research

activities and to minimize internal contributions. This has meant that knowledge, information, and analytical capacities do not accumulate as institutional memory. A related problem is that officials in ODA-related ministries and agencies change posts every few years. Improvement in scale can be expected following organizational reform, but a critical mass of human resources is necessary to conduct studies and research that are worthy of international dissemination. It has been impossible for the few experienced Japanese ODA researchers to accumulate such research findings. Japan's fiscal deficit problem also impinges on this issue⁴³. But it will be a bad bargain if fiscal deficit considerations result in the simplification or abandonment of in-depth research on development and aid. The complexity of development is now widely acknowledged. To use aid wisely, it is essential to investigate this complexity, including the impact of its institutional and organizational aspects.

Concluding this chapter, points of consideration are enumerated for improving the efficiency and effectiveness of development research and of studies on aid strategies and policies:

- (1) Create groups to conduct comprehensive analyses of strategies, policies and information regarding development aid. As the links between development and other diplomatic issues and domestic issues have strengthened, the need to analyze these links consistently and regularly has increased also. Relevant study topics would include: (a) Moves by major donors and recipient countries; (b) Reviews of domestic and foreign research and studies; (c) Examination of Japan's comparative advantages in implementing ODA; (d) Status of the world's natural resources including oil; (e) Issues related to trade and FDI including FTAs and the WTO; (f) Issues of security including terrorism.
- (2) Focus strategic research on important recipient countries and sectors. Because of the importance to development of institutions in the broad sense, an interdisciplinary approach to development is needed. The major work *Development Study on Assisting Vietnam in a Transition to Market Economy*⁴⁵, conducted in the late 1990s, may have taken a long time and cost a lot of money to complete, but its benefits are signifi-

43. For example, see MOFA (2005).

44. For example, see MOFA (2005).

45. See Ishikawa (2006) Chapter 5.

cant and it is an important asset for both Japan and recipient countries. For smaller-scale studies, research similar to the World Bank's economic and sector work (ESW) on development in individual countries is certainly feasible. Focused strategic research on important recipient countries and sectors would contribute much to the international community.

- (3) Establish ODA Task Force Support Units. The role and importance of local ODA task forces are likely to grow. Support systems such as remote seminars are being developed but Tokyo needs to provide more support to strengthen local capabilities. The World Bank already is strengthening its local systems. Sector and theme specialists work at headquarters and support local staff as the need arises. It would be beneficial also for Japan to create mobile units constituted by specialists in important sectors to respond to requests from local task forces. The capabilities of sector specialists in JICA and the Economic Cooperation Bureau of MOFA should be up-graded so they can serve as the foundation of a more permanent, all-Japan support system.
- (4) Attend to long-term human resource development. In recent years the training and education of aid specialists and students in Japan has deepened, but many of these people remain unsure what specific skills are required of them, making it very difficult for them to get jobs in the field of development and international assistance. Those who leave international organizations or consulting firms in their 30s or 40s find limited opportunities to use their skills. At the same time, many of the areas of specialized knowledge related to development are constantly evolving so there is a constant demand for competent specialists. There is, in effect, a mismatch between the demand and supply of human resources. To eliminate this mismatch, better communication is needed among ODA ministries, implementing agencies, universities and private consulting firms so that training and education will be more aligned with the needs of employers.
- (5) Enhance collaboration with the private sector. Chapter 8 will discuss the involvement of the Japanese private sector in assisting developing countries, an involvement that has been quite limited. In view of the fact that a flourishing private sector was a vital factor in Japan's own economic development, the importance of constructing a system which deepens and encourages the involvement of the private sector

in other countries' development is clear.

One last important note: To be serious about disseminating information from Japan to the world, studies and research papers by government-affiliated agencies must be written in English.

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Rediscovering the Role for Japan

‘Counterforce’ against the ‘Negative Side’ of the Trends in International Aid

Yasutami Shimomura¹

2-1. Objective of this chapter²

2-1-1 Japan’s role in the international aid community

The objective of this chapter is to redefine a role for Japan in the international aid community. This community includes international organizations, governments of industrialized countries, researchers, opinion leaders, and international NGOs that play central roles in helping developing countries and leading international discussion about how aid should be designed and implemented. While recognizing the value of new ideas, strategies, and approaches that have been proposed by the international aid community and are now dominant trends, a *negative side* tends to be overlooked. I recommend that Japan not only promote these new trends but also discuss problems of this negative side and propose countermeasures. Japan should become a counterforce against the negative side. No country is currently playing this role, but it is an important one that will help prevent negative effects for developing countries.

2-1-2 New aid trends

As discussed in Chapter 1, the challenges facing the international aid community have become more diverse, complex, and difficult amidst criticism that aid for developing countries has not produced satisfactory results. This frustration, along with financial difficulties experienced by major donor coun-

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2. I would like to thank Professor Izumi Ohno of the National Graduate Institute for Policy Studies for providing valuable advice and information for this chapter.

tries, led to the global phenomenon of aid fatigue. Under this condition, governments of many developed countries and international organizations find it difficult to convince taxpayers or shareholders of the value of continuing to support developing countries.

Under such circumstances, the international aid community has new proposals in an attempt to cope with new challenges and global issues and thus improve aid effectiveness.

In the *White Paper on Official Development Assistance 2003*, the Japanese Ministry of Foreign Affairs (MOFA) summarized recent aid trends and showed a willingness to go along with them. At the same time, MOFA kept its distance and advocated ideas that are uniquely Japanese. Examples include:

- Highlighting the role of infrastructure in poverty alleviation and economic development;
- Questioning Poverty Reduction Strategy Papers (PRSPs);³
- Reservations about new aid modalities such as harmonizing procedures; and
- Criticism of the Commitment to Development Index.

On the whole, the White Paper is a balanced response to international aid trends. While I commend the Japanese government for taking such an appropriate stance, the negative side of new aid trends that hides behind the *positive side* should be examined more extensively than afforded in the White Paper, especially in light of its significant influence over developing countries. This is the main theme of this chapter.

2-1-3 Positive side and negative side — Two thematic areas

Only by examining the negative side and the positive side of recent international aid trends can we grasp the entire picture of these new trends and have a debate based on an accurate overview. In this chapter I would like to examine the negative side by focusing on two thematic areas — *dominance of donor perspectives* and *disengagement from the reality of developing countries* as seen in proposed aid approaches. Specific problems include *selective aid*, *ownership* (of recipient countries), *Poverty Reduction Strategy Papers* (PRSPs), and *new aid modalities* represented by a sector-wide approach and budget support.

3. A new term, Poverty Reduction Strategy, has also been used recently. In this chapter the document will be consistently referred to as the PRSP.

(1) Dominance of donor perspectives — selective aid and ownership

Key terms in the examination of dominance of donor perspectives include *selective aid* and *ownership* (of recipient countries). Selective aid is a typical symptom of the dominance of donor perspectives. Another area where the dominance of donor perspectives manifests itself is the concept of ownership. When we carefully examine past debates about ownership, such a concept advocated by the international aid community may be nothing but a convenience. From this recognition emerges a desire to pursue *true ownership*.

(2) Aid approaches — detachment from the field and disengagement from reality

Detachment of new aid approaches from the reality of developing countries can be examined by considering PRSPs. In addition, I would like to look at the new aid modalities represented by a sector-wide approach and budget support. While many researchers and aid practitioners have made valuable observations on these matters, this chapter will focus on issues that have yet to be discussed explicitly.

The first issue is time in the field. From the perspective of developing countries governments, one of the characteristics of PRSPs and new aid modalities is the burden of paperwork and complex tasks of donor coordination. As weak government institutions are overwhelmed by paperwork and donor coordination work, inevitably the time and energy that technocrats can spend in the field are reduced significantly.

This also means that donors must spend more time dealing with central government institutions. When donors spend more time at the capital or international conferences coordinating with technocrats and other donors, they have less time to visit the field where poverty reduction and economic development actually take place, thus donors become detached from the frontline of aid.

There are other, similar tendencies in the new aid modalities. In coordination processes such as a sector-wide approach and budget support, developing countries are supposed to play a leading role or direct the processes (Harrold, 2003). If this is true, those who mainly speak for a developing country must be technocrats due to the required expertise and statistical data to be processed. A system in which technocrats based in a capital play a central role naturally detaches them from the field. Thus, I am concerned that both donors and developing country technocrats do not spend enough time in the field.

The second issue is the tendency to pay more attention to formal institutions than to the reality of developing countries. Observation of various PRSPs reveals a common characteristic — attention is not focused on how economic and social structures are functioning in reality, but rather what institutions are lacking or weak. As a result, the focus of reform is placed on introducing new institutions and fixing existing ones, and many countries are required to introduce new legislation, organizations, and rules as a condition for receiving a loan. This is apparent by looking at various PRSPs.⁴

What is important, however, to reduce poverty and spur economic development is how the economy and society function, not institutions themselves. A tendency to pay too much attention to formal institutions leads to detachment from the economic and social realities of developing countries.

2-1-4 Nurture strengths rather than point out weaknesses

At the core of the standard approach by the international aid community is a prescription for eliminating weaknesses based on a diagnosis that things don't go well because of bad institutions and policies. An alternative approach that Japan should advocate would be an endogenous prescription that identifies and exploits the strengths inherent in the economic and social systems of a developing country — nurture strengths rather than point out weaknesses — is our basic message.

2-2. Dominance of donor perspectives is the negative side

2-2-1 Significance and problems of selective aid

(1) G8 Africa Action Plan and Millennium Challenge Account

One of the pinnacles of the donor-centric trend was the G8 Africa Action Plan, which was announced at the Kananaskis Summit in June 2002. It is a donor action plan that supports the New Partnership for Africa's Development (NEPAD) adopted by African nations. In the Action Plan, the G8 countries announced their intention "to focus our efforts on countries that demonstrate a political and financial commitment to good governance and the rule of law, investing in their people, and pursuing policies that spur economic growth and alleviate poverty." Thus, the policy of selection and con-

4. A comparative table of policy matrices for 13 countries in JICA (2004) is useful.

centration was launched and three selection criteria were defined: (1) good governance and rule of law, (2) emphasis on education and training, and (3) appropriate policies (meaning those that promote market principles).

In March 2002 before the Kananaskis Summit, the Bush administration of the United States announced the Millennium Challenge Account (MCA). It is a mechanism to 'reward' developing countries with good performance. Three performance evaluation criteria were established to select eligible countries (Applegarth, 2003):

- Good governance — democratic political system, rule of law, human rights, transparency, accountability;
- Economic freedom; and
- Investing in people — budget allocations for primary education and health care.

A comparison of the G8 Africa Action Plan adopted at the Kananaskis Summit and the MCA of the U.S. reveals a common basic philosophy and a striking similarity in selection criteria. Even before these developments, the Netherlands New Aid Policy, which adopted the selection and concentration principle, and the World Bank report *Assessing Aid* (1998) pointed to being selective about aid recipient countries. Selective aid has become a dominant force in international aid.

(2) Two background factors — New Public Management and aid fatigue

Two factors have contributed to the emergence of selective aid as a popular concept. One is New Public Management (NPM), which was adopted by OECD countries in the 1980s as a basic theory for public sector reform, and the other is aid fatigue that major donors have been experiencing since the 1990s. The philosophy of selective aid became influential as a result of interactions between these two factors.

Major donor countries struggling with budget deficits and public debt sought to revitalize the public sector and looked for a better functioning and less costly system. As a precondition for reducing the scale and scope of the public sector and building a system that functions efficiently and effectively, a *results orientation* was emphasized along with decentralization, devolution, and privatization. To adopt results orientation, a series of frameworks were proposed to clearly define objectives, establish goals, assign responsibilities and incentives to achieve them, and monitor progress (Miyagawa and Yamamoto, 2002, Chap. 1).

Meanwhile, fiscal difficulties of major donor countries created a situation where more of the public became skeptical about development aid and began asking why it was still being offered. As some research showed that aid was not producing desired effects, it became more difficult for donor countries governments to convince their taxpayers, and for international organizations to convince their shareholders, to maintain aid programs. As these changes took place, *results* became a much more important factor for the international aid community.

One effective way to ensure aid effectiveness is to identify projects that do not or cannot be expected to produce results. In some countries it is more difficult to produce results or projects have lower chance of succeeding, which leads to a view that in order to make aid more effective, donors must be selective about aid recipients and concentrate resources on countries with better prospects. Accountability to taxpayers and shareholders led to such an approach.

(3) Selective aid and humanitarian crises

The trend of emphasizing aid results has important virtues, but at the same time it has serious negative effects.

One of the more important criteria for selecting recipient countries is governance. If we assume that aid to developing countries with poor governance is less effective than aid to other countries,⁵ what kind of developing countries will see their aid reduced or suspended based on this assumption? Countries deemed by the international aid community to have very poor governance. Table 2-1 shows that these countries also have the lowest human development indices and the highest poverty rates. In many of the poorest or least-developed countries, the threat to human security and poor governance go hand-in-hand. What will happen if aid to these countries is reduced or suspended on the grounds of poor governance? We should expect that the living conditions of the poorest part of the population will deteriorate and humanitarian crises would likely follow. Selective aid is an approach that ranks aid effectiveness over the condition of the poorest people, an approach that is representative of the dominance of donor perspectives.

5. The concept of governance as defined by the international aid community has limited ability to explain the differences in performance of developing countries. See Shimomura (2005b) and Shimomura (2006) (to be published).

Table 2-1. Percentage of poor population and human development indicator in lowest ranking countries* in governance indicator

*12 countries evaluated as the worst five in either 1) rule of law, 2) government's effectiveness, or 3) corruption in *Human Development Report*, 2002.

	related governance indicator	population below income poverty line less than \$1 dday(%)	Human Development Indicator rank among 177 countries
Tajikistan	①	n.a.	122
Myanmar	③	n.a.	129
Papua New Guinea	③	n.a.	137
Sudan	③	n.a.	141
Republic of Congo	②	n.a.	142
Haiti	①	n.a.	153
Angola	①	n.a.	160
Democratic Republic of Congo	① ② ③	n.a.	167
Burundi	③	58.4	169
Guinea-Bissau	① ②	n.a.	172
Mali	②	72.8	174
Republic of Sierra Leone	②	57.0	176

Source: UNDP, *Human Development Report*, 2002

UNDP, *Human Development Report*, 2004

(4) Humanitarian crises as enormous social costs

The pursuit of selective aid is an alternative that might trigger a collapse of fragile states and incur enormous social costs in the form of humanitarian crises. Selection of aid recipient countries by the governments of industrialized countries and international organizations allows them to ensure aid effectiveness and fulfill responsibilities to their taxpayers and shareholders. At the same time, it also has a potential to cause famine, epidemics, and refugee problems by reducing assistance to countries where it is more difficult to produce or expect results, destroying the human security of the poorest populations. Furthermore, we cannot ignore the possibility that it might lead to armed conflicts such as civil wars, ethnic hostilities, or environmental degradation, including desertification.

Once famine, epidemics, refugees, or conflicts arise, donor countries can expect their people to support emergency assistance, peace building, and reconstruction efforts as humanitarian and heroic acts. However, they cannot expect good results from fragile states or public support for assisting them before these states actually collapse. This is the dilemma that donors are facing. While it is very difficult to resolve, I would like to propose these actions:

- Compare the monetary costs to donors (aid does not produce desired effects) and the social costs (destruction of human security of the poorest people in fragile countries);
- Confirm that the social costs are far greater than the donor monetary costs; and
- Consider improving aid modalities so that aid to fragile states contributes as much as possible to prevent them from collapsing.

We should re-examine our assistance to fragile states in view of the enormous costs that humanitarian crises bring to the global society. By doing so, we will be able to find a way to cast off the donors' one-sided logic represented by the concept of selective aid.

2-2-2 New trends surrounding ownership

The international aid community emphasizes partnership and ownership. The statement of the High Level Meeting in 2000 of OECD's Development Assistance Committee (DAC) emphasizes that "partnership with developing countries who have a sense of ownership is the basis of our cooperation" (OECD, 2001, p. 24). Japan's revised Official Development Assistance Charter also clearly states in the Basic Policies section that Japan respects "the ownership by developing countries." Needless to say, the emphasis on ownership is appropriate and warranted, however, there is a need to re-examine the debates on ownership within the context of new aid trends.

(1) Improving ownership by aid coordination

In the international aid community, donors are actively trying to coordinate with one another in order to use their limited aid resources effectively. An argument that aid coordination strengthens the ownership of developing countries is gaining influence (Kihara, 2003, pp. 42-46). Based on Ghana's experience, P. Harrold of the World Bank states that the objective of the sector-wide approach is to prevent chaotic emergence of too many donor-led projects and overcome the lack of ownership by developing countries (Harrold, 2003).

This idea — strengthening ownership by aid coordination — is based on a premise that the government of a developing country will direct donors in the framework of aid coordination. It is assumed that the government will prepare development and poverty reduction strategies with the help of donor experts, bring their plans to donor meetings, and play a leading role in coordinating donor debates. This is often described as "the government of a

developing country, not donors, is in the driver's seat and holding the handle."⁶

(2) Testing the ownership

Considering the reality of relationships between developing countries and the international aid community, how often do we find a situation where the government of a developing country is in the driver's seat? To find out, the following question would be effective:

"When an alternative preferred by the government of a developing country is not aligned with the advice of the international aid community and international best practice, would the wish of the government be honored?"

If the answer to that question is yes, then we can say that the government is in the driver's seat and has the true ownership. If the answer is no, it means that even if the government is holding the handle, the driving path is dictated by someone else.

Unfortunately, we should expect that the international aid community is very unlikely to accept policies that do not conform to its preferences. As discussed earlier, we must consider the reality in which selective aid has become a dominant trend. Also, the World Bank (1998) defines the concept of ownership as "strong domestic support for reforms (that the international aid community requires as a condition for assistance)" and states that "ownership is essential for adjustment loans to succeed" (World Bank, 1998, p. 52). The ownership defined in that publication is nothing but requiring developing countries to strongly commit, of their own will, to policies preferred by the international aid community and faithfully implement them.

(3) Looking for true ownership

For a developing country to have true ownership, it needs to secure a freedom to choose policies that it considers best after considering advice from the international aid community and international best practice.

It is possible to find examples where a developing country made its own decision on an important development issue and a certain level of success was confirmed in an ex-post evaluation. One such example in recent years is the management policy adopted by the Malaysian government during the East Asian financial crisis at the end of the 1990s. It is interesting to note that the IMF, which ferociously criticized the Malaysian government for this well-

6. Former World Bank President Wolfensohn said that "[developing] countries must sit in the driver's seat and determine the course" (Wolfensohn, 1999, p. 9).

known unorthodox choice, later conducted a comprehensive review (Meesook et al., 2001) and concluded matter-of-factly that the choice by Malaysia did not lead to serious problems. Another, older example is the Eastern Seaboard Development Project in Thailand, which was the flagship project of the country's Fifth Five-Year Plan during the 1980s. This megaproject was designed to enhance export competitiveness and alleviate the problems of over-concentration in Bangkok by constructing two industrial parks with deep seaports on the coast southwest of Bangkok. The Japanese government provided more than ¥130 billion in loans for the project. The initial plan included construction of a urea fertilizer plant for the National Fertilizer Corporation (NFC). Despite the fact that the World Bank and Japan — the two largest donors for Thailand at that time — recommended building the plant, the Thai government decided against it. An ex-post calculation showed that the plant would have lost money, suggesting that the Thai government made a good decision (Shimomura, 2003, Chap. 6).

One could argue that, even if true ownership is desirable, some developing countries cannot be trusted with the handle in light of their governance conditions. This concern over the level of governance in developing countries is understandable, but it is somewhat inconsistent to have that concern and emphasize their ownership at the same time. We should reexamine our inclination to advocate respect for ownership.

As Takahashi correctly points out, policy choices faced by a developing country are “a product of extremely complex political and economic mechanisms, just as complex as they are in an industrialized country,” and “those mechanisms are defined to a large extent by domestic conditions of the developing country. If aid donors are going to influence its preferences, they must understand these political and economic mechanisms and think hard about how to deal with them” (Takahashi, 2005, p. 78).

We should return and re-evaluate the dominance of donor logic.

2-3. Removal from the field as the negative side

2-3-1 Poverty Reduction Strategy Papers (PRSPs)

(1) Identifying problems

As a brief survey of several PRSPs reveals, lists of policy measures deemed necessary to reduce poverty are comprehensive and extremely long. It is the developing country's bureaucracy that must handle the bulk of work associ-

ated with this huge number of policy measures to be implemented — coordinating with the donor community, gathering statistical data, and preparing documents. This work, however, far exceeds the capacity of weak government machinery of the poorest or least-developed countries. When weak governments are forced to concentrate on paperwork and coordination, we cannot expect them to have time and energy to spend in the field where poverty alleviation and economic development actually occur. Under this pressure, developing country governments become increasingly detached from the field.

Let us consider the PRSP for example. A PRSP specifies goals, which ministries should implement them, and deadlines for their achievement aligned with a diverse set of policy tasks. These elements are central to donor coordination. Therefore, those who toil on the ground for individual projects designed to alleviate poverty and promote economic development have limited opportunities to participate in donor coordination meetings, except, perhaps, for influential local NGOs. Inevitably, the voice of technocrats is more likely to be reflected in policy measures than the voice of those working on the field.

Also, negotiations about policy mostly take place in the capital of the developing country or at international conferences, far away from the field where poverty reduction and development efforts actually occur, a situation I consider as donor detachment from the field.

(2) PRSPs problems found in real examples

Let us look at actual examples of PRSPs to illustrate this point: Laos (IMF, 2004), Tanzania (The United Republic of Tanzania, 2005), and Sri Lanka (World Bank, 2003).

- **Laos.** The list of policy measures required under a PRSP is long. The list for Laos is in two parts, the first of which deals with the macroeconomic and governance environment and is divided into these five categories:

- ① National development framework (includes 37 targets and 47 performance indicators),
- ② Policy matrix for revenue collection,
- ③ Policy/program matrix for public expenditure management,
- ④ Policy/program matrix for the financial sector, and
- ⑤ Governance initiatives.

The second part is called Sector/Cross-sector and National Programmes Matrices, which specifies a large number of detailed targets, policy mea-

asures, and monitoring indicators for each of the following 10 categories:

- ①Agriculture and forestry,
- ②Education,
- ③Health,
- ④Transportation,
- ⑤Gender,
- ⑥Environmental protection,
- ⑦Drug control,
- ⑧Unexploded explosive ordnance (UXO) contamination,
- ⑨HIV/AIDS prevention, and
- ⑩Trade.

Many people would be overwhelmed by the sheer scale and the enormous workload this list implies, but at the same time they would feel disturbed by the gap between the capacity of the public sector of a developing country and the enormous scale of the tasks that it faces. Those who have been in the building of a Laotian government agency would surely see the gap between this list and the reality of Laos.

- **Tanzania.** The matrix of Tanzania's PRSP is divided into three clusters: growth and reduction of income poverty, improvement of quality of life and social well-being, and governance and accountability. Each cluster includes goals, targets, and strategies (Table 2-2).
- **Sri Lanka.** While Sri Lanka's PRSP includes six categories, it is much more compact than those of Laos and Tanzania, which suggests that the content of a PRSP is not necessarily aligned with the operational capacity of a country.

Looking at the content of actual PRSPs begs this fundamental question: Who prepared this document, and how? Considering the amount of work involved, the PRSPs of Laos and Tanzania could not have been prepared without inputs from many outside experts, which reveals not only a detachment from the field but also the lack of ownership. As of June 2005, 49 countries had prepared PRSPs (World Bank, 2005, p.1), which suggests that PRSPs have a significant job creation effect for experts who work in the international aid community.

2-3-2 New aid modalities — detached from the field

Key terms for the so-called new aid modalities represented by a sector-wide approach and budget support include *fungibility*, *traceability*, *public expenditure reviews*, *common funds*, and *harmonized procedures*. What kinds of information and expertise are required to uphold these key words?

Table 2-2. Matrix of Tanzania's PRSP

Cluster 1: Growth and reduction of income poverty	
Goals	Targets
1: Ensuring sound economic management	2 items: Macroeconomic stability maintained; reduced unemployment and address underemployment in rural area
2: Promoting sustainable and broad-based growth	11 items: Accelerated GDP growth rate; scaled up participation of the informal sector and SMEs; increased technological innovation, upgrading and use of technologies; etc.
3: Improved food availability and accessibility at household level in urban and rural areas	2 items: Increased food crops production; maintained strategic grain reserve
4: Reducing poverty of both men and women in rural areas	7 items: Reduced proportion of rural population below the basic needs poverty line; reduced proportion of rural food poor; increased off farm income generating activities; etc.
5: Reducing poverty of both men and women in urban areas	2 items: Reduced proportion of urban population below the basic needs poverty line; reduced proportion of urban food poor
6: Provision of reliable and affordable energy to consumers	2 items: Liberalization of the power sub-sector; at least 3 production-sharing agreements
Cluster 2 Improvement of quality of life and social well-being	
Goals	Targets
1: Ensuring equitable access to quality primary and secondary education for boys and girls, universal literacy among men and women and expansion of higher, technical, and vocational education	8 items: Early childhood; primary enrolment; secondary enrolment; etc.
2: Improved survival, health, and well-being of all children and women and of especially vulnerable groups	5 items: Infant & child health; child nutrition; HIV/AIDS; etc.
3: Increased access to clean, affordable, and safe water, sanitation, decent shelter, and a safe and sustainable environment and thereby, reduced vulnerability from environmental risk	5 items: Water; sanitation & waste management; pollution; etc.
4: Adequate social protection and rights of the vulnerable and needy groups with basic needs and services	4 items: Social protection; support to vulnerable groups; child protection &
5: Systems in place to ensure effective universal access to quality public services that are affordable and available	5 items: Roads; schools & health facilities; social service sectors; etc.

Cluster 3 Governance and accountability

Goals	Targets
1: Structures and systems of governance as well as the rule of law are democratic, participatory, representative, accountable, and inclusive	1 item & 7 sub-categories: institutional reforms; parliament and other governance institutions; participation and representation at local level; etc.
2: Equitable allocation of public resources with corruption effectively	2 items & 16 sub-categories: Equity; participation and access to information; anti-
3: Effective public service framework in place to provide foundation for service delivery improvements and poverty reduction	2 items & 10 sub-categories: public service intervention; commercial courts; surveys; etc.
4: Rights of the poor and vulnerable groups are protected and promoted in the justice system	1 item & 10 sub-categories: District courts; legal reforms; laws and gender; etc.
5: Reduction of political and social exclusion and intolerance	1 item & 6 sub-categories: Local authorities and CSOs, CBOs; political parties; civic education; etc.
6: Improved personal and material security, reduced crime, eliminate sexual abuse and domestic violence	1 item & 8 sub-categories: Prisons and community; police force and community; women's rights; etc.
7: National cultural identities enhanced and promoted	1 item & 4 sub-categories: Moral education; Swahili language; etc.

Reviewing public expenditures with donor economists — especially those in international organizations — while keeping an eye on the concepts of fungibility and traceability requires knowledge of macroeconomic indicators — especially fiscal statistics and budgetary systems. Those who design harmonized procedures and manage common funds must be well versed, at the least, in the trends of international finance and procurement rules of domestic government agencies. Those in developing countries who have this kind of knowledge and experience — and access to necessary statistics — are limited to technocrats who typically work for economic ministries in the central government.

Discussions that drive the new aid modalities would typically take place in an office in the capital. An air-conditioned room would feature computer monitors showing statistics and thick volumes of procurement regulations and manuals. That place belongs in a different world, far away from the sweat of primary health care workers who visit rural villages, mud in the foundation work for a bridge construction, the stench of slums in big cities, and the scorching sun shining over saplings planted in a desert. As developing country technocrats and the staff of aid agencies are consumed by the work in

capital cities, their attention, time, and energy for the field are inevitably crowded out.

2-3-3 Disproportionate emphasis on formal institutions and disengagement from reality

(1) Identifying problems — A case study of the power sector in Sri Lanka

One common characteristic found in PRSPs is that attention tends to be focused on what kinds of institutions are lacking or inadequate in developing countries. As a result, the focus of reform is placed on introducing new institutions and fixing existing institutions and many countries are required to introduce new bills, organizations, and rules as a condition to receive a loan.

One item in the second category of Sri Lanka's PRSP (improve investment environment for private sector activity) is power sector reform, which lists three pillars as policy measures:

- ① Increase the electricity tariff to a level where cost recovery is possible;
- ② Unbundle the Ceylon Electricity Board (CEB) so that generation, transmission, and distribution of electricity are separated; and
- ③ Encourage independent power producers (IPPs).

For the second target of unbundling the CEB, the Parliament passed the Electricity Reform Act and Public Utility Commission Act in October 2002, and the PRSP moved on to selection of the chairman of the Public Utility Commission and drastic changes in power sector organizations and regulations. Sri Lanka at that time had a power structure where the President and Prime Minister belonged to different political parties. The President fired the Prime Minister and the resulting political instability continues to this day. As a result, the "notice through official gazettes" (the final confirmation procedure by the government) has not taken place for the two bills, leaving the PRSP's power sector reform at a standstill. As a 'stick' to promote the reforms agreed to in the PRSP, the international aid community has essentially suspended its assistance to the power sector.

Meanwhile, the CEB's finances have deteriorated. It fell into the red in FY2000 and its losses have rapidly increased since then. If the CEB continues to lose money under this gridlock, there is a concern that its ability to provide a stable electricity supply may be affected. When profitability declines, budgets for functions such as maintenance, training of technicians, and environmental activities tend to be reduced.

When I met the resident representative and his staff economist at a major international organization Colombo office, they explained, “When the two bills are enacted the unbundling will become a reality. When the CEB is unbundled the management will become more efficient due to competitive forces, and things will get better.”

If the deficit becomes a serious problem, I asked, and the CEB is unable to allocate sufficient funds for maintenance and other essential functions, the ability of the CEB to do its job may have been eroded when organizational reform finally takes place. They responded to my concern by saying, “If unbundling takes place, the new management will quickly take actions and the problems will be solved.”

I pointed out the problems of training facilities for technicians. The facilities are deteriorating because of a long period of insufficient funding. They only have antiquated equipment and the morale of both instructors and technicians is low. It is those technicians who are the backbone of an uninterrupted power supply, especially in the areas of transmission and distribution. Deficiency in their training can lead to serious problems.

In response, they insisted, “Although we share your concern, when unbundling takes place the new management will implement an effective prescription and things will get better.” This conversation confirmed that, while local representatives of the international aid community were well-informed about the political situation in Sri Lanka and the institutional aspects of the power sector, they did not seem to have visited the frontline of the CEB in maintenance and training. They were not familiar with reality and their understanding was very abstract.

This is only one small example, but it highlights the fact that the attention of the international aid community is fixated upon formal institutional changes such as introduction of reform bills, organizational and regulatory changes, and personnel changes. The reality of rank-and-file employees who support a stable power supply is not understood properly. This is a typical symptom of donor detachment.

(2) An alternative perspective

How can we overcome the reality described above? The international aid community emphasizes institutional and policy improvements, but even if some institutions are missing, well-performing developing countries have mechanisms in their social systems that carry out the same functions to some extent. There are quite a few examples where, even if institutions seem

inadequate on the surface, there are quite a few examples where the functions required of them are in fact carried out.⁷

It is never easy to design new institutions that fit well with the indigenous economic and social systems in a country. There are many examples where alien systems were grafted without sufficient consideration of characteristics of indigenous economic and social systems and the newly introduced systems do not function properly or produce expected results. Simply pursuing institutional changes is not enough. It would be more effective to find structures functioning under the existing institutions and take advantage of their underlying mechanisms to achieve the desired goals, and at the same time consider the alternative approach of taking time to examine indigenous characteristics of the recipient country and design institutions that match these characteristics.

2-4. Conclusion and recommendation

New ideas, strategies, and approaches have been proposed by the international aid community and they have become a dominant force. While they have many virtues that should be appreciated, in this chapter I have pointed out their often overlooked negative side.

The objective of this chapter is to think about a unique role for Japan within the international aid community. I would like to propose that Japan become the ‘counterforce’ against the negative side which tends to be overlooked by the international aid community. Specifically, Japan should raise issues about the negative side and recommend countermeasures in addition to actively contributing to promote the new trends.

This chapter focused on the dominance of donor perspectives and disengagement from the reality of developing countries. One way to overcome these symptoms is to advocate identifying and exploiting the underlying strengths inherent in the developing country economic and social systems. Then nurture strengths rather than pointing out weaknesses as an alternative to the international aid community’s standard approach — diagnose problems caused by institutions and policies and prescribe to overcome the weaknesses. I hope that Japan’s role will be reconstructed based on this perspective.

7. Shimomura (2006) (to be published) discusses specific East Asian examples in detail.

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Structures of Donor Partnerships

For more effective partnerships

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Introduction

In an effort to make aid more effective in developing countries, donor coordination began to increase in 2000. This trend produced the Paris Declaration on Aid Effectiveness in March 2005. The declaration suggested how donor countries could build partnerships to improve aid effectiveness. Suggestions included aligning aid to the policies and institutions of recipient countries and harmonizing aid procedures. In response to this trend, the Japanese aid system and organizations have praised the general ideas of aid coordination and partnership, but have not necessarily followed through with specific actions.

Why has Japan embraced the general idea of partnerships and yet been cautious when it comes to specifics? This chapter will systematically examine the factors that have led to this position and formulate a hypothesis. We will use Organization Theory and Exchange Theory to clarify the characteristics of the Japanese aid system and organizations as well as the merits and drawbacks of participating in partnerships to understand the underlying factors. We will also draw on the experience of other countries. Through this examination we will identify the essential elements required if Japan is to contribute more to Poverty Reduction Strategies (PRS) with an emphasis on partnerships, which will become an important goal for Japanese foreign policy.

Our analysis uses the proposals and analyses by the Development Assistance Committee/Organization for Economic Cooperation and Development (DAC/OECD) of Japanese aid, as found in its peer reviews and

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other documents, including guidelines that the DAC has proposed to donors as non-binding targets. These recommendations calling on donors to implement drastic reforms are typically made by the DAC to improve aid effectiveness. While the merits of individual recommendations can be debated, this chapter discusses issues that will arise when we accept the recommendations as the basis of our aid activities. We can at least clarify what improvements and efforts will be required of the Japanese aid system and organizations if they are to follow the DAC recommendations and build partnerships.

There are many types of partnerships, but our primary focus in this chapter is on those among donors. Partnerships are being developed between donors and recipient governments, and between donors and civil society. In some cases, characteristics of donor partnerships are defined by other partnerships. We have limited the scope of our analysis to partnerships among donors. This limit restricts our arguments from the perspective of illuminating the overall structure of partnerships, however, we believe that the challenges for the Japanese aid system and organizations will be clarified by examining partnerships at the donor level by comparing aid systems. The second chapter of the DAC/OECD Guidelines on Poverty Reduction (2001) still remains the best comprehensive guide on partnerships.

The first section of this chapter summarizes the main debates in the DAC about the Japanese aid system and organizations. Next we review existing definitions of partnerships and describe the Organization Theory and Exchange Theory used in our analysis. The third section uses these theoretical concepts in an attempt to understand the Japanese aid system from the perspective of Organization Theory. The fourth section provides a tentative analysis of factors that contribute to the lack of active pursuit of partnerships or lack of abilities from the perspective of Organizational Theory and Exchange Theory. The fifth section examines potential actions that Japan can take to develop partnerships, and the concluding section discusses the outlook for the future.

3-1. Debates on the Japanese aid system and organizations in the DAC

International aid in the 1990s faced a new paradigm - partnerships. As aid agencies understood and shared a concept of equal partnerships with recipient governments and respect for coordination among aid agencies to avoid redundancy and inefficiency, partnerships among donor agencies, govern-

ments, NGOs, and civil society became a norm. In the 1990s aid agencies began to refer to the necessity to pursue partnerships in various policy documents (WCEFA Secretariat, 1990; DAC/OECD, 1996; World Bank, 2000; Eriksson, 2001; DFID, 2003). In recent years the concepts of ownership and partnership have become very important in development assistance. While these two concepts have been frequently quoted since the publication of DAC's New Development Strategy in 1996, few documents offer clear definitions of them.³ In the international aid community, the actual functions of partnerships have not been analyzed carefully, questioning their significance and effectiveness in the context of comprehensive policies and their implementation. Currently the only available evaluation of donor implementation systems is the DAC's Peer Review.

The DAC conducts peer reviews of two member countries every year. In 2003 the Committee evaluated Japan and offered harsh criticism of the country's aid system (OECD, 2003c). The reviewing members noted that Japan's ODA reform, including revision of the ODA Charter, had progressed since the last Peer Review, but they noted that the aid system remained centralized and that the ministries and headquarters were compartmentalized. They also commented that the Japanese government "should develop a government-wide approach to mainstream cross-cutting issues, rather than treating them as separate sectors, centering on the concerns of poverty reduction as part of achieving the Millennium Development Goals." These comments are pertinent to Organization Theory and point out problems related to aid implementation systems, not individual development programs or projects.

One recommendation about aid allocations stated that "development of a clearer policy on how Japan intends to focus on poor countries or poor populations within countries should be considered." In other words, Japan was urged to develop a concrete pro-poor policy. For aid implementation, the Committee proposed that "Japan should consider moving away from an instrument based co-operation system to a more country based approach, as well as establishing country budget envelopes." These recommendations mean that if the Japanese government is to promote and accelerate the PRS, it needs clearer policies and methodologies. They also emphasized the importance of preparing Country Assistance Strategies (CASs).⁴ In the strate-

3. Killick (1998) and others have analyzed the relationship between ownership and structural adjustment policies, but they have not offered a clear definition of ownership itself.

4. The CAS used to be prepared by the World Bank, but bilateral donors began to use that name to refer to their own strategies as well. Incidentally, the DAC stated that the MOFA "should leave the implementation of grant assistance to JICA and focus their manpower on developing strategies and policies."

gy arena, the Ministry of Foreign Affairs (MOFA) has made special efforts in recent years; it abolished an existing division in the Economic Cooperation Bureau and created two divisions that deal with country assistance.

In the case studies of the peer review, Japan's efforts in Tanzania, i.e. active participation in aid coordination in Tanzania and Vietnam, (i. e. coordination with JBIC-World Bank-ADB and Japan-U.K. cooperation, and the ODA Task Force in Vietnam) received high marks. Some DAC members opined that these efforts should be emulated by other countries, but almost two years after these discussions took place in January 2004, we do not see any efforts to do so by other countries. This may help to explain the gap between Japan's general stance and specific donor partnerships. Despite the efforts of various parties, there may be internal and organizational factors that are strong enough to suppress external influences, including the call for and the necessity of partnerships.

To summarize the analyses of DAC reviewing countries: Japan's current ODA administration system is compartmentalized. To ensure a comprehensive perspective and consistent policies, it has been proposed that the aid system based on multiple ministries and implementing organizations should be abandoned and that policies should be designed by an organization with more streamlined authority. That organization should concentrate on strategies, policies, and coordinating the aid system, and leave implementation to appropriate agencies as much as possible. Program implementation undertaken by a policy ministry could risk blunting any evaluations related to accountability.⁵ We need to show a theoretical framework and systematically examine why Japan's aid system has had difficulty in dealing with these problems.

3-2. Conceptual framework for understanding partnerships

We now turn to existing definitions of partnerships and propose Organization Theory and Exchange Theory as conceptual frameworks for understanding the meaning of partnership.

5. The World Bank's 2004 report contrasts policy ministries and implementing agencies by stating that in developing countries "policy ministries set and enforce the rules of the game played by service delivery agencies while the latter prepare internal 'policies' that are unique to each organization." This argument applies to the Japanese aid system as well (World Bank, 2004, p. 50).

(1) Defining partnerships

Partnerships are now a new phase beyond cooperation and collaboration (Mullinix, 2001; Annex 1). Partnerships share more political pain and gain and require strong commitments and investments (Balloch and Taylor, 2001).

The interdisciplinary literature has only a limited number of definitions in the context of international development/cooperation. Bray (1999) defined partnership simply as “persons (or organizations) who share (similar actions)” and pointed out that while the term generally implies equal appropriations, in reality there is often a dominant partner and its characteristics change significantly under different settings and over time. Similarly, Brinkerhoff (2002) defined an ideal partnership as an active relationship between different actors based on mutually agreed-upon objectives, which is pursued with a shared understanding of reasonable appropriation of tasks based on each partner’s comparative advantages. On the other hand, she also said organizational and political constraints make ideal partnerships clearly unrealistic.

Attempts to define partnership have been made in an interdisciplinary context and through the analyses of real situations. If we summarize common factors found in various definitions, we can define partnership as a strong implementation system that becomes viable when two or more organizations or individuals share not only objectives or goals but also mutual trust, risks, and responsibilities. Partnership faces various organizational and political constraints and takes different shapes at different times and under different circumstances. This definition implies that, especially in the field of international cooperation, we need to analyze organizational and political constraints in greater detail, which can take various forms. Organization Theory and Exchange Theory are two such analytical tools.

(2) Organization Theory

Organization Theory tries to identify goals of an organization as a whole and its individual members, and aims to analyze the functions of different organizations. Classically, an organization is defined as “a system of activities and forces consciously coordinated by two or more persons” (Barnard, 1938), including internal activities such as plans, organizational structures, and communications. We need to analyze how organizational goals are defined and by whom.

To achieve conscious coordination, it is important that organizational cul-

ture - shared and internalized beliefs and norms - controls and gives meaning and guidance to individual members who are involved in collective actions, in addition to integrating the organization (Scott, 1987). Organizational culture provides shared and internalized beliefs and norms, meaning, and codes of conduct to its members. In other words, an organization creates organizational culture and its individual members share similar behavior and response patterns.

One of the theses of Organization Theory is that various individuals join an organization to achieve a goal but their motives and the goal of the organization are not necessarily the same. As in Rousseau's general will and individual will, aggregating the objectives of individual participants may not add up to the goal of the organization (Scott, 1987). This is also true when more than one or more small organizations form a larger organization. An organization is also influenced by the broader social and cultural environment, for example, popular opinion. Thus an organization is sensitive not only to internal functions but also to external influences of the broader, social and cultural environment (Meyer and Scott, 1992; Scott and Christensen, 1995).

If we apply this Organization Theory to partnerships in international aid, sharing a target of aid impacts is not enough. It is also important to examine the ideal forms of partnership while considering organizational decisionmaking mechanisms, organizational culture, norms and beliefs, and the sociocultural, political, and economic background of aid agencies.

(3) Exchange Theory

Exchange Theory was developed by scholars of political economy who focused on monetary markets and was later expanded to explain social and political behavior (Baldwin, 1990). The basic premise of Exchange Theory is the 'reciprocal relationship' which functions as long as people believe in and actually find reciprocal interests in an 'exchange' (Chadwick-Jones, 1976; Huston and Burgess, 1979). In this sense an exchange relationship is a product of mutually dependent actors; the actions of one actor are realized in a relationship with the actions of other actors.

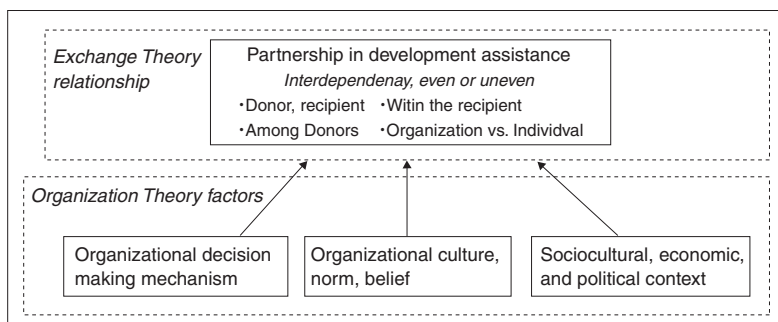
The Social Exchange Theory classifies mutual dependence into three levels based on the nature of exchanges - factual, normative, and structural (Ceri, 1990; Annex 2). Blau (1964) said that establishing a friendly relationship (either between individuals or organizations) is establishing a function of social exchanges and explained that a social exchange is not a norm for reciprocal actions; instead, it starts from ontological conditions of an

exchange, and a norm is formed from there. A political exchange requires negotiators to become political actors in an institutional sense. Politics are interactive actions and can be analyzed from various perspectives of individuals involved in the exchange. It is an analysis of what policies and compensation individuals expect to obtain with a certain cost and what they offer in exchange (Curry and Wade, 1968). For example, Honman (1961) and Blau (1964) described the origin of a political structure as a product of an asymmetric exchange relationship that emerges as one group becomes dependent on the services provided by another group.

Thus today's theory on social or political exchange depends much on mutual dependencies at the factual level when it studies the reasons why certain forms of exchange have come to exist. The level of interaction changes depending on the individuals involved and their social and political roles and status, but we also need to consider the conditions of equal and unequal interactions. We can analyze the observed passive stance of Japan toward partnerships by considering these conditions of interactions.

Figure 3-1 shows a conceptual framework we created based on Organization Theory and Exchange Theory. By conceptualizing partnership as an 'exchange relationship' we have established exchange relationships at four levels: (1) between a donor and a recipient government, (2) between donors, (3) within a recipient government, and (4) between an organization and individuals. This chapter focuses on (2). Exchange relationships at multiple levels that form a partnership are, as Organization Theory shows, influenced by socio-cultural, economic, and political context, as well as organizational culture and decisionmaking mechanisms.

Figure 3-1. Conceptual framework



3-3. Understanding Japan's aid system with Organization Theory

We now turn to Japan's aid system from the perspective of Organization Theory. Related organizations in the Japanese aid system include development assistance agencies, both policymaking ministries and implementing agencies.

(1) Japanese Overseas Development Assistance

In the late 1990s when the trend toward poverty reduction began to accelerate, the DAC (2001) began to prepare Guidelines on Poverty Reduction. In Chapter 5, entitled "Institutional Changes and Development for Mainstreaming Poverty Reduction, Partnership and Policy Coherence," the DAC examined changes within aid agencies and staff training that would be necessary for donors to mainstream the poverty reduction strategy as described in the Guideline. Changes within aid agencies are explained as "changes in their organizational structures, incentives, practices, systems and cultures." This is an extremely comprehensive prescription from the viewpoint of Organization Theory. The DAC showed options for self-examination and changes within aid agencies based on the recognition that donors cannot implement a Poverty Reduction Strategy (PRS) effectively with their existing organizational structures.

The Guidelines illustrated five models that as of 2001 represented the diverse organizational setups of ODA donor agencies (Table 3-1). Japan corresponds to Model (4), "Multiple Ministries with Separate Implementing Agencies" along with Austria and France. DAC's 1999 analytical paper com-

Table 3-1. 5 organizational structure models in the Development Assistance Agencies

	Organization type	Fall within the organization type
①	Organization at the regional bureau in Ministry of Foreign Affairs	Denmark, Finland, Netherlands
②	A bureau or a division in Ministry of Foreign Affairs	Ireland, Italy, New Zealand, Switzerland
③	Organization consists of (foreign ministry or development agency) and implementing agency	Belgium, Germany, Luxembourg, Norway, Sweden
④	Organization consists of several government offices and several implementing agencies	Austria, EU, France, Japan, Spain, Portugal
⑤	Independent development agency	Australia, Canada, U.K., U.S.

Source: Chang, H, Fell, A. M., Laird M.

*U.S. is now categorized as ④ because, apart from USAID, the development assistance by Millennium Challenge Account started in 2002.

mented that in general this setup “requires additional efforts to coordinate agencies and ensure policy coherence.”

From the viewpoint of Organization Theory, targets of an organization and sub-organizations are not necessarily identical even under normal circumstances. Compared to Models (1), (2), and (5) where decisionmaking processes are controlled by a single organization and Model (3) where coordination is required only between two closely-related organizations, Model (4) is the most difficult setup in terms of coordination and communication because it involves many parallel organizations and a complex decisionmaking network. Indeed, while aid agencies increasingly accepted the 1990s notion that poverty reduction is their overarching objective, organizations categorized in Model (4) tended to reluctantly accept it except for the multilateral European Commission (EC).⁶ One possible explanation for this reluctance is that it is difficult for a donor country with this type of structure to coordinate different organizations and narrow their objectives, resulting in vague and broad organizational objectives.⁷ In an aid system that includes multiple ministries and separate implementing agencies, key objectives tend to multiply and it is difficult to prioritize them. Even if objectives are shared, different organizations have different aid schemes, methods, and geographical focus areas so they tend to provide aid based on their own interpretations. This is a weakness of this system.

(2) External demands for the Japanese aid system and its organizational constraints

Japan accepted the argument of aid effectiveness at the Paris High Level Forum (2005 Paris Declaration) and the targets established by the previous 2001 Rome Declaration on Harmonization and DAC Guidelines, but has still been unable to build active partnerships with other donors and recipient countries for program implementation and development aid management. This problem manifests itself not only in weak participation with fiscal assistance and sector programs (although their individual merits are debatable), but also in various organizations' procedural issues such as untying ODA, respecting procurement procedures of recipient governments, and improving the predictability of aid over multiple fiscal years.⁸

6. DAC/OECD, 1999, p. 2, Table 1.1.

7. In 1999 when the author asked several officers of the DAC department in charge of peer reviews which donors are the most divergent between general aid objectives and specifics, their unanimous answer was France and Japan.

The reasons for weak partnerships can also be explained from the perspective of Organization Theory. For example, too many ministries are involved in decisionmaking; the compartmentalized administrative systems divided by sectors and aid schemes make it harder to build relationships with partners (governments and donors); centralized decisionmaking systems that rely on central ministries and headquarters are often unsuitable for partnerships based in recipient countries; and local staff lack expertise and coordination abilities.

It is also important to note that Japan went through fewer social, economic, and political reforms that could have affected partnerships than other countries. For example, when the British Overseas Development Administration was upgraded to the Department for International Development (DFID), Clare Short was appointed as secretary of state for international development following the change in government. She quickly held up poverty reduction as an overriding objective and showed a willingness to accept the failures of past assistance. Under such a strong leader who had political momentum, the DFID reviewed and published the shortcomings of the conventional project-type assistance and began to reorganize itself along sector lines, and introduced sector programs and fiscal assistance and other scheme changes. In the context of broader trends in the international political economy, the move toward political and economic integration in Europe - symbolized by the EU - had a significant impact on aid agencies. European agencies are given incentives to harmonize their procedures and political support for aid coordination. These external factors are essential irrespective of their effectiveness when we examine aid trends because they are sometimes powerful enough to cause organizational changes in aid agencies. In Japan, it is safe to say that there had been few external factors that were strong enough to cause reorganization that promoted partnerships until discussions about consolidating government-affiliated financial institutions and related decisionmaking began to take place at the end of 2005.

Finally, in relation to social, economic, and political influences, comparing attitudes toward partnerships with donor aid contributions is interesting. The DAC categorizes major donor countries into four groups based on the amount of their aid. If we categorize the same donors based on their attitudes toward partnerships, there is a correlation between their attitudes and their

8. In Tanzania, Japan used to be the only donor that did not regularly disclose aid commitments and expenditures by country and sector, but recently Japan began to report estimate amounts to the Mid-Term Expenditure Framework (DFID, 2005, pp. 6-26).

aid contributions (Table 3-2). Donors in the ‘medium’ and ‘relatively large’ categories tend to be more positive about partnerships while fewer donors are positive in the ‘small’ and ‘large’ categories. Large donors may have fewer incentives to cooperate with other donors, while it is probably difficult for small donors to implement aid projects that are large enough to have identifiable impacts because their aid amounts are so small. They also have lower expectations for their influence. It is plausible that medium-sized donors tend to have stronger motivations to improve aid effectiveness and increase their influence. For example, Scandinavian countries are trying to increase their influence by joining the aid coordination framework under the leadership of the U.K. and by building close relationships with selected ministries and agencies of recipient governments (DAC/OECD, 1999, p. 83). Of course we cannot explain donor tendencies toward partnerships solely by their aid contributions, however, we believe that some donors have intrinsic motives to develop partnerships and achieve poverty reduction while medium-sized donors, like the Scandinavian countries, want to use partnerships as a means to increase their influence.⁹

Table 3-2. Donors’ size and attitude toward partnership

	Size of donors	Aiding donor's attitude toward partnership and country		
		positive	negative	proportion of positive countries to negative countries
1	7 small sized donors (less than 300 million dollars in bilateral aid total)	Finland, Ireland (2)	Austria, Greece, Luxembourg, New Zealand, Portugal (5)	2/7 (28.6%)
2	9 middle sized donors (500-1,500million dollars in bilateral aid total)	Belgium, Canada, Denmark, Norway, Sweden (5)	Austria, Italy, Spain, Switzerland (4)	5/9 (55.6%)
3	4 relatively large sized donors (2-4 billion dollars in bilateral aid total)	Netherland, U.K. (2)	France, Germany (2)	2/4 (50.0%)
4	2 large sized donors (more than 9 billion dollars)	(0)	Japan, U.S. (2)	0/2 (0%)

Can we explain Japan’s reluctant or cautious stance toward partnerships solely by these organizational constraints? There are organizations such as

9. Africa is the main target for aid from the Scandinavian countries and the U.K. The latter also has many immigrants from its former colonies. These factors have probably provided momentum to strengthen partnerships.

the EU that have the same constraints and yet are trying to reform their procedures in order to strengthen partnerships. If that is the case, we need to consider a larger framework of political constraints in addition to organizational constraints. In other words, we need to understand partnerships from the perspective of Exchange Theory. In the following section, we use Exchange Theory to deepen our examination of partnerships and propose hypotheses about the factors that contribute to the ambivalent stance of Japan.

3-4. Partnership elements from the perspective of Exchange Theory

Why does Japan support the general idea of poverty reduction and aid coordination while it shows reluctance when it comes to specific measures? In this section we will discuss two of the three factors shown in Table 3-3 - other than Factor 1 based on Organization Theory mentioned in the previous section - in order to understand Japan's reluctance toward partnerships. Factor 2 is based on Exchange Theory. Factor 3 indicates that there may be some aspects that cannot be explained by these theories, i.e., a factor that is beyond the organization and political relationships of aid agencies and has more cultural aspects. In the following sections we explain these hypotheses individually and examine Japan in detail while referring to other donor countries.

Table 3-3. Factors defining the degree of commitment toward partnership

		Problems
Factor1	Restriction from organisational reason	Disintegration of the development system → restriction in localization of development system → Unable to engage in the partnership
Factor2	Failure of exchange relation	Less gain from the exchange relation, or lose more than gain domestically
Factor3	Belief in the different philosophy and policy in development assistance	Have much of its own philosophy or experience enough to be negative toward the partnership

(1) Factors that determine a commitment to partnership

What gives rise to Factor 2, a situation where an exchange relationship cannot be formed? When it can be formed, the probability of an entity committing to a partnership can be described by the following formula, where α is the benefit that can be gained from an exchange relationship and β is the

benefit that is lost because of the relationship:

$$\text{Prob}(P) = \alpha - \beta \dots\dots\dots (1)$$

For this exchange relationship to work, the condition ' $\alpha > \beta$ ' must be met. This is the logic that Scandinavian countries and the U.K. insist upon - the benefit of maximizing aid effectiveness is larger than the losses experienced by individual donors. If this is true, an exchange relationship works because aid agencies believe there are reciprocal interests in the 'exchange' and they indeed see their value.

On the other hand, from the perspective of donors who are more reluctant toward partnerships, such as Japan and France, ' α ' and ' β ' in a partnership are not necessarily fixed - their value depends on 'terms and conditions.' Therefore, ' p = terms and conditions' is a factor that compounds the lost benefit. In this definition, the exchange relationship becomes less viable when $p > 1$.

$$\text{Prob}(P) = \alpha - p \beta \dots\dots\dots (2)$$

When Japan agrees with a general idea but objects to specifics, we can consider this ' p ' as a parameter that does not appear when discussing the general idea but appears when dealing with specifics. This ' p ' encompasses organizational characteristics and various conditions. Therefore we need to examine the phenomenon in which Japan's ' p ' becomes effective when specifics are being discussed.

Next, if we incorporate Factor 3 which considers that the extent of participation in a partnership is affected not only by the exchange relationship but also by different aid philosophies and methods (γ), the formula is:

$$\text{Prob}(P) = \alpha - p \beta - q \gamma \dots\dots\dots (3)$$

Here, ' γ ' is a commitment to a different aid philosophy and ' q ' is a parameter that changes depending on the subject of aid and the maturity of the partnership. If $\alpha - p \beta > q \gamma$, then it is possible to commit to the partnership. In the case of the United States, which is known to have a reluctance for partnerships, the balance tends to be $q \gamma > \alpha - p \beta$ due to its unique aid philosophy that attaches great importance to political considerations. The demands by U.S. Ambassador John Bolton for 700 changes to a 50-page UN draft declaration in the fall of 2005 is a perfect example of this political difference.

While ' q ' can be positive or negative, we assume for the time being that q

= 1 in the case of Japan because the government now applies aid methods based on an 'Asia-born philosophy' to other regions as well.

(2) Underlying elements of factors that determine partnership

What is involved in 'p', the parameter representing additional costs of partnerships described in the previous section? In this case, we can assume that 'p' is closely related to organizational constraints as well. Elements that can constitute such costs are summarized in Table 3-4.

Table 3-4. Parameter of further cost to the partnership

Parameter	Explanation
p1	Communication costs
p2	Cost arising from not being able to entrust things to others (system with the characteristic features of running its own business alone, pursuing self-complete value or reliability)
p3	Cost arising because of different nature of development schemes (project, technical cooperation in kind, leading role of headquarters and fiscal year system)

First, the 'p1' or communication cost becomes especially high if local human resource development is inadequate. This refers to personnel who can actively take part in partnerships at the local level. It requires not only linguistic competence but also expertise about sectors, challenges, and knowledge of the recipient country. An aid agency that recruits more personnel with these abilities and expertise would have a lower 'p1' cost and therefore fewer impediments to partnerships. Also, from the perspective of Organization Theory, when decisionmaking authority within an organization is not delegated to the field or decisionmaking is time consuming because coordinating mechanisms or procedures are complicated, the system may not be able to take advantage of qualified personnel no matter how many are trained. Therefore, the decisionmaking mechanisms may increase the communication cost.

Second, 'p2' or the cost of not being able to rely on others arises when an aid agency has a system that expects to receive explicit reports about the aid it provides. For example, the U.K. and Canada entrusted their aid to the Ugandan education sector to the daily administration of the EC and the Netherlands and participated in biannual sector meetings. They reduced the cost of having dedicated staff in the field and built close partnerships with other donor agencies. They can do this, presumably, because they are an organization that is willing to delegate its work to others. In contrast, if a

donor such as Japan needs its own personnel to manage aid projects or requires a procedure for evidence, the 'p2' cost is higher and the benefits from a partnership are reduced.

Another important issue about 'p2' is the significance of being able to delegate work to others. If a donor is interested in a technically sophisticated but limited area and tries to implement and evaluate its aid program, its field of view tends to be narrowly focused and it is difficult to precisely position its program within the recipient society. In such a case the intention to coordinate with other actors will be discouraged. If a donor can become part of a larger picture, it is more efficient to delegate some work to others while staying with an overall framework and consequently see the value of a partnership. In this sense Japanese assistance has a strong tendency to be complicated, thus there is less interest in delegating work to others.

Third, one type of aid that is considered to be incompatible with partnerships in recent years is in-kind contributions. In-kind contributions are a mainstream aid modality in Japan, and it is not easy under the current system to provide money to a recipient government. On the other hand, monetary contributions are more mainstream in the U.S. and European countries. One advantage of monetary contributions is that they are easy for a recipient government to receive. Also, if all donors provide monetary contributions, procurement procedures and staff assignments can be carried out simultaneously, allowing the government to simplify its internal procedures. For example, when a development study on alternatives to the Panama Canal was conducted by Japan, the U.S., and Panama in the mid-1980s, the largest obstacle to aid coordination was the difference in aid schemes. The three countries agreed in principle that each would contribute one-third of the overall cost, but the Japanese government and the Japan International Cooperation Agency (JICA) had a very difficult time coordinating the cost sharing because they were only allowed to make in-kind contributions, in contrast to the U.S. and Panama.¹⁰

There is a difference between 'γ' (belief in different aid philosophies and methods) and 'p3' (heterogeneity of aid schemes). The 'p3' refers to the possibility that different aid schemes may get in the way of aid coordination even if partners have similar aid philosophies, whereas 'γ' refers to a fundamental difference in aid philosophies.

All of these elements affecting exchange terms and partnership condi-

10. Ultimately, the third-party repayment system was combined with the three-country agreement to establish Japan's debt burden before implementation and disbursements.

tions are closely related to Organization Theory in that decisionmaking mechanisms, culture, norms, and beliefs in an organization are behind them. How have the countries that commit to partnerships coordinated such elements as 'p1', 'p2', and 'p3' in order to make partnerships work? In the next section we will look at the efforts of several countries based on OECD documents.

(3) Aid agency efforts

Donor countries that are now committed to partnerships did not start out with perfect conditions. In this section, we will look at several countries to see what kinds of organizational reforms have been implemented in order to build partnerships (OECD, 2003a, 2003b, 2005a, and 2005b).

P1 - EFFORTS TO REDUCE COMMUNICATION COSTS

Sweden. The Swedish International Development Agency (SIDA) encourages its staff to acquire five skills in order to enhance aid effectiveness in the field and build effective partnerships - strategic, professional, learning, relational, and functional (OECD, 2005a). SIDA aims to achieve effective management of its overall assistance by assigning staff with these skills to the field. SIDA also believes that having resident representatives with these skills in recipient countries will enhance aid coordination and partnerships (Wiklund and Palm, 2004 : 21).

SIDA has adopted specific measures for internal and external communications. To ensure productive internal communications, it was considered to be important for all employees to recognize their significance and to have close communications among embassies, SIDA headquarters, and the Ministry of Foreign Affairs so that they can speak with one voice. For external communications, there is a tentative plan to have close communication with other donors at all times. SIDA plans to implement pilot projects that incorporate dialogue with other donors in its sector programs.

Denmark. To enhance aid effectiveness, Denmark is actively delegating responsibilities to its aid professionals in recipient countries. Based on an annual contract between the ambassador to each recipient country and headquarters, tasks of identifying, implementing, administering, and monitoring country programs are all delegated to the local office and headquarters functions are limited to appraisals and evaluations. The personnel and responsibilities of regional departments in the headquarters have been reduced and their functions are now limited to finalizing country assistance strategies and attending high-level meetings with recipient governments. Instead, a quality

assurance department was created at headquarters to handle the annual contracts between ambassadors and headquarters, support the development of local staff, and conduct aid evaluations. Local offices are also encouraged to hire more local employees in the recipient country and assign them greater responsibilities. On average, four out of 12 professional staff members in each office are hired locally. Thanks to these organizational reforms, the entire international cooperation system at the local level became more efficient, and local communications command more respect now.

UNDP. In Tanzania, the UNDP, along with the government and the Economic and Social Research Foundation, has created an online database called Tanzania Online. Using this database, donor countries, recipient governments, NGOs, civil society, and academic organizations can review studies and reports on Tanzania's development, priority issues, status of poverty reduction, and sector reforms. This initiative helps promote communication through affordable information sharing.

P2 - EFFORTS TO DELEGATE WORK TO OTHERS

Norway and Sweden. To reduce administrative and labor costs borne by the governments of Malawi and Ethiopia, Norway and Sweden are trying to delegate some of their aid operations to each other. In Malawi, the two donors split the cost of \$14 million and identified spending projects with the Malawi government, but the funds are administered by Norway. Based on Norway's requests, Sweden transfers funds every six months to an account of the Norwegian Agency for Development (NORAD) for projects and programs identified at annual meetings. Norway is in charge of conducting project identification studies, making decisions to implement projects, and monitoring and evaluating them. Sweden sometimes takes part in studies or evaluations upon Norway's requests (OECD, 2003a : 93).

In Ethiopia, the relationship between the two countries is more interactive. Both countries support sector programs in the health and education sectors, so they are trying to reduce costs by delegating their own operations to Sweden for the health sector and Norway for the education sector, sharing collected information and reports, and implementing fiscal management and audits together.

Canada and the U.K. In 2002 in Madhya Pradesh, India, the Canadian International Development Agency (CIDA) decided to delegate the preparation of its medium-term health sector strategy to the British Department for International Development (DFID). Through this arrangement, DFID's India

Office hired a consultant using the pound-denominated CIDA-DFID common fund to prepare the strategy. The funds were transferred from CIDA to DFID. Also, financial management of consultant employment was based on British rules and modalities. OECD praised this effective cooperation that allows one country to reduce its manpower and financial burden without excessively increasing the burden of another country.

Australia and New Zealand. In 2000/01, the Australian Agency for International Development (AusAID) and New Zealand's International Aid and Development Agency (NZAID) conducted a study to implement joint programs in the Pacific region. The study confirmed that mutual delegation reduces administrative costs and reporting requirements on the part of recipient countries and makes programs more focused. On the other hand, in subsequent discussions questions were raised about ensuring each donor's visibility and accountability. Recipient countries also expressed their concern over possible reduction in the ownership of aid programs and the overall amount of aid. Discussion continued, however, and cooperation was realized in a middle school development program in Kiribati in which NZAID deposited funds to AusAID, which administered and managed the program. This case is drawing attention as an example of cooperation by sorting out the benefits and disadvantages of all the countries involved.

France and Germany. In the Republic of Mali, the French Development Agency (AFD), German Development Bank (KfW), and German Agency for Technical Cooperation (GTZ) agreed to entrust the administration of infrastructure development of their joint investment program to AFD and provide technical assistance. AFD would use its own administrative rules and regulations and exclusively handle all communications with the Malian Ministry of Education. Aid agencies consulted with each other to decide how to procure goods. To avoid multiple reporting formats, AFD prepared reports based on the rules of the German Ministry for Economic Cooperation and Development while GTZ prepared all reports on technical cooperation and submitted them to both governments. These simplified and unified procedures reduced time and resources for both donors and Mali.

Multilateral cooperation. In Tanzania, cooperation in the form of delegation is being pursued within a framework of multilateral cooperation. According to a report prepared by DFID (Balogun, 2005), three out of 16 donor countries - Germany, Finland, and the Netherlands - are performing operations that are delegated to them by other donors. Four donors - the U.K., Ireland, the U.S., and the World Bank - have been asked to carry out

some tasks for other donors. For example, Ireland and the Netherlands co-chair the Local Governments Reform Program. The British DFID, together with USAID, plays a leading role in the area of reinforcing parliamentary systems. Also, the World Bank participates in thematic debates under the leadership of donors for the Poverty Reduction Budget Support (PRBS). In addition, differentiated roles among donors participating in fiscal assistance and the Sector Wide Approach (SWAp) function as a mechanism to delegate certain operations to others. For example, in Tanzania, donors participating in the PRBS and SWAp take turns as the lead donor and represent all donors in communicating with the Tanzanian government.

Denmark, Finland, Ireland, and Switzerland are planning to implement mutual delegation of joint programs in various countries beginning in FY2005/06 (Killick et al., 2005).

P3 - DEALING WITH THE COST OF HETEROGENEOUS AID SCHEMES

Canada. In 2002 CIDA established an internal working group on program assistance to study the reasons why the current aid system could not participate in program assistance from contractual, legal, and financial perspectives. The working group looked at other bilateral and multilateral donors and extracted the necessary conditions for financial assistance. The study found that changes in internal rules were required to allow payments based on the achievements of performance targets instead of reimbursements of expenditures or advance payments. As a result, they considered creating a new organization within the Canadian government's Finance Committee Secretariat to raise the maximum amount of advance remittances and reduce the frequency of accounting reports by recipient governments.

New Zealand. New Zealand's accounting system underwent a drastic reform in 1994 based on the idea of New Public Management (NPM). First, a three-year projection was required for each budget item. This ensured continuity in aid planning and administration and made it easier to predict budget allocations. Second, NZAID was allowed to exceed the budget by up to 10 percent or carry up to 20 percent of its annual budget over to the next fiscal year. Through these measures NZAID was released from the pressure of being tied to the donor country's fiscal year and acquired flexibility to respond to every possible situation including unexpected problems in developing countries. Such flexibility is necessary for partnerships.

Germany. Germany was known for its technical assistance in specific areas such as vocational training, but during the past 10 years it has successfully

expanded this narrow strength to capacity development and has broadened the scope of its cooperation. For example, in order to have more flexibility to deal with local situations, Germany has decentralized its organizational structure and increased the number of local staff hired in recipient countries. It also gave the function of coordinating multiple aid implementing agencies to local organizations. It is also trying out program and fiscal assistance. While Germany has shifted its narrowly-defined technical assistance to broader capacity development, DAC has pointed out insufficient coordination among local agencies and insufficient policy harmonization with recipient governments (OECD, 2005b). These issues may have emerged because Germany did not recognize the necessity for dialogue as acutely as did Sweden, including organizational culture. At any rate, Germany has been fairly successful in reducing the cost of heterogeneous aid schemes through organizational and institutional reforms.

If we look at donor country efforts to develop partnerships from the perspective of Organization Theory and Exchange Theory, these efforts are defined by various factors. If there are organizational constraints or an exchange relationship cannot be established, donors may not see any value in partnership, however, more than a few countries have found ways to improve aid efficiency and effectiveness by reducing various costs associated with partnerships. Cost adjustments require a commitment to partnerships and confidence in other donors and recipient governments as partners. In general, however, if a donor follows the policies suggested by the Paris Declaration and the DAC New Development Strategy, it is not difficult to find organizational reforms and exchange opportunities. The following section discusses the conditions necessary for Japan to develop partnerships and measures that could move the country in that direction.

3-5. Measures that Japan can take

This section examines how Japan could enhance its partnerships based on the three defining factors: (1) organizational constraints, (2) failure of exchange relationships, and (3) different aid philosophies and methods.

(1) Measures to overcome organizational constraints

Four possible measures deal with factors that can be explained by Organization Theory. First, multiple policy agencies and implementing agencies will function more efficiently and effectively if they are merged at appro-

priate levels. Clarification and efficiency of decisionmaking processes within an organization are essential for effective partnerships. The adverse effects of a compartmentalized organizational structure that hinder the formation of partnerships should be eliminated.

Second, even if the first measure is impossible to implement, it is important to share information and knowledge within multiple policy ministries and implementing agencies, or among local embassies and resident offices and central ministries and headquarters. To ensure policy coherence, they will need to share an overriding objective and priorities, and systematically align the activities of each organization in each sector to that objective. It is clear from Germany's example that this issue cannot be solved by simply promoting decentralization and giving leadership to local offices from an organizational perspective. Internal coordination is a prerequisite for, and therefore in a sense more important than, partnerships with other organizations. Japanese aid agencies have created ODA task forces at the local level and are now enhancing cooperation. If delegation of authority is added to these mechanisms, it may open a door for greater local leadership.

The third alternative is to conduct experiments in regions and countries where incentives to promote partnerships exist. From a perspective of using partnership as a tool, Japan is the lead donor in many Asian countries but often remains a medium-sized donor in Africa. It is indeed possible to share internal and exterior motives to use partnerships to enhance one's own influence. In any aid scheme area, it is possible to build a system where the current aid schemes and organizations strengthen partnerships for the common goal of poverty reduction.

Finally, in an organizational culture repeated actions and learning to implement aid projects will produce better impacts. Aid specialists are necessary not only in implementing agencies but also in policy ministries, especially in human resource management. They need to be developed from within over a long period. In the same context, promotion of personnel exchanges between policy ministries and implementing agencies should also be continued.

It takes time to build partnerships and the necessary skills are always evolving. Many donors trying to deal with these issues are consolidating aid agencies in low-income countries while their representatives actively develop partnerships locally. In the aid systems of Japan, Germany, and France where policy ministries and implementing agencies were separate and multi-layered, ingenuity was needed to build a system where field experience is

directly reflected in new policies. In a sense, the lack of this ingenuity has been hindering the decisionmaking mechanism that promotes change and improvements in aid organizations. We need to create new channels of communication that reduce the distance between the field and policymaking. For example, when JICA experts return to Japan they should be able to directly report to the executive officers of MOFA's Economic Cooperation Bureau if necessary, in addition to regular debriefing sessions at JICA's operational departments. This cannot be realized if organizations concentrate on performing routine tasks under established lines of authority. An organization needs to be more open and dynamic so that policymakers can interact and share knowledge with local staff, experts, and consultants who are often more creative and work closer to the field.

(2) Measures to overcome the failure of exchange relationships

For exchange relationships, we considered the following equation in the previous section:

$$\text{Prob}(P) = \alpha - p\beta - q\gamma \quad \text{and} \quad q=1 \quad \dots\dots\dots (3)$$

If an exchange relationship can be expressed by this equation, measures we can take to promote partnerships are those that increase α (benefits gained by an exchange relationship) and/or decrease $p\beta$ (lost benefits due to the relationship) and γ (commitment to different aid philosophies).

When one believes that there will be unseen benefits in the future and/or there are moral values, ' α ' becomes larger. In terms of future benefits, can Japan expect any from Africa, for example? The answer is probably not much, at least in a materialistic sense. Japan is unlikely to import oil from Africa, and Japanese business investments are not expected to increase much in the region except in South Africa. This makes it clear that it is important to find moral values and form a national consensus around them so that the government can commit to partnerships. To do so, sufficient budgets should be allocated for serious but easy-to-understand public relations campaigns and educate the public on the importance of development.

Next, in order to reduce ' $p\beta$ ' one needs to adjust the three parameters described in the previous section: ' p_1 ' (communication cost), ' p_2 ' (cost of not being able to rely on others), and ' p_3 ' (cost of heterogeneous aid schemes). First, in order to reduce communication costs, we need a focused skill development effort as SIDA has done. To promote partnerships and implement effective program assistance, a donor must have regular dialogue with vari-

ous stakeholders in the recipient country, conduct baseline studies, and monitor progress to detect changes at various levels. If a donor can't carry out that kind of multi-layered communication, it would not be able to provide program assistance. To provide program assistance, Japan should study the past efforts of SIDA. Also, Japanese aid professionals need to acquire the ability to develop logic based on clear policies, presentation skills, and foreign languages.

We can begin to address the cost of not being able to rely on others by overcoming the polarization between Japanese bilateral aid and multilateral aid. For multilateral aid projects, Japan participates in appraisals as a Board member but does not demand any further involvement. For bilateral aid, however, the Japanese aid system tries to confirm its impacts and accounting evidence unilaterally. The demarcation between bilateral and multilateral aid, however, does not reflect the needs of developing countries accurately. Japan should recognize that there is a gray area between them, and that area is indeed the fertile ground for partnerships.

Partnerships in individual low-income countries involve both bilateral and multilateral donors. The 'p2' (cost of not being able to rely on others) will not change unless there is a fundamental change in this recognition. More specifically, it is necessary to follow the example of New Zealand and make the General Accounting Office, the Foreign Relations Committee, and the Budget Committee of the Diet understand how harmful it is to force Japanese budget systems on developing countries. Once a fundamental understanding and agreements are shared within the government, this problem may cease to be the huge obstacle as it is now.

The 'p3' (cost of heterogeneous aid schemes) is perhaps the most difficult to deal with. Japan's aid projects take unique forms in comparison to other donors. Japanese institutions are not designed to target rural societies of low-income countries. For example, it is difficult for them to make contributions to current budgets of recipient governments and use local experts and resources. The rigid 'blueprint' approach that tries to carry out initial plans faithfully is also a problem. Sector programs do not exclude projects, but other countries have pointed out the problems of projects and either shifted to programs or incorporated program approaches. Projects can take various forms, however. Japanese projects need to be more flexible and expansive so that they can adapt to the situations of low-income countries.

(3) Measures to deal with different aid philosophies and methods

For 'γ' (commitment to a different aid philosophy), Japan's development philosophy in Asia has rejected the idea of directly transferring resources and income to the poor. Instead, Japan has sought to increase the productivity and efficiency of the economy and the society, and to achieve the objectives of a development agenda through subsequent income redistribution. This philosophy is based on Asian experience where economic and social infrastructure that were most suitable to each development stage were built and organically linked to markets, either by design or coincidence. Ownership and self-help of recipient countries were also emphasized. Are donors who have focused on economic development and infrastructure, such as Japan, unsuitable for partnerships? The answer is no. For instance, there are coordination examples in Indochina where the Asian Development Bank built highways and Japan built bridges.

Since the 1990s, Japan has shifted its focus partly to the social sector and is expanding aid in maternal and child health and basic education. The same can be said for human security and an emphasis on Africa. If Japan's aid philosophy and areas of strength shift or expand, the force with which Japan clings stubbornly to 'γ' may be reduced. Development philosophy depends on historical context. In the East Asian experience of the 1970s and 1980s, the partnership principle did not function very strongly. However, it is unclear just how effectively this East Asian experience translates to Africa in this decade. If we think positively, Japan's identity as a donor is to digest the past Asian experience and at the same time formulate a broader philosophy for new subjects in a new age.

The demarcation between bilateral and multilateral aid is strictly artificial. Bilateral and multilateral donors work together in some areas. As reduction of absolute poverty and basic support in social sectors take the center stage of aid to low-income countries under the Millennium Development Goals (MDGs), we can expect that Japan will be increasingly required to actively participate in partnerships. Therefore, the aid philosophy that Japan has maintained in relatively wealthy developing countries and production sectors in the East and Southeast Asia will not be completely rejected. At this point, Japan needs to keep this philosophy functioning in Asia and at the same time be flexible enough to have additional perspectives around the MDGs. Also, there are occasions when the general philosophy of Japanese individuals and organizations to support self-help and self-reliance becomes important in the areas of partnership to pursue the MDGs. Even if they want to make com-

ments based on that philosophy, the Japanese can't do so effectively if they are not inside the partnership system. As such, the effective way to reduce 'γ' is not to deny Japan's traditional philosophy. It is a multi-faceted stance that allows Japan to decide whether to explicitly advocate its aid philosophy or to gradually advocate it as a framework of reference in the forum of partnerships.

If, however, Japan is a minority in the partnership forum, there is a concern that Japan may not be able to advocate its own aid philosophy and methods at all.

In relation to Exchange Theory, partnership has political implications. Foster (2002) explains, rather optimistically, that donor aid coordination has permeated from the global dimension to the project dimension under partnership policies. On the other hand, Klees (2001) warns that forcing a consensus on sector programs in the name of partnership may make donor positions stronger and more monolithic, but the donor community will be affected by the unequal distribution of power within itself. As Bray (1999) and Brinkerhoff (2002) have pointed out, the assumption that a partnership is formed by an equal relationship between partners does not necessarily hold in a context where asymmetric power dictates the character and form of a partnership that is already constrained by organizational and political limitations.

If we accept this asymmetric power, it is possible to imagine a scenario where dominant donors that lead in the area of partnerships - for example, the U.K. and the World Bank - oppress the organizational identities and priorities of other donors so that they can explain their goals and intentions with a louder voice.¹¹ Under current conditions, it is probable that a partnership among donors may formulate an unequal exchange relationship. Very small donors may face organizational and political struggles every day in such an environment, but with its aid volume, Japan has a good chance of being able to exert an influence from within. Therefore, to believe that participating in a partnership itself will hinder the efforts to explain and develop Japan's unique aid philosophy and ideas vastly underestimates the presence of Japan as a donor.

In low-income country social sectors such as primary health care, primary education, and food security, and especially sub-sectors that deal with life and death of people and basic human rights, it is always difficult for a donor

11. An organizational identity is, according to Brinkerhoff, an element that comprises partnership together with mutuality, and signifies a rationale to select certain partners.

to achieve a sizable impact by itself. Germany, from the perspective of partnerships, has emphasized the environment and governance in which other donors were not deeply involved (OECD, 2005b). This is one way of continuing project assistance, but it may be difficult for Japan to stick to a code of conduct that is completely different from mainstream aid because it has provided relatively little aid in the area of governance, and is rather very interested in social sectors. However, depending on the sub-sector issue, Japan's aid philosophy to respect the local situation sometimes can be effective, as it was for the Strengthening of Mathematics and Science in Secondary Education Project (SMASSE) in Kenya. The judgment and selection as to which sub-sector is suitable for project assistance, should be carefully examined when Country Assistance Plans are prepared.

There are many points to note in making a commitment to partnerships based on the OECD/DAC guidelines. We have also identified many points to be improved in Japan's aid traditional-type systems and organizations. Table 3-5 summarizes proposed measures in light of above discussions.

Table 3-5. Measures to structure the partnership

Factors	Problems	Measures
Restriction from organisational reason	Disintegration of the development system → restriction localization in of development system→Unable to engage in the partnership	<ul style="list-style-type: none"> ● Integration of several ministries and implementing agencies. ● Information and knowledge sharing with in the organization or between the local embassy / office and the ministry/headquarters. ● Establish priorly the experimental organization in particular regions or countries (i.e., low income countries, Africa) ● Establish more speedy communication means between experiences in the field and policy making process.
Failure of exchange relation	Less gain from the exchange relation, or lose more than gain domestically	<ul style="list-style-type: none"> ● Popularize the moral value of development aid-the common goal of the partnership ● Intensive human resource development involved in development assistance. ● Reconsider the extreme concept in bilateral and multinational aid. ● Develop the flexible did scheme for low income countries. ● Develop the special aid scheme for the social sector where the local human resources and institution building play an important role.
Belief in the different philosophy and policy in development assistance	Have much of its own philosophy or experience enough to be negative toward the partnership	<ul style="list-style-type: none"> ● Review or reform the aid philosophy which enable to respond flexibly to the situation in each country or region. ● Build the confidence in exercising influence inside, even if the partneeship is supported by the unven exchange relationship.

3-6. Conclusion

Against the backdrop of poverty reduction and MDGs, there is a prominent trend in which donors build partnerships with the governments of developing countries, civil society, and other donors to turn policies and strategies into preparation, implementation, and evaluation of effective programs. Reforming the public sector and decentralizing institutions calls for program support and donor coordination. Under these circumstances, Japan took a leading stance with Scandinavian countries in the preparation of the DAC New Development Strategy in 1996 but is not necessarily at the center of the reform trend at present.

We assume that Japan cannot build a result-oriented and accountable system in line with current aid trends unless the system of Japanese aid for low-income countries is drastically reformed. Therefore, we probably need to use partnerships as a spring board to reform Japanese aid. Partnerships improve the overall effectiveness of development aid and at the same time contribute to the accountability of Japanese aid. Many factors are needed for poverty reduction efforts to produce results, and most are beyond the scope of bilateral donors and general development aid (DAC/OECD, 2001 : 58).

In this chapter we have considered how Japanese aid can move forward with partnerships. It would be ideal if Japanese aid could be expressed by this equation:

$$\text{Prob}(P) = \alpha - p\beta - q\gamma \quad \text{and} \quad p=1 \quad \dots\dots\dots(4)$$

In this ideal situation, the additional cost of a partnership (p) is infinitely close to one and aid system constraints are almost totally eliminated. What remains is the net gain/loss by entering a partnership ($\alpha - \beta$) and the aid philosophy or methods that change depending on the target region, country, and sector ($q\gamma$). Parameter ' q ' is flexible depending on the target of aid and maturity of the partnership, and in fact can be positive or negative. Aid policies for individual countries need flexible capacities to discern the timing and situation of the country and sector in question.

From the perspective of Organization Theory, bringing ' p ' closer to 1 signifies that an aid agency promotes learning by its members and acquires an ability to change continuously to maintain competitiveness. In a sense, this means that the Japanese aid system and organizations become a 'learning organization' (Senge, 1990). This concept refers to an evolving organization whose members continuously expand their abilities, constantly incorporate

new and more universal ideas, and openly learn from each other.

Finally, it is important to establish 'q' as a mind-set. In the previous section, we assumed that 'q1' because the Japanese aid philosophy is uniform based on its experience in Asia. However, we need to change the 'q' in order to pursue more effective partnerships. Referring to differences between aid coordination in Africa and Asia, Takahashi (2001) said, "Beginning with how the governments are formulated, there is a marked diversity in the aid receiving environment in developing countries . . . We should not think that there is one universal answer that works both inside and outside of Africa." Japanese aid should determine 'q' as a principle that allows free and rational actions based purely on ideas and strategies and not on organizational constraints. Therefore, what determines the structure of a partnership is a general solution that includes three elements: character of the target (country, sector), actions of partners (recipient societies, donors), and experience and philosophy. The future direction requires aid policies and institutions that enable these elements to achieve the best combination.

Annex 1

The interdisciplinary concept of partnership is defined as a collective mode of behavior in an organization where various sectors interact with each other to achieve a common goal. Its origin is the 'social partnership' in the framework of Organization Theory (Waddock, 1991). In the world of business, partnership is defined as "an alliance of individuals who agree to act as joint owners of a for-profit business" (Winicur, 1993 : 1). Typically, partners agree on the terms of a partnership in writing and all income is returned to partners as earnings from the business. Larkin (1994) recognized several types of public-private partnerships. In some cases a partnership is led by the private sector, in others it is dominated by the public sector, and in others the government and businesses are equal partners. He also argued that a successful public-private partnership means something more than superficial goodwill and requires cooperative efforts based on mutual respect that do not arise automatically (Larkin, 1994 : 9).

In the area of health and social services, Poole (1995) defined partnership as "an alliance of two or more persons, groups or organizations that aims to achieve a common objective which cannot be achieved individually" and said it can be characterized by "common membership, democratic participation and shared responsibilities" (Poole, 1995 : 1). According to Poole, partnership is distinguished from cooptation, cooperation and coordination: it is

similar to collaboration, and demands peaceful alliances even with ‘enemies’ if they are in the interest of the beneficiary population. Focusing on this political nature of partnership, Balloch and Taylor (2001) said that it means both pain and gain at the same time and requires commitments and investments. Partnership has “the potential to make the delivery of services more coherent and hence more effective” but it “has a lot of tensions and needs to find a balance between the flexibility to begin a new business and accountability for public spending, a balance between leadership, expertise and participation, and a balance between consensus and diversity” (Balloch and Taylor, 2001 : 7).

In the area of education, there is a tendency to focus on the necessary factors of effective partnerships rather than on a rigid definition. For example, Patterson et al. (1999) list six factors for effective partnerships: mutual trust, honest communication, common objectives, flexible governance, and a culture of positive tension and inquiry. Mullinix (2001) built on these concepts and elaborated the partnership process which follows three phases: pre-partnership, emergent partnership, to full partnership. According to Mullinix, the maturity of a partnership can be measured in terms of focus of interaction, activities/projects/programs, period and origin, benefit, trust and respect, organizational structures, organizational strategies and information access, locus of influence, and written agreements or contracts.

Annex 2

At the factual level, an exchange affects the dynamics of interaction, is reconstructed based on the consequences, and is recognized as a concept of equal or unequal exchange. At the normative level, it is examined from the perspective of social norms which institutionalize and regulate the acts of exchange themselves, and it displays the cultural characteristics of the acts themselves. At the structural level, the act of exchange is examined with a focus on social relationships that support it.

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Infrastructure Finance: A New Direction for Yen Loans¹

Yasuhisa Ojima²

Nowadays, as long as we are in an industrial country, we have perfect roads and railroads, so we can live without being aware of the importance of infrastructure. But when we go to other countries we cannot expect so much, and that is when we are reminded how important it is.

— Nanami Shiono (2001) Roma-jin no Monogatari, Shinchosha

4-1. Aid effectiveness and yen loans

Increasing aid to help achieve the Millennium Development goals is one aim of the international development community. From a macroeconomic perspective, however, how much more aid can be absorbed?

A series of empirical analyses have examined that question. The question of whether or not aid contributes to economic growth and poverty reduction is both old and new, but a typical empirical analysis posits economic growth as the explained (dependent) variable and estimates the coefficients of a set of explanatory (independent) variables including aid (typically with the OLS or GLS method). Many recent empirical analyses seem to follow a popular pattern — they assume the relationship between growth and aid to be nonlinear and find a saturation point that represents the limit of absorptive capacity by a recipient country. When a nonlinear relationship is assumed, a

1. In preparing this manuscript, I presented the draft as “Infrastructure Finance in East Asia” at a seminar held by Kyoto University Graduate School of Economics. At that time I received valuable comments from Mr. Naohiro Kitano (Kyoto University) and the participants. I would like to thank them for their contributions, however, I am responsible for any and all errors. Also, much of Sections 2 through 5 of this chapter is based on Ojima (2006a).

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square of 'aid' is included as an explanatory variable that makes the estimated equation a quadric function (and the coefficient for the aid squared variable negative). The point where the marginal effect of aid on growth becomes zero is considered the saturation point.

In an efficient survey of the literature by Clemens and Radelet (2003), the saturation point expressed as an aid/GDP ratio was measured at 33.7 percent by Collier and Dollar (2002) and 22.8 percent or 26.8 percent by Hansen and Tarp (2000). They concluded that the aid/GDP ratio generally falls between 15 and 45 percent. These empirical analyses that look for a saturation point do not distinguish the issues of donors who provide aid and those of developing countries that receive aid, but those who analyze donor motives include Alesina and Dollar (2000) and Sawada and Yamada (2003). On the other hand, studies that analyze aid effectiveness in developing countries include *Assessing Aid* by the World Bank and Burnside and Dollar (2000), which is particularly influential.

There have been two attempts to analyze the effectiveness of yen loans:

- *Study on the Economic Development of Developing Countries and the Role of Yen Loans* (Economic Planning Agency of Japan, 2000), and
- *The Effects of Japan's Economic Cooperation on the Development of Asian Economies* (Kenichi Kawasaki, 2002).

The first paper empirically analyzes whether yen loans promote economic growth and whether fungibility exists. It concludes that "Estimation (regression analysis) of a hundred countries confirmed that continuous provision of aid amounting to 1 percent of the GDP of the recipient country has an effect of increasing the growth rate by 0.23 percent. After examining the aid coefficient based on this, we can expect that the increment of GDP will be comparable to the amount of aid in eight years, and the increment will be about twice the amount of aid provided in 16 years." The second paper uses the CGE (Computable General Equilibrium) model and reports that between FY1996 and FY2000 yen loans increased GDP by 1.65 percent in Vietnam, 0.71 percent in the Philippines, 0.5 percent in Indonesia, 0.49 percent in Thailand, 0.2 percent in Malaysia, and 0.12 percent in China, with the annual average ranging from about 0.1 percent to 1.6 percent. In these empirical analyses the transmission mechanism through which yen loans contributed to economic development is treated as a black box.

However, looking at Japanese assistance to the ASEAN countries as a typical example that shows the characteristics and contributions of yen loans, there have been two main transmission mechanisms:

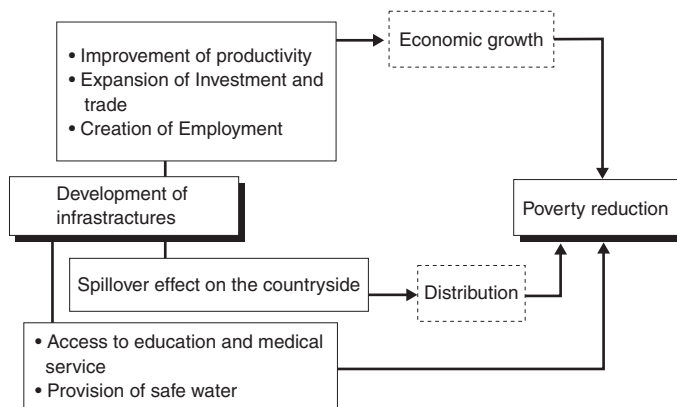
improving the capacity to export and attract investment by supporting the economic infrastructure; and ensuring the social stability through rural development.

This chapter discusses how we can make the traditional pillar of ‘yen loans – infrastructure’ more effective while focusing on the role of infrastructure in alleviating poverty and growing an economy.

4-2. Renewed recognition of infrastructure

Infrastructure³ is the foundation for a country’s economic and social activities and supports the economic and social development of developing countries through various channels. Poverty reduction was recognized as the overarching goal⁴ in the United Nations Millennium Declaration of 2000 and the Millennium Development Goals (MDGs) that were adopted in 2001 as its roadmap. While poverty itself has multiple aspects, the first goal of the MDGs emphasizes income poverty. Infrastructure is thought to contribute to poverty reduction mainly through three channels (Fig. 4-1).

Figure 4-1. Relationship between development of infrastructures and poverty reduction



Source: Yamada, Ojima, et al. (2005)

3. For the purposes of this chapter, infrastructure primarily means economic infrastructure such as transportation, energy, telecommunication, water and sanitation, and includes physical facilities (roads, power plants, etc.) and services (transportation services, electricity services, etc.).
4. Reduce by one-half the world’s poverty ratio of 28.3 percent as of 1990 to 14.2 percent by 2015.

The first channel is poverty reduction through economic development. Efficient transport infrastructure (roads, railroads, ports), reliable energy infrastructure, a safe water supply and sanitation infrastructure, and modern communications reduce transaction costs of business and improve productivity. Sophisticated urban infrastructure enables densely populated cities to exist and brings agglomeration. These achievements also improve the investment climate and potential for long-term economic development by attracting foreign direct investments and expanding international trade.⁵ Sustained economic growth, in turn, contributes to poverty reduction in developing countries (Dollar and Kraay, 2002).

The second channel is the contribution to the distribution of economic growth. For example, transport infrastructure that connects urban and rural areas is essential for the rural economy to meet the demands of the urban economy for agricultural and other products. Through the interaction between the rural and urban areas, it also helps the effects of growth to affect rural areas. Infrastructure plays an essential role in realizing the mechanism of the classic two-sector model of agriculture and industry.

The third channel includes direct contributions to the poor. Building the transport infrastructure makes it easier for the poor to access education and medical services, and access to markets can provide opportunities to improve their livelihood. Electricity improves the quality of medical services⁶ (e.g., preservation of vaccines in refrigerators, lighting for operating rooms), and may free rural women and children from long hours of gathering firewood. A supply of safe water is essential for the health of the poor.

While there is a limited number of infrastructure-related indicators in the MDGs, infrastructure does play an important role in achieving them through these three channels (Leipziger et al., 2003; Willoughby, 2004). However, there have not been sufficient empirical analyses on the quantitative effects of infrastructure because infrastructure channels are multifac-

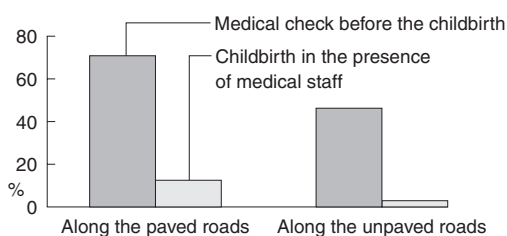
5. Building infrastructure does not automatically lead to economic growth. To understand the relationship between investments and economic growth as 1:1, see Easterly (1999). In addition to infrastructure building, other factors such as the country's policy and institutional environment and human capital would be necessary. On the other hand, even if these other factors exist, poor infrastructure would be a bottleneck for growth.

6. For example, *Energy for the Poor* (DFID, 2002b) suggests that support for energy can address many issues including economic growth, poverty reduction, education, health, and gender. It shows that when electricity (economic infrastructure) is supplied, women and children spend less time on housework and gathering firewood, which increases women's opportunities for economic activities (promotion of gender equality) and children's opportunities to attend school. It also shows that supply of electricity makes it possible for hospitals to preserve vaccines and other medical supplies in refrigerators.

eted. In addition, there are many issues, including the time-lag between infrastructure building and manifestation of its benefits, the difficulty of capturing small benefits that spread widely, and the lack of systematic data. While these challenges remain, several attempts have been made to provide some limited empirical analyses.

For example, the Japan Bank for International Cooperation (JBIC) conducted an empirical analysis on the relationship between roads and medical services. A study in Indonesia found that 70 percent of pregnant women living along a paved road had a health checkup before childbirth, but for women who lived along an unpaved road the figure was only 46 percent (Fig. 4-2). Building roads increased the consultation rate and led to better maternal health.

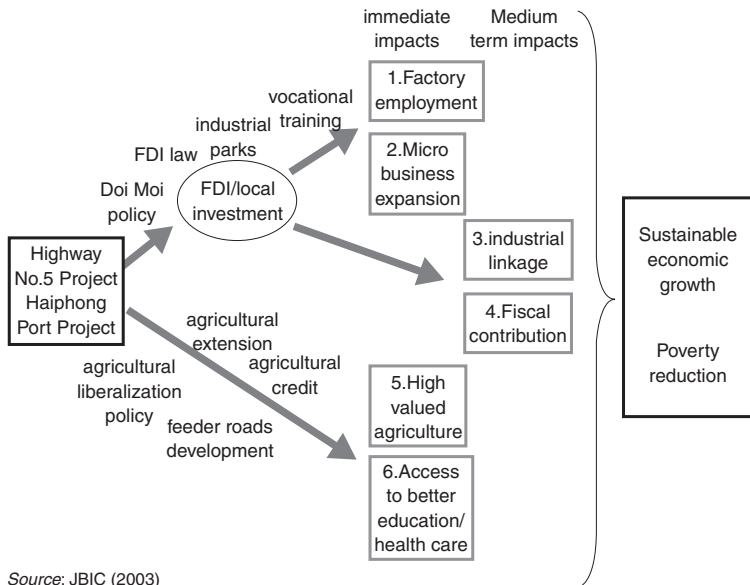
Figure 4-2. Road construction and medical service



Source: Yamada, Ojima, et al. (2005)

JBIC also conducted a study of transport infrastructure projects in northern Vietnam and confirmed the effects of building transport infrastructure (Haiphong Port and Highway No. 5) through the following six transmission mechanisms (Fig. 4-3):

- Factories were built along the highway with foreign direct investments (FDI) and local investments, creating about 40,000 jobs.
- Industrial parks were built along the highway, which led to the creation of small- and medium-sized enterprises and hence jobs.
- Stronger industrial links were forged between local and foreign enterprises.
- Fiscal impacts included increased tax revenues from foreign companies.
- Increased production of high value-added agricultural products improved the livelihood of farmers.
- Access to education and health services was improved.

Figure 4-3. Infrastructure effect : case of northern Vietnam transportation infrastructure

Of course these effects were not achieved solely by building infrastructure — their extent depends on the recipient country's commitment (the Doi Moi policy, introduction of foreign investment law), links with other projects (development of industrial parks, vocational training, rural credit finance), and other factors. Infrastructure is an essential condition for economic growth and poverty reduction, but we must not forget that policies, institutions, and human resources that can effectively utilize the infrastructure are necessary to increase its effects.

4-3. Demand for infrastructure

Even though infrastructure is being built in developing countries, it is not enough. For example, the capacity of power facilities is far less than that of developed countries. The average power consumption per capita (2001) is only 1,054 kilowatt hours (kwh) in developing countries, while a person in an industrialized country consumes an average of 8,876 kwh. The average number of telephone lines in developing countries is about one-fifth the number in developed countries, and the degree of road development (road density) is about one-fourth (Table 4-1). The UN Millennium Project (2005) points out

Table 4-1. Infrastructure stock in developing countries

	Electricity capacity (per thousand) (kW)	Electricity consumption (per person) (kWh)	Number of telephones (per thousand)	Road density (Km/Km ²)	Access to safe spring (%)
	2001year	2001year	2001year	2000year*	2000year
Developing countries	272	1,054	95	0.15	78
East Asia	223	921	59	0.15	71
Europe	992	3,425	217	0.11	88
Central Asia					
Latin America the Caribbean	431	1,709	150	0.15	88
Sea					
Middle East	338	1,411	86	0.08	84
North Africa					
South Asia	99	426	31	0.94	76
Sub-Saharan Africa	105	394	29	0.08	62
	2,044	8,876	501	0.58	99

*the most recent numbers available between 1996 to 2000 are adopted

Source: World Bank (2004)

that a significant amount of investment — a big push — in major infrastructure is needed to escape the poverty trap. For this reason, there is a robust demand for infrastructure building in developing countries. Fay and Yepes (2003) estimate that the developing countries need a total annual investment of about US\$ 460 billion by 2010. Regionally, the annual demand for capital in East Asia (including Southeast Asia and the Pacific) between 2005 and 2010 is estimated to be about US\$ 200 billion (ADB, JBIC, and WB, 2005), and the annual demand in Africa is estimated to be about US\$ 20 billion (Commission for Africa, 2005).

4-4. Current state of infrastructure financing

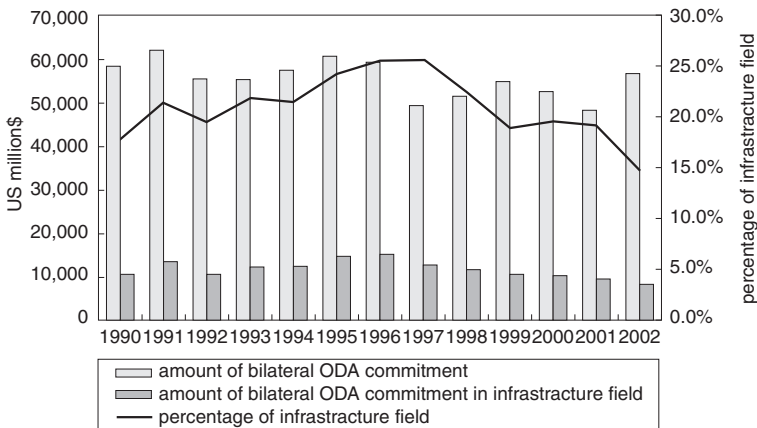
What is the current state of financing to deal with these infrastructure gaps? Funding sources necessary for building and maintaining infrastructure include domestic funds (government revenue and infrastructure user fees, etc.), private funds, and development assistance (Official Development Assistance or ODA). The British Department for International Development (DFID) (2002b) estimates that about 70 percent of the funds necessary for

new investments in infrastructure are from domestic sources, while 25 per cent are from the private sector and 5 percent from ODA.

(1) ODA financing

Support for infrastructure from ODA declined during the 1990s (Fig. 4-4) for three main reasons. First, the increasing focus on poverty reduction as the objective of development assistance gave rise to the notion that infrastructure was just hollow buildings and often a white elephant. The focus of aid also shifted to social sectors and the emphasis was placed on program assistance to improve the policy and institutional environment. A second factor was the expectation that private funds would support more infrastructure development. The background that influenced this thinking was: (i) poor performance of public institutions in developing countries (deficits, excess staffing); (ii) the movement to promote private sector participation led by the World Bank and IMF; and (iii) involvement of private investors in financing infrastructure. The third factor was the increasingly vocal concern over negative effects of large-scale infrastructure projects on the environment and society.

Figure 4-4. percentage of bilateral ODA (into infrastructure field commitment)

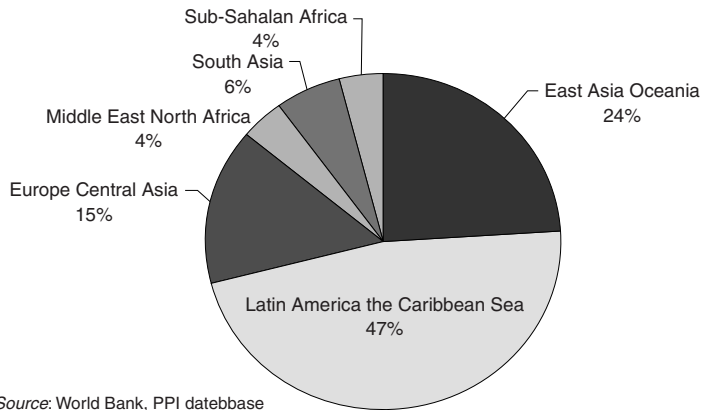


Source: OECD/DAC, CRS data base

(2) Private funds

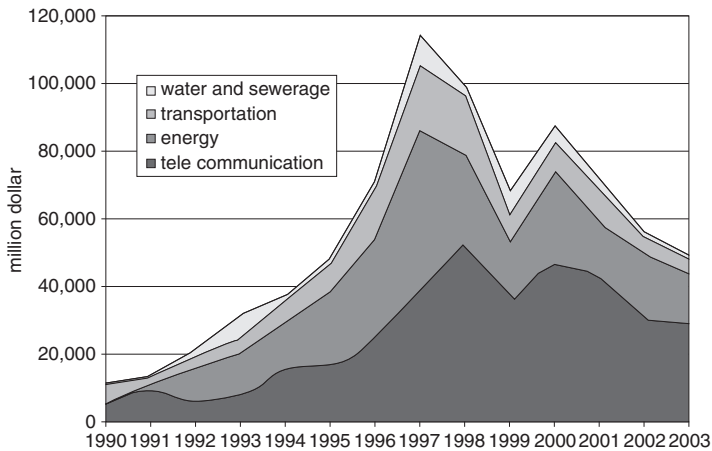
What have been the trends with private funding that were the subject of high expectations? Between 1990 and 2003, more than US\$ 780 billion was invested in more than 2,700 private infrastructure projects in developing countries

Figure 4-5. regional trend of private sector involved infrastructure (1990-2003)



Source: World Bank, PPI database

Figure 4-6. sector trend of private sector involved infrastructure (1990-2003)



Source: World Bank, PPI database

and economies in transition. These investments were not evenly distributed in different regions. About one-half of the total went to Latin America and the Caribbean (most of which were asset divisions) while one-fourth went to East Asia and the Pacific (mainly to new projects), and about 4 percent to Sub-Saharan Africa, the Middle East, and North Africa (reflecting their poor progress in reforms) (Fig. 4-5). The distribution was uneven across sectors as well, and most investments went to the communication and power sectors.

The total investments peaked at US\$ 114 billion in 1997 as the unbundled private supply model gained popularity, but declined to about US\$ 50 billion in 2003 (Fig. 4-6).

One reason for this sharp decline was the deterioration of infrastructure investments and private financing markets, which were affected by currency/financial crises and corporate scandals involving the flag-bearers of privately financed infrastructure such as Enron. Also, effective regulations and attractive domestic conditions (such as market size and density) are necessary for infrastructure investments, and even if these conditions are met, there is a significant risk to investing in the infrastructure sector of a developing country.

(3) Domestic funds

Building infrastructure with domestic funds is mainly financed by public investments, however, the debt/fiscal crises of the early 1980s forced fiscal adjustments on many countries that had a significant impact on public infrastructure investments (Estache, 2001). For example, the public investments as a percentage of GDP in Latin America declined between 1980/84 and 1995/98 from 3.1 percent to 0.2 percent in Argentina, from 5.0 percent to 2.0 percent in Bolivia, from 3.7 percent to 0.6 percent in Brazil, from 3.1 percent to 1.7 percent in Chile, from 2.5 percent to 0.4 percent in Mexico, and from 2.0 percent to 0.6 percent in Peru (Kessides, 2004). As discussed above, private financing was expected to fill the gap left by this decline, but did not fare as well as expected.

In order to increase public infrastructure investments there has been a movement to ensure 'fiscal space' by improving the methods to establish fiscal targets in IMF programs. One of the issues is whether fiscal targets should be set in terms of the current fiscal balance instead of traditional indicators — the overall fiscal balance and the level of public debt (IMF, 2004).⁷ The aim is to make it easier to continue public investments even under fiscal austerity by separating them from the current fiscal balance because productive public investments promote economic growth, increase future government revenue, and pay off in the long run. Another aim is to ease the competition between infrastructure spending and other spending (for social insurance and health care, for example) by separating them. However, the IMF's

7. Other issues include whether public enterprises that are run on a commercial basis should be included in fiscal indicators, and whether the debt sustainability analysis should include potential risks associated with Public Private Partnership (PPP).

basic objective is to pursue short-term macroeconomic stability by managing the overall fiscal balance and to ensure long-term debt sustainability by managing the level of public debt (Hemming and Ter-Minassian, 2004).

Infrastructure user fees collected from consumers can also be an important source of domestic funds, but there is a problem — in developing countries the fees are too low in comparison to infrastructure costs. One reason is that fee levels involve complicated interests of the government, service providers, and consumers, for example, one argument against fee increases is political — infrastructure users belong to high- or middle-income groups. The second reason is a concern about the ability of poor people to pay, which makes it more difficult to raise the fees. There may be a third reason — it is possible that inefficient management is inflating infrastructure costs.

4-5. Private participation and privatization from industrial organization theory

The infrastructure supply model is a prerequisite for infrastructure financing. If the government or public corporations build and own infrastructure and provide infrastructure services, infrastructure financing would be mainly handled by public funds. On the other hand, if they adopt an infrastructure supply model that uses private sector initiatives through privatization and private participation, the emphasis of infrastructure financing shifts to the mobilization of private funds. This section discusses the significance and deficiencies of these models in light of the characteristics of infrastructure.

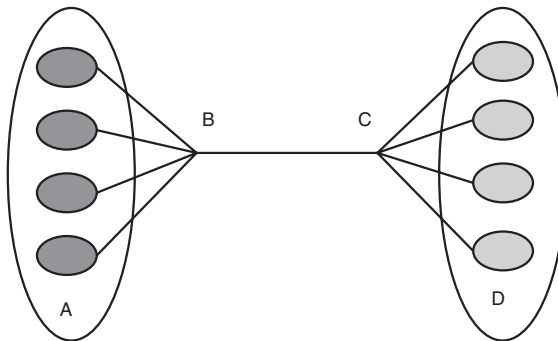
(1) Infrastructure network

The most important characteristic of infrastructure is that it works as a network.⁸ To provide infrastructure services such as power, transport, and communication services, there must be a network of infrastructure facilities. For example, electricity services can be provided to consumers only if a network includes generation (A in Fig. 4-7), transmission (B-C), and distribution (C). In a similar vein, water cannot be supplied without a network that includes water sources (reservoirs, rivers) (A in Fig. 4-7), aqueducts or pipelines (B-C), water treatment plants (C), pumping stations and distribution reservoirs (C), and water distribution networks (D).

8. Yoda (2000) is a good book that attempts an economic analysis of these network industries using the findings of the old and new industrial organization theories.

For transportation or communication, services are provided not through unidirectional (from upstream to downstream) networks like these, but through bidirectional road or communication networks (for example, A and D in Figure 4-7 can be regarded as intra-city lines while B-C can be regarded as inter-city lines). Significant infrastructure investments are necessary to maintain or improve network facilities that produce these infrastructure services.

Figure 4-7. characteristic of infrastructure : network



(2) Integration

After World War II the typical model for providing infrastructure services such as power, communication, transport, water, and sanitation was state owned and vertically integrated, not only in developing countries but also in industrialized countries (Kessides, 2004). On what theoretical grounds did this integrated public supply model become mainstream? The main reason is the features of a natural monopoly found in infrastructure. It is well known that natural monopolies cause market failures and provide the rationale for public intervention, and the fundamental factors that give rise to these natural monopolies are economies of scale, economies of scope, and sunk costs.⁹

Infrastructure network facilities (A through D in Figure 4-7) require fixed capital investments to keep pace with an expansion such as an increase in the number of users or an increase in the network distance, but the average cost per unit of goods or services declines as the scale of production related to infrastructure expands. This is an example of economies of scale. Under these conditions it is more efficient to have a monopoly rather than

9. For details, see Uekusa (2000).

multiple entities that provide infrastructure services. Next, in providing infrastructure services, vertical integration of functions from production to delivery to consumers can avoid redundant investments and ensure technical consistency. Benefits including reduced costs can be enjoyed and economies of scope come to exist. Furthermore, network supply facilities not only need significant fixed investments but are also difficult to resell. This characteristic increases the sunk costs and creates entry barriers. These factors give rise to a structure where new barriers to entry are formed, infrastructure services tend to be provided in a monopolistic manner, both of which increase the risk of monopoly pricing that is socially undesirable. On the other hand, consumers demand infrastructure services that are affordable and of high quality because they are essential for their lives.

The rationale for a vertical integration model can also be examined by comparing it to unbundling infrastructure networks (the vertical separation model). Unbundling these networks can create coordination problems (Kessides, 2004), which can be explained with the New Contract Theory.¹⁰ Infrastructure assets are difficult to resell and their transactions are limited — they have ‘asset specificity’. Also, contracts associated with unbundling (e.g., concession contracts to be described later) cannot provide for every possible event that may occur in the future, and therefore by definition are ‘incomplete contracts’. Asset specificity and incomplete contracts may cause a hold-up — in an infrastructure investment, for example, the contractor may take opportunistic actions such as breaking the contract or demanding renegotiation after the investment becomes a sunk cost. There is an incentive for vertical integration from the perspective of avoiding transaction costs associated with preparing complete contracts (which stipulate all future obligations in advance) in order to avoid this problem.

There are also technical reasons to adopt a vertical integration model, especially for electricity because it requires sophisticated system adjustments to balance the demand and supply in real time (Kessides, 2004). Also, electricity is a semi-finished product at the time of generation — it is not a

10. While conventional economics develops its argument based on markets, the Contract Theory analyzes economic phenomena in the dimensions of ‘transactions’ and ‘contracts’. Roughly speaking, it consists of the Complete Contract Theory (the conventional contract theory) and the Incomplete Contract Theory (the new contract theory). The former presupposes the existence of complete contracts and mainly deals with the issues that arise from asymmetric information such as moral hazards and adverse selection. On the other hand, the latter starts from the circumstance where complex contracts are not written and deals with how institutions, laws, and organizations complement contracts, and other issues (Yanagawa, 2000).

complete product unless it is transmitted (Nanbu and Nishimura, 2002). These technical characteristics rationalize the vertically integrated structure in the power sector.

The state owned, vertically integrated public supply model can provide economies of scale and scope while avoiding the problem of monopoly pricing (market failure) and issues of economic and technical coordination.

(3) Unbundling

The integrated public supply model in developing countries came under pressure from various quarters. The first pressure came from developed countries. Beginning in the late 1970s, deregulation in the US, restructuring and privatization in the UK, and the EU directives for broader liberalization and creation of a single market gave rise to a strong trend for privatization that took developing countries and transitional economies by storm. The second pressure was born out of macroeconomic factors in developing countries — the debt and fiscal crises in the early 1980s (Estache, 2001). The debt problems of the 1980s were caused by a deterioration in the ability to pay, so many countries were forced to accept structural adjustments, including fiscal reform (e.g., conditionalities such as reducing subsidies to state-owned enterprises in order to reduce fiscal deficits), which had a significant impact on public infrastructure investments.

The third pressure came from a microeconomic factor of developing countries — the performance of public entities, including public corporations. Many of these companies were often run by managers who were appointed because of their political loyalty (and not their abilities), pursued multiple, ambiguous, and conflicting goals, and could not utilize investment funds effectively. In addition, price controls were imposed without considering their impact on the fiscal performance of public entities, damaging their abilities to mobilize investments and provide reliable services (Kerf and Smith, 1996). The fourth pressure was technological innovations that improved the technologies for producing and delivering infrastructure services. The reduction in sunk costs also contributed to introduction of competition in infrastructure networks. For example, new technologies reduced the minimum scale of power generation plants and helped reduce investment costs and time required for planning and construction. Also, low-cost, small-scale generation plants enable micro-grids that supply power to consumers from a short distance, so they might reduce the dependency on transmission and distribution networks. In the telecommunication industry, technological

innovation changed the entire cost structure of the industry.

Under these pressures, developing countries also began to adopt an unbundled private supply model that utilizes private sector resources. This model has three characteristics: (i) sector restructuring and unbundling; (ii) regulatory reform; and (iii) competitive bidding or auctions (Guasch, 2004). Let us look at the thinking behind the first characteristic, sector reorganization and unbundling. With infrastructure networks, we assumed that a sector includes a single network (e.g., generation → transmission → distribution, in the case of a power network) that has a tendency for a natural monopoly. There is, however, a need to examine each component of this network to determine if it lends itself to competition. Some components of a network may have conditions conducive to the introduction of competition. For example, the production component and downstream distribution component of utilities, parts of a telecommunication network (long-distance services, etc.), and operation of a railroad network have some sunk costs but they can be reduced with technological innovation, and therefore are suitable for competition (Table 4-2).

Table 4-2. Uncompetitive and components of infrastructure network

Industry		
Electricity	High pressure gas pipeline Gas supply	Power generation Supply to end users
Gas	High-tension transmission Load power distribution	Production Supply to end users Storage
Tele communication	Local loop (subscriber line)	Long-distance Mobile, Value-added service
Railroad	Track, Signal infrastructure	Railroad management and maintenance
Water and sewerage	Distribution pipe network waste water collection network	Water purification Sewage treatment

Source: Kessides (2004)

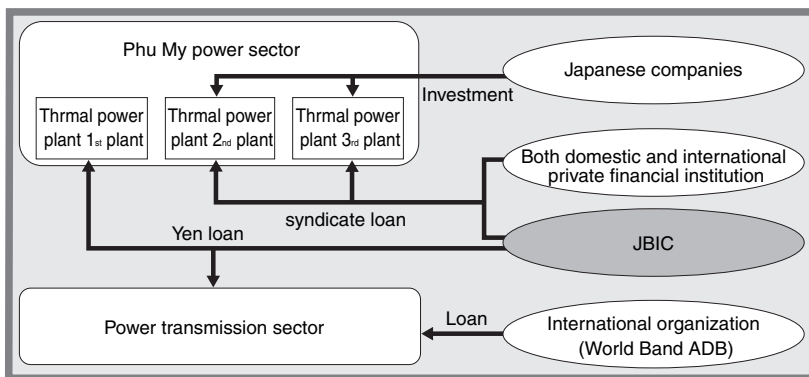
This was how an idea was born — we should introduce competition by unbundling the naturally monopolistic components and potentially competitive segments. In the power sector, the transmission and distribution components would be separated from the generation component; in the communication sector, the local loop would be separated from long-distance, mobile, and value-added service components; and in the railroad sector, fixed equipment such as rail tracks and signals would be separated from administration and maintenance. On the other hand, infrastructure facilities that are a non-

competitive component are called ‘bottleneck’ or ‘essential’ facilities and cannot be used for other purposes. Therefore, these facilities represent fixed costs, a large part of which is sunk costs. They are also difficult to reproduce from technical and economic perspectives. While bottleneck monopolies remain in these components and would be administered by the public sector,¹¹ regulatory reform would be required to avoid the adverse effects of monopolies. As main components of regulatory reform, independent regulatory bodies would be established and rules would be introduced to regulate the supply of infrastructure services by the private sector. This is the second of the three characteristics mentioned above. The third point, adoption of competitive bidding or auctions, is required to select the most efficient private operator while eliminating the monopoly rent.

(4) Role of yen loans

Under the structure described above, what roles can ODA play in the unbundled infrastructure model that seeks to mobilize private resources and privatization? One approach is to build bottleneck facilities. If a private company does so, it would not only have significant costs, but also create a risk that the company may enjoy the monopoly rent by monopolizing the bottleneck. For example, when JBIC assisted the Phu My Thermal Power Plant Project

Figure 4-8. Function of yen loan : case of Vietnam Phu My thermal power plants



11. Some think that even if ‘competition in the market’ is not feasible, this non-competitive (naturally monopolistic) component can be turned into a competitive component by ‘competition for the market’ through competitive bidding and regular rebidding. However, there are still remaining issues such as the concern that incomplete contracts might invite opportunistic renegotiation and that it is difficult to monitor operators who made successful bids.

in Vietnam, it provided yen loans to the transmission component, the bottleneck facility in the power sector (Fig. 4-8).

This was a precondition for implementing the power plant component with the private sector initiative because electricity revenue cannot be obtained without adequate transmission facilities. If the generation sector is liberalized and transmission charges are set at high levels, certain power plants may be at a cost disadvantage compared to other plants. A yen loan was also provided for the construction of the first thermal power plant. Its construction with a yen loan had a demonstration effect and contributed to reducing investment uncertainties. As a result, the BOT (: Build-Operate-Transfer) method was adopted for construction of the second and third power plants.

(5) Mobilization of private resources and privatization

The discussion about mobilization of private resources and privatization can be summarized as follows. The unbundled private supply model unbundles infrastructure networks, implements regulatory reform including the establishment of regulatory agencies, and selects private operators through competitive bidding or auctions, but there are several points that we should be careful about (Kessides, 2004; Guasch, 2004).

First, we should note that unbundling is not a panacea. We need to consider the market size and density of the country in question as a precondition for unbundling. If the market size and density are not sufficient for many operators to function there will not be enough competition. Many developing countries have a problem of small markets. For example, in the power sector the peak system load is less than 150 MW in 60 developing countries, 150 to 500 MW in 30 countries, and 510 to 1,000 MW in 20 countries. Even a size of 1,000 MW is too small to introduce competition. Another factor necessary for unbundling mature and developed network facilities that have already reduced the necessity for new investments that tend to cause incentive problems. However, conditions in many developing countries and transition economies are just the opposite. These countries need significant new investments because the networks are underdeveloped or not properly maintained and upgraded. Therefore, the fact that a state-owned system was not effective does not necessarily mean that unbundling, privatization, and mobilization of private resources are appropriate for all developing countries.

Second, even if unbundling is appropriate, we must note that it is difficult to alter the structural choices dealing with the degree of vertical integration,

regulations, and institutions after the private sector has participated (the problem of irreversibility). If the rules of the game of private participation are not made clear in advance, private sector demands risk premiums and the cost of privatization and mobilization of private resources rises. If the government does not commit to the structure of the infrastructure industry, the private sector thinks that the government itself may take opportunistic actions. We also need to carefully design the regulation of non-competitive components (bottleneck facilities) in order to harmonize competitive and non-competitive components.

Third, we need to pay attention to the problem of renegotiation in the concession system. For example, more than 1,000 concessions were granted in Latin America and the Caribbean between 1985 and 2000, but more than 30 percent of all concessions were renegotiated (Guasch, 2004). The main challenge of an infrastructure concession is to prepare a complete contract that covers every contingency that can occur over time. However, an incomplete contract is inevitable if we consider technical complexities and economic uncertainties. When the parties face new information or experience, adjustments through a renegotiation are necessary and also meaningful in terms of trying to find new risk sharing between the public and private sectors. On the other hand, as discussed earlier, the incomplete contract and specificity of infrastructure assets create the potential for opportunistic renegotiation by both the government and the private concessionaire. The renegotiation may benefit the private operator (the hold-up problem). If the private operator demands renegotiation soon after the concession has been granted and the government refuses, it would lead to cancellation or interruption of the concession and risk increasing the transaction costs of future concession contracts. Faced with this dilemma, sometimes the government has no choice but to agree to renegotiation.

Fourth, we need to ensure that the poor can receive and benefit from infrastructure services. The main incentive for private companies to participate in infrastructure projects is commercial motivation, so they tend to focus on the communication and energy sectors where they can realize returns relatively early and easily. They also tend to be interested in projects at the central government level and not those at the local level. Therefore, the government needs to offer incentives in order to ensure that the poor will benefit from infrastructure services (DFID, 2002b).

4-6. Loans or grants?

This section examines financing modalities. The debate is intensifying about whether financing to achieve the MDGs should be grants or loans. The Meltzer Report submitted to the US Congress in 2000 (Meltzer, 2000) proposed that multilateral organizations such as the World Bank should concentrate on the least developed countries, stop loan operations, and provide only grants. In fact, the International Development Association (IDA) of the World Bank Group has increased the share of grants in its financial assistance in recent years.¹² Also, the International Finance Facility (IFF) we discussed in the previous section assumes that funds are provided through grants. Moreover, Bulow and Rogoff (2005) proposed a complete changeover by multilateral organization from loans to grants, together with concrete methodologies.¹³ These developments show that grants are becoming the mainstream.

(1) Significance of loans

Has the significance of loan assistance been really lost? Let us examine the keys to the effectiveness of loans from several perspectives (Ojima, 2004).

Sustainability and stability of aid volume. If donors are to provide the financing necessary to achieve the MDGs and provide those funds in a sustainable manner, loans allow them to re-use loan payments and therefore reduce donor burden, thus enabling a relatively large amount of aid. Odedokun (2004) points out that mainstreaming grants has reduced the amount of funds received by developing countries (on a gross disbursement basis), while aid funds have been volatile and unpredictable (Bulir and Hamann, 2003). Loans, which are provided in a stable manner because they put less fiscal burden on donors, tend to function as a stable source of development funds for recipient countries. Unquestionably, Japanese yen loans, which have been provided in step with China's five-year development plans, for example, made stable contributions to the performance of Asian countries

12. In the 13th IDA Replenishment (agreed in 2002), 18 to 20 percent of its financial cooperation would be grants and the share would further increase to about 30 percent in the 14th Replenishment (agreed in 2005).

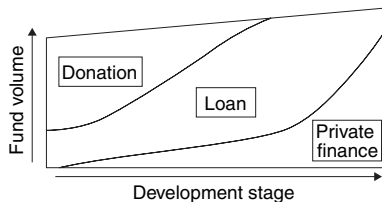
13. Specifically, they recommend that multilateral organizations should stop providing new loans (the first stage), stop borrowing from private capital markets (the second stage; existing debt would be repaid with the repayments from developing countries), and change their capital from callable to paid-in (the third stage). The gradual process would take about 20 years. Furthermore, they claim that this approach can be applied not only for multilateral donors but also bilateral donors when they withdraw from loan operations.

in terms of growth and poverty reduction.

Discipline by loans. Assistance is provided based on a loan agreement between a donor and a recipient country. The donor appraises projects and programs beforehand, later confirms how the funds are being spent, and monitors progress of the project based on the loan agreement. The recipient country also follows such a procedure. In the case of a loan, the project usually becomes ‘on budget’ and undergoes a rigorous screening process in the country. Most yen loan recipient countries require approval by the cabinet or parliament. These factors provide an incentive for the recipient country to try to recover the cost. An empirical analysis showed that an increase in loans leads to an increase in government revenue of the recipient country, which can be interpreted as a government-wide effort for cost recovery (Clements et al., 2004). These fiscal responses are also important to ensure that achievement of the MDGs will be sustainable.

Development stages. Development is a continuous, nonlinear process that involves economic and social changes. The process of procuring development funds also evolves continuously from grants to loans to private financing (graduation from aid), and these stages often overlap (Fig. 4-9). In a process that begins with aid dependency and eventually reaches the final stage of market dependency where most funds are raised from markets, loan assistance plays a role in supporting developing countries during a period of transition before they have access to financial markets. For example, loan assistance helps improve the financial and debt management abilities of the recipient country through transactions such as receiving and repaying loan proceeds. The formation of credit culture is essential to participate in the international financial system. When adequate information about investment opportunities and debt servicing capacity is provided to a loan provider, the history of credit exposure and repayment helps improve the credit worthiness of a recipient country.

Figure 4-9. Development stage of development funds



Source: Yamada, Ojima, et al. (2005)

Impact on economic growth. Has the impact of loan assistance been demonstrated? Sawada et al. (2004) separated aid into three types — loans, grants, and technical assistance, and estimated the effects of each type to promote growth. They found that loan assistance is always positive regardless of the policy environment, and said that the effect of loan assistance may be stronger than the others. This “suggests that loan assistance has a stronger incentive effect for more efficient investments and policy interventions that lead to higher growth” (Sawada, 2004).¹⁴

(2) Complementarity of loans and grants

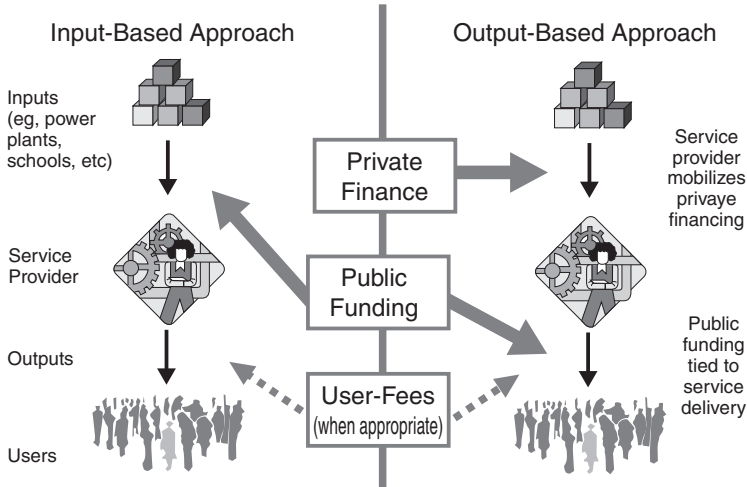
The circumstantial evidence for the effectiveness of loans does not directly prove that loans are better than grants. As a precondition for the success of loans, debt must not become excessive. Also, some elements of loan effectiveness can be realized by grants. For example, it is possible to strengthen screening and monitoring functions using grant agreements or even include grants in the recipient country budget. The Paris Declaration released in March 2005 established an international goal of including aid projects in budgets, whether they are supported by loans or grants. Loans and grants can be complementary, and it is important to find the best way to combine them. For example, a pilot project funded by a grant could confirm feasibility, followed support by a loan. (In an afforestation project, for example, a grant could be used to select a species to plant, which would move to geographical expansion funded by a loan.) It is essential that such a transition happen systematically in order to be effective. An empirical analysis also found that an appropriate combination of loans and grants has positive effects on growth (Iimi and Ojima, 2005).

One attempt to improve the delivery of infrastructure services while taking advantage of the complementarity of loans and grants is ‘output-based aid’. To realize high-quality infrastructure services at reasonable prices, this type of aid effectively uses financial resources by assigning different roles to public and private funds. The role of public funds is to take what have traditionally been inputs (e.g., constructing power plants and schools) and make them subsidies to outputs (e.g., realizing service delivery to the poor). This

14. Sawada (2004) compared welfare (direct income assistance) and workfare (income support that requires recipients to work) as incentive effects of debt and theoretically formulated the latter’s screening functions and incentive effects (Besley and Coate, 1992), as well as contrary research on the disincentive effects of debt (Krugman, 1988), and points out that there is a need for further theorization of incentive effects of loans.

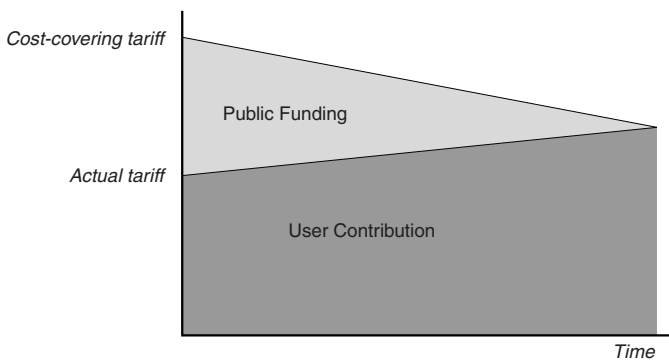
includes (i) cost of new connections, (ii) supporting the transition to a cost-recovery fee structure, and (iii) supporting target groups, including the poor (Fig. 4-10).

Figure 4-10. Concept of Output-based Aid



Subsidies themselves are supposed to be time-limited. Initially, significant subsidies may be needed to reach the cost recovery threshold, but as the threshold is lowered by efficient management and the level of recovery from users gradually increases, it is expected that eventually subsidies will no longer be necessary (Fig. 4-11). When selecting a private operator (a com-

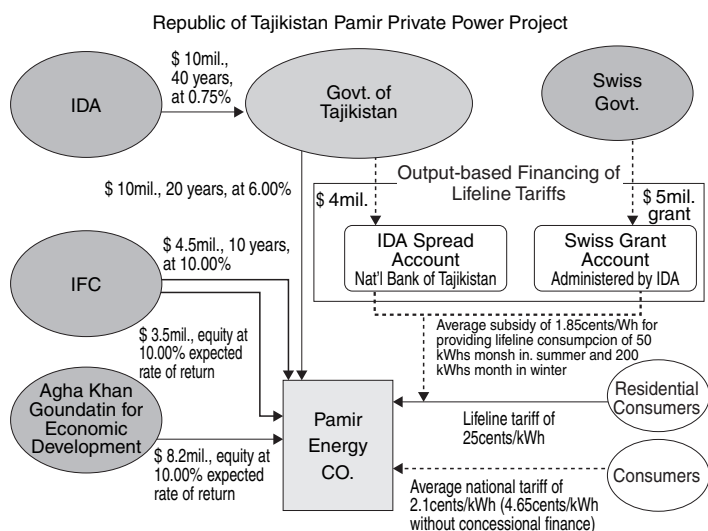
Figure 4-11. Concept of temporary subsidy



pany or NGO) by competitive bidding, quality of services and level of required subsidies are used as selection criteria.

One concrete example is the Pamir Private Power Project in Tajikistan (Fig. 4-12). The Republic of Tajikistan is one of the poorest of the former Soviet republics (per capita GNI of US\$ 180) and the target area of this project, Gorno-Badakshan region, is especially poor with a population of 250,000 and a monthly average household income of US\$ 27. The natural environment is also harsh, with the temperature dropping to minus 30 degrees Celsius in winter.

Figure 4-12. Overview of Republic of Tajikistan Pamir Power Project



Source: Jacquet and Klein (2005)

An unstable power supply disrupts education and health services, and they also have an air pollution problem. For these reasons, they plan to stabilize the power supply by expanding the Pamir Hydropower Plant (from 14MW to 28MW), rehabilitating the power transmission and distribution networks, and taking water from Yashkur Lake. This project targets the poor and uses a blend of public and private funds by providing subsidies (IDA's back finance) to ensure affordability to the poor while ensuring the sustainability of the power company. Notable is the role of subsidies through grant financing, which keep the service price low at 0.25 cents per kwh. However, it is expected that the subsidy eventually will be abolished (Fig. 4-11).

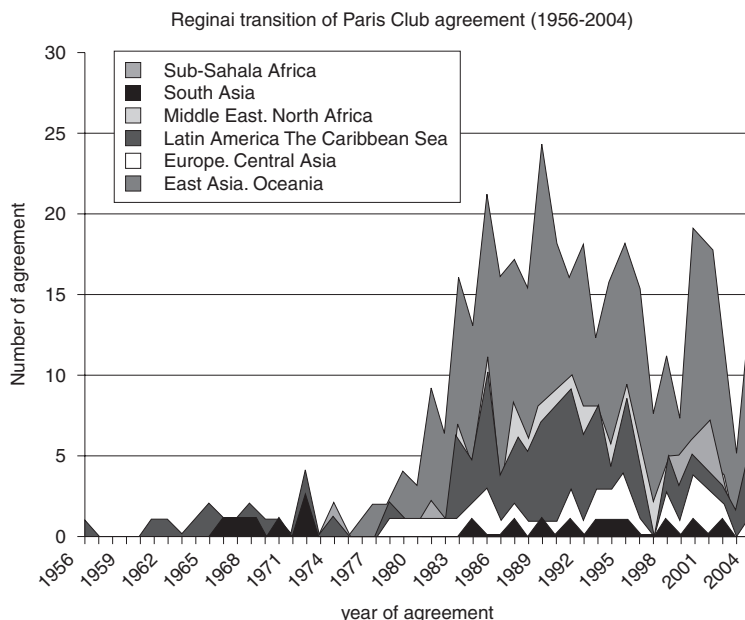
Of course, this scheme has some problems. For example, (i) there is a risk that subsidies will be provided to unintended people, (ii) operation of the system will be less efficient than expected and the cost recovery threshold will not be reached, and (iii) as a result, the subsidies are treated as permanent. However, assistance that combines loans and grants exploits their complementarity.

(3) Assistance for Africa

Finally, in the debate about loans and grants is the issue of debt. Incurring debt is not necessarily bad for a developing country because borrowing allows economic entities, including the government, to smooth consumption and make productive investments, thereby aiding the economy. On the other hand, there have been many debt crises such as the accumulated debt in Latin America during the 1980s, the debt problem of low-income countries, especially the Heavily Indebted Poorest Countries (HIPCs) during the 1990s, and the declaration of default by Argentina in 2001. The Paris Club, a group of industrialized countries that deals with debt problems of developing countries, has agreed to 376 debt relief packages since its inception in 1956 through the end of 2004. Figure 4-13 shows the regional breakdown of debtor countries that received relief based on a Paris Club agreement. There were very few Paris Club agreements during the 1960s and the 1970s, but the number suddenly increased after the 1980s. While the share of Latin American countries increased after the mid-1980s following the accumulated debt problem, the largest share until now always belonged to Sub-Saharan Africa. This is why we can say that the problem of HIPCs in the 1990s was the debt problem of Sub-Saharan Africa. In Africa, yen loans are still provided to Morocco, Tunisia, and a few other countries, but providing loans to Sub-Saharan Africa remains a challenge.

The HIPCs Initiative functions as an international framework for debt reduction, but one target of the Millennium Development Goals is to complete the process of the Initiative (to be precise, to reach the completion point). Even in Sub-Saharan Africa, some countries, including Tanzania, Uganda, Ethiopia, and Ghana, have reached the completion point. Reaching the completion point means that the concern about excessive debt has been alleviated for the time being, which raises the question of how to support the former HIPCs. Should we expect that debt reduction will be repeated and refrain from providing new yen loans?

We should not refrain from providing new loans across the board.

Figure 4-13. Transition of Paris Club agreement

Source: Ojima (2006b)

Instead, we should stick to two basic points. First, before providing a loan (*ex ante*), avoid the problem of adverse selection by screening recipient countries properly with the condition that they must try to improve themselves. Second, after the loan is provided (*ex post*), use the monitoring functions of project management so that the recipient country continues its efforts for structural improvements. When it comes to supporting HIPC's whose debt has been reduced, preconditions for new aid should include stronger screening and monitoring, along with an examination of current debt. We should be cautious about providing loans to countries whose debt has been reduced, but on the other hand, they cannot rely on grants forever. It is not realistic, however, to leapfrog from grants to private funds because private investors would consider it was too risky. Japan should show its unique character by making good use of loans as well (Ojima, 2006c).

One assistance method that takes advantage of Japan's unique character is the Enhanced Private Sector Assistance (EPSA) for Africa, which is being proposed by our government under the leadership of the Ministry of Finance. One idea included in EPSA is to provide up to US\$1 billion of yen

loans in five years through the African Development Bank. This assistance will likely target an improved investment environment, including infrastructure and private sector development, among others. We can also expect that the partnership with the African Development Bank will strengthen screening and monitoring functions.

4-7. Decentralization and regional finance

As the so-called ‘trinity reform’ is advancing in Japan, the trend of decentralization can be seen everywhere in the world, and developing countries are no exception. Merits of decentralization include: (i) accountability is ensured at a level closer to voters; (ii) increased participation of citizens in public administration (e.g., stronger voice about how tax revenues are spent); (iii) improved capabilities of local governments; (iv) improved local administration services; and (v) increased revenues through the devolution of taxing power to local governments. Especially important are the benefits of infrastructure supply being more responsive to beneficiaries’ needs. On the other hand, disadvantages of decentralization include: (i) destabilization of the macro economy and fewer options in policy implementation; (ii) reduced efficiency from the viewpoint of the entire state; (iii) regional conflict of interest; and (iv) increased income disparity due to the reduced transfer function of the central government. When building infrastructure, we especially need to consider that coordination may not take place at the state level, thus economy of scale may be reduced. In Japan, however, certain infrastructure such as water supplies and sanitation facilities are typically built and maintained by municipalities as location-specific, local public goods. Local governments should be responsible for those infrastructure projects that are local public goods.

Local governments are separated from the central government, and as decentralization has progressed, regional assistance has emerged as a new challenge. The assistance to Indonesia’s Aceh special territory serves as an example, and regional assistance requires political considerations. When loans are directly provided to local governments without a guarantee from the central government, securing repayment may be more difficult. One example of regional assistance is JBIC’s collaboration with the US Agency for International Development (USAID) on water sector assistance schemes in the Philippines.

The first scheme in the Philippines is the Municipal Water Loan

Financing Initiative (Fig. 4-14). It combines an existing yen loan to the Development Bank of the Philippines (DBP), a two-step loan to the Policy Finance for Industrial Pollution Control Project (II), and USAID’s Development Credit Authority (DCA) for the Local Government Unit Guarantee Corporation (LGUGC). A combination of yen loan funds and local private financial institutions (guaranteed by the USAID’s DCA) will finance municipal water and/or sanitation projects. The second scheme is the Water Revolving Fund (Fig. 4-15). Based on a model used at the state level in the

Figure 4-14. Philippines municipal finance

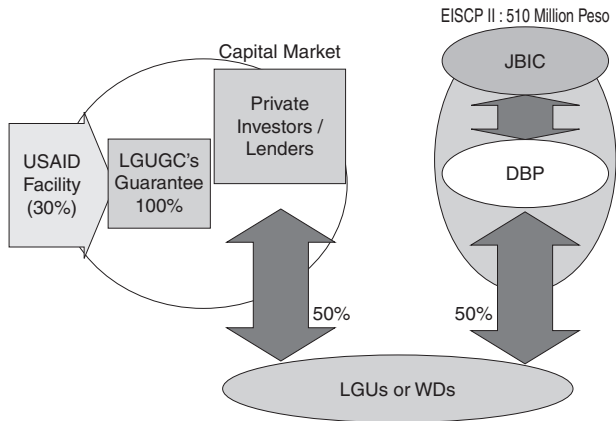
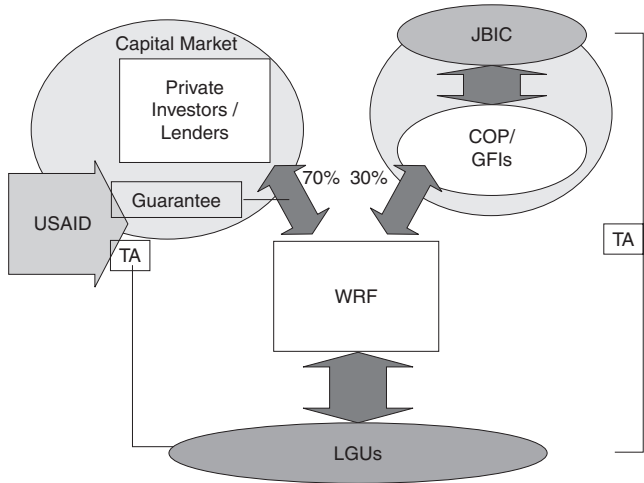


Figure 4-15. Philippines Revolving Fund Framework



US, this is an attempt to create one such fund for the Philippines by using the yen loan funds and the USAID/DCA guarantee scheme. This is still at the conceptual stage and many design issues remain such as the different roles of the central and local governments and the administration of the entire fund, including the private finance portion. Nevertheless, these attempts toward regional assistance are about to move forward step by step.

4-8. New direction for yen loans

The renewed recognition of infrastructure does not mean that we should simply continue traditional assistance for infrastructure. Far from it, we need to confront the trade-off between the social justice of delivering services to the poor and the economic efficiency needed for sustainable service delivery. The financing to build and maintain infrastructure is significant, so it is essential to identify how to strengthen its financing. Under these circumstances, what roles should yen loans play?

First, if we see infrastructure as a network, we need to continue our assistance for 'bottleneck' facilities. This is a precondition for the mobilization of private resources and privatization. Specifically, the transmission component of the power sector, the intra-city component of telecommunication, the distribution network of water supplies, the sewer pipe network of sanitation, and the tracks component of a railroad are examples of the bottleneck facilities. If we are to build an integrated infrastructure network due to the conditions such as market size and market density, assistance to components other than the bottleneck facilities may be necessary.

Second, we need to advance collaboration between projects funded by loans and grants instead of seeing them as opposing forces. In strengthening delivery of infrastructure services to the poor, subsidies to cover connections and other costs are indispensable, and such subsidies are better financed by grants, not loans. We obviously need to strengthen coordination between yen loan projects and grant projects, but beyond that, we need a mechanism to simultaneously provide a loan and a grant for one project or program. It is possible, albeit from a different perspective, to combine assistance by equity investment with technical assistance (for example, a JICA expert could participate in the management of an implementing agency in the recipient country).

Third, we need to take a stronger initiative for regional financing. Traditional schemes can handle assistance through central governments, but

as decentralization continues and administrative and fiscal authorities are delegated to local governments, we might need to consider assistance with less involvement of the central government.

Fourth, we need to expand the ODA financing function itself. As the name suggests, yen loans provide funds denominated in yen, but if assistance in other currencies is possible, we would be able to increase development impact, especially if revenue from infrastructure projects are typically denominated in the local currency. One of the causes of the Asian currency and financial crises was the mismatch of currency and terms. If the recipient country could receive local currency loans, it could avoid exchange risks, but the exchange risk is then transferred to the donor as the loan provider. We need to carefully choose a currency that can be hedged (Thai baht, Chinese renminbi, or Malaysia ringgit, for example). The supply of local currency also has a direct effect on the money supply of the recipient country, so we may need to consider consistency with monetary policy.

Other than local currency loans, there is a possibility of guarantees by ODA. The main advantage of this scheme is that we can expect to mobilize domestic savings or encourage the mobilization of foreign private funds. However, the assistance as guarantees does not involve direct financial mobilization on the part of the donor, so we need to examine whether it qualifies as ODA as defined by the DAC. France has argued that assistance by guarantees should be considered as ODA. Their argument can be summarized as follows: (i) although the funds themselves are not provided by a public entity, the reduction of capital costs by a guarantee is essentially created by the public entity (the requirement of public entity); (ii) the assistance supports projects that are similar to those supported by conventional ODA (such as microcredits) (the requirement of development objective); and (iii) the difference between the market interest rate and the interest rate with a guarantee qualifies as a concessional element (the requirement of concessionality). While this point needs to be carefully examined, guarantees also have the potential to become an important tool for infrastructure financing.

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Improving Grant Aid Cooperation Strategy and Effectiveness

Formation of a comprehensive economic cooperation policy

Izumi Ohno¹

In recent years, the focus of international aid has been shifting to grants and to the poorest countries. This has brought, increased expectation in the international arena that Japan's grant aid cooperation would be expanded. Meanwhile, in the domestic sphere the fiscal conditions surrounding ODA budgets (especially the general account budget) remain tight, prompting strong demand that ODA be used effectively and efficiently. This combination of circumstance means that at this time, Japan's grant aid cooperation is being questioned more than ever, both domestically and internationally.

Against this background, this chapter examines the directions and measures Japan might take to improve its grant aid cooperation, taking into account changes in both the internal and external aid environments and efforts to realize the visions of the new ODA Charter. Micro-level improvements have recently been made in grant aid cooperation as part of efforts to reform the Ministry of Foreign Affairs (MOFA) and improve the efficiency of budget administration. These improvements warrant appreciation. However, they are based on existing aid schemes, planning and implementation systems, not on strategic thinking that positions grant aid cooperation within comprehensive economic cooperation policy. To address actively the issues

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important both to Japan and to the international community, such as the promotion of economic partnership in East Asia and support for the least developed countries, it is necessary to consider how to utilize grant aid within a comprehensive vision of economic cooperation. Incremental improvements in the current grant aid schemes are not enough; drastic reforms at the macro-level are essential, such as the establishment of more flexible aid modalities, consideration of different combinations of various schemes including public-private partnerships (PPPs), and building the systems to support these.

This chapter is structured as follows. Section 1 provides an overview of Japan's grant aid cooperation; its history, characteristics (aid schemes, sub-schemes, budgets, allocations by region and country, etc.) and planning and implementation systems. Section 2 describes internal and external debates surrounding grant aid cooperation and the subsequent micro-level improvement efforts based on them, such as the pursuit of better transparency, proper implementation, cost reduction, expansion of evaluations and rapid response to reconstruction needs. Section 3 points out three changes in the international aid environment that became prominent in the late 1990s — (i) increased share of grants in response to the worsening debt problems of poor countries; (ii) changes in aid approaches which accelerated with the introduction of Poverty Reduction Strategy Papers (PRSPs); and (iii) the shift toward an increasing focus on the poorest countries as aid recipients. It — then examines the challenges posed by these changes to Japan's ODA, especially with regard to grant aid. Finally, Section 4 explains that, in order to realize the two-track ODA vision that underlies the new ODA Charter revised in August 2003, it is necessary to formulate a comprehensive economic cooperation policy which will take into consideration the needs of Japan and also of the international society. Section 4 also points a new direction for Japan's strategic utilization of grant aid cooperation and the specific measures necessary to it.

5-1. Characteristics of Japan's grant aid cooperation

(1) Overview of history, aid schemes and sub-schemes

Grant aid cooperation is a modality of aid which provides funds with no repayment obligation (grants) to recipient developing countries whose income levels are low². As a tentative criterion for determining eligibility, the

Japanese government accepts the eligibility criterion of the International Development Association (IDA), provider of concessional financial assistance such as interest-free loans and grants within the World Bank Group. In terms of sectors, the basic human needs (BHN) related sectors such as health care, sanitation, water supply, primary and secondary education, and rural and agricultural development as well as environmental protection are the main pillars. Projects in these sectors generally yield low economic return and are therefore difficult to finance with loans; nonetheless, they are considered to be directly linked to the improvement of living standards of the people and to contribute to human resource development.

Grant aid cooperation began with the introduction of food aid in 1968 followed by general grant aid in 1969. General grant aid was at that time centered on general project grants, project-type cooperation in a wide range of sectors, including health care, education, agriculture, livelihoods improvement, the environment, transportation and telecommunication (mainly funds for building facilities and purchasing equipment and materials). In the 1970s, emergency grants, fisheries grants, cultural grants and aid for increased food production were introduced one after another. Later, more tailored grant aid cooperation was introduced to meet the needs of different developing countries. In 1978, the Japanese government introduced the debt-relief grant scheme³ which provided grants to developing countries facing serious debt repayment problems. (When the country repays its yen loan debt, a grant in the amount of the repayment or a part thereof is provided.) In 1987, the government introduced the non-project grants scheme (grant aid to support the improvement of economic structure) which provides foreign currency assistance (balance of payments assistance) to import goods urgently needed to promote structural adjustment policies under the advice of the World Bank and the International Monetary Fund (IMF). In 1989, the grant aid for grass-roots human security scheme was introduced to support relatively small projects implemented by local municipalities, educational and medical organizations and NGOs in developing countries. In 2002, the grant aid for Japanese

2. The primary eligibility for receiving grant aid in FY2005 was based on per capita GNI as of 2003 to be \$1,465 or less, but this condition is applied flexibly in consideration of the needs and diplomatic impact (MOFA document).

3. In 1999 in response to the adoption of the Enhanced HIPC (Heavily Indebted Poor Countries) Initiative, the government used the same scheme to launch the HIPC Assistance Grant. However, amid the global trend of debt reduction, the government later abolished the debt-relief grant scheme and switched to debt forgiveness in 2003.

NGO projects scheme was adopted to support economic and social development projects and emergency humanitarian assistance projects implemented in developing countries by Japanese NGOs.

Based on this history, current grant aid cooperation is categorized as follows: (1) general project grants, (2) non-project grants, (3) grant aid for grassroots human security, (4) grant aid for Japanese NGO projects, (5) grant aid for human resource development scholarship, (6) fisheries grants, (7) cultural grants, (8) emergency grants, (9) food aid and (10) grant aid for underprivileged farmers (until FY2005 known as aid for increased food production). Among these schemes, general project grants hold the largest share, accounting for 43% of total grant aid cooperation in the FY2005 initial budget. Figure 5-1 and Table 5-1 give overview and explanations of these schemes.

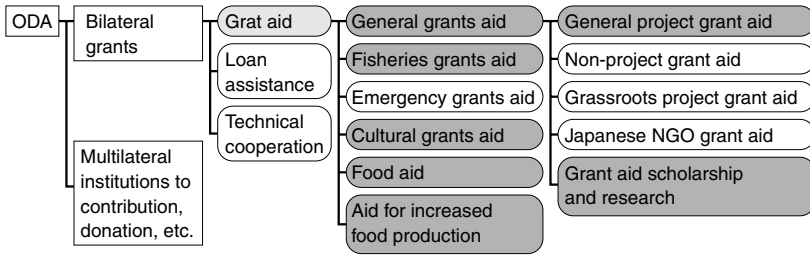
(2) Budget changes

Grant aid cooperation is financed entirely by the general account budget. Most technical cooperation funds, with the minor small exception of the special account, also come from the general account budget. Sources of yen loans consist primarily of the capital subscription from the general account budget, borrowing from the fiscal investment and loan program (FILP) and loan repayments from developing countries. The amount of assistance for the general account budget, which supports grant aid and technical cooperation, is determined each fiscal year and the budget must be used in the same fiscal year.

Under tight fiscal conditions, Japan's ODA budget has been reduced six years in succession since FY2000. The cumulative effect of this tightening, is a decline of more than 30% below the peak recorded in 1997⁴ (general account budget basis). The grant aid budget has also been reduced more than 30% over the same period. According to Figure 5-2, which shows changes in the operation budget, the reduction of the overall ODA budget has led to an especially large reduction in general project grants. The budget for emergency grants, on the other hand, is increasing on an operational basis. This is due, partly to reconstruction assistance for Iraq and

4. The ODA budget for FY2006 (the general account portion) was also reduced by 3.4% year-on-year. Japan had been the largest ODA donor in the world since 1991, but the US has been the top donor since 2001.

Fig. 5-1 Japanese ODA and grant aid



Source: Refer to JICA website, “JICA and grant aid” (<http://www.jica.go.jp/activities/jicaaid/ol10.html>).

Note: Gray items are schemes where JICA conducts prior studies and facilitation, based on agreement with MOFA.

Table. 5-1 Overview of grant aid schemes and 2005 budet

Scheme (budet hundreds of million of yen)	Starting year	Summary
Expenses for economic development assistance, etc. (the following includes grants only) (160.598 billion yen)		
General grants (754.8) · regional development · Grant for infectious disease prevention and treatment · Information technology aid · Governance aid · Water resource and environment aid · Anti-personnel mine clearance aid · Child welfare aid · Rehabilitation aid · Human resources development strengthening aid · Etc.	1969	Project-type grant aids in sectors covering basic human needs (social welfare and environment improvement, transportation and telecommunication, medical service and healthcare, education, agriculture and forestry, etc.). It is becoming more common to integrate economic infrastructures (e.g., roads, bridges, ports, telecommunication), which used to be basically dealt with loans before, into the grant aids, taking situations of heavily-indebted poor countries into account.
No-project grant aid (255) · Sector program aid · Grant aid for conflict prevention and peace building · Grant aid for disposal of small arms · Etc.	1987	Provide foreign currency necessary to import materials (balance of payments support). The recipient development can save the surplus of domestic currency brought by assistance fund (foreign currency) as the reserve fund and, after consultation with the Japanese government, use it for the activities that contributes to the economy. Social development (sector program aid uses the reserve fund mainly to the sector projects).
Grant aid for grassroots and human security projects (140)	1989	It started as a small-sized grant aid and changed its name to “Grant aid for grassroots projects” in 1995. It supports the economic. Social development projects implemented by the local government, education and medical institute, and NGO, targeting relatively small-sized projects which is benefi-

		cial at grassroots level (10 million yen at the maximum per project). in 2003, it changed its name to reflect more of the concept of "Human security" and expanded its targeting fields, in addition to traditional BHN, to the peace building and reconstruction support, and emergent humanitarian assistance (the maximum amount was accordingly increased up to one hundred million yen per project).
Grant aid for Japanese NGO's projects (140)	2002	Support social economic projects and emergent humanitarian assistance by Japanese NGO's projects. Social development and (Non-Governmental Organizations Cooperation Division in MOFA, and Japanese embassies).
Grant aid for scholarship and research (40) · Scholarship aid · Research aid	1999	Support developing countries' students to study in Japan and support for the travel and accommodation allowance of the developing countries' and (or) Japanese researchers necessary to promote the research activity in relation to economic and social development issues faced in developing countries.
Grant aid for fishery (56)	1973	To contribute to fisheries promotion in developing countries, offer funding to fishing ships, fishing gears, fishing training facilities, training ships, fishing port facilities, and construction of fishery research facility.
Cultural grant aid (23.7)	1975	Started as a part of international cooperation in relations to cultural exchange, supporting conservation and promotion of culture in developing countries. Support the purchase of necessary equipments and materials for the preservation and utilization of cultural assets and heritages, cultural performances and displays (Cultural exchange Division in MOFA).
Emergency grant aid (307.98) · Grant aid for disaster relief · Grant aid for reconstruction and development · Grant aid for democratization	1973	Started with the emergent assistance for disasters and provide affected people, refugees, and displaced people in natural disasters or civil wars with urgent humanitarian assistance. The fund is either directly to the affected government given or indirectly to international humanitarian assistance organizations (WFP, UNHCR, etc.). It started the democratization support in 1995 (by providing the developing country's government or international institutes with the purchases cost of materials necessary for democracy promotion projects).
Aid cost for increase of food production (15.924 billion yen)		
Food aid (KR) (109.2)	1968	Provide developing countries facing food shortage with the funds necessarily to purchase main crops such as wheat, rice, and corn.
Grant aid for increased food production (2KR) (50.04)	1977	To support the plan to expand food production in developing countries pursuing food self-sufficiency, provide the funds necessarily to purchase

		agricultural materials such as fertilizers and agricultural machines. Changed its name (Aid for expansion of food production) in 2005.
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Source: Refer to ODA website (MOFA), JICA website, "JICA and Grant Aid", and JICS website, "Grant Aid."

Note: In 2007 several new schemes are to be introduced including 'Grant aid for anti-terrorism and security policy' (7 billion yen), "Grant aid for disaster prevention and emergency restoration (3.5 billion yen)," and "Grant aid for community development (4 billion yen)" as new schemes.

Afghanistan and partly to assistance and recovery from the Sumatra earthquake and the Indian Ocean tsunami⁵ of December 2004. The grant aid for grassroots human security scheme was launched in 1989 as a small-scale grant facility with an annual budget of ¥300 million (32 countries, 96 projects). But it has grown rapidly ; its annual budget having reached ¥15 billion in FY2003-04. The average annual number of projects for the three years from FY2002 to FY2004 was about 1,400.

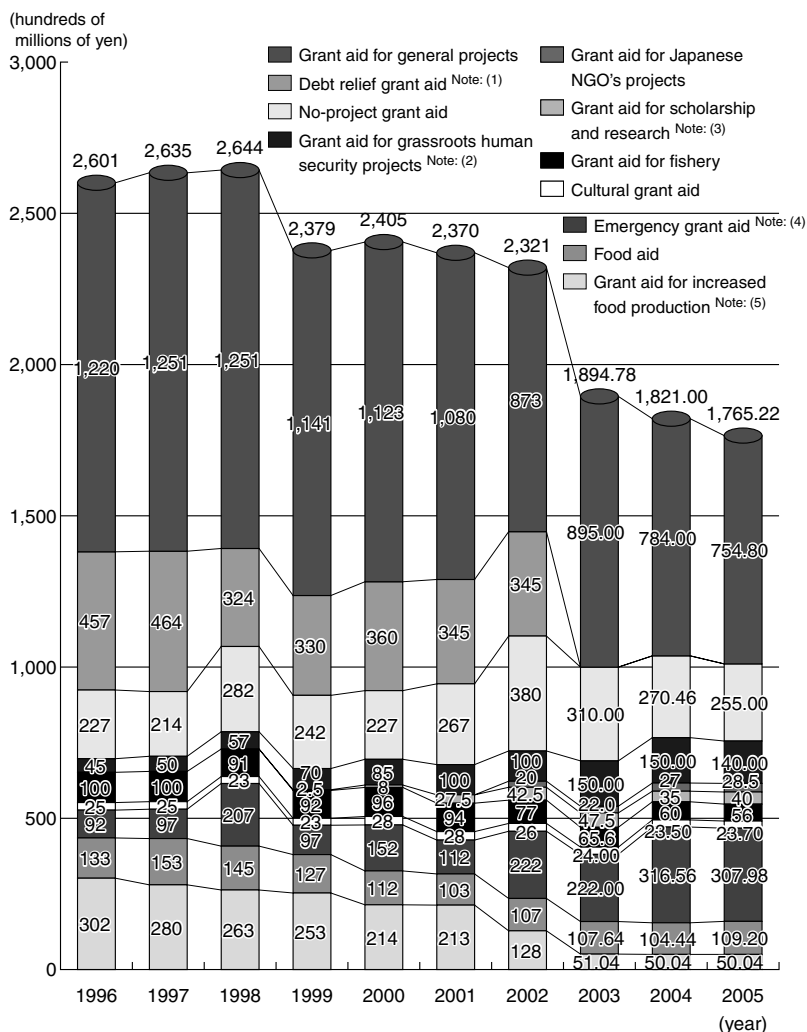
(3) Distribution by region and country

The regional and country distribution of Japan's grant aid shows that the top recipient for many years was Asia. Asia was followed by Africa with the Middle East and Latin America in third place receiving about the same amounts. Beginning with reconstruction assistance for Afghanistan and Iraq, from circa 2003, assistance for the Middle East grew significantly. In FY2004, the Middle East region received the most grant aid, surpassing both Asia and Africa. In FY2000 on the exchange of note (E/N) basis, Asia's share was 41%, followed by Africa (29%) and Latin America (13%). The Middle East was in fourth place with just 9%. By FY2004, however, the distribution had changed dramatically, with the Middle East taking top place (44%), followed by Asia (29%) and Africa (17%). (see Figure 5-3)

In Africa the main modalities of Japanese ODA are grants and technical cooperation because yen loans have been suspended in countries that have applied to receive the benefits of the Enhanced HIPC (Heavily Indebted Poor Countries) initiative⁶. The increasing international attention directed to Africa's development has prompted many donors to increase their aid to that

5. For example, the government allocated an additional ¥118.8 billion to the grant budget within the supplemental budget in FY2003 in order to implement the provision of \$1.5 billion in grants pledged in October, 2003 at the Iraq Reconstruction Donor Conference (Nakao 2005). It has been pointed out, therefore, that the general account budget was not reduced as drastically as the initial plan suggested.

6. At the G8 Summit in 2005, the Japanese government announced a plan to resume providing yen loans in collaboration with the African Development Bank as a "joint initiative for the development of the private sector in Africa" (Enhanced Private Sector Assistance for Africa: EPSA).

Fig. 5-2 Transition of uncompensated financial assistance business budget

Source: MOFA "ODA white paper 2005" Figure III-36 "Budget transitich of grant aid"

Note: (1) Abolished in 2002.

(2) Changed from "Grant aid for grassroots projects" in 2003.

(2) Changed from "Grant aid for scholarship programs (started in 1999)" in 2001.

(2) Changed from "Disaster relief of emergency grant aid" in 1995.

(2) Changed from "Grant aid for increased food production" in 2005.

region (especially their grant aid). In the case of Japan, however, reduction in the ODA budget has seen grant aid for Africa reduced by 30% on a net spending basis (US\$) – to 40% from its peak in 1999. The total ODA amount for the

Fig. 5-3 Transition of regional distribution of grant aid
(comparison between 2000 and 2004)

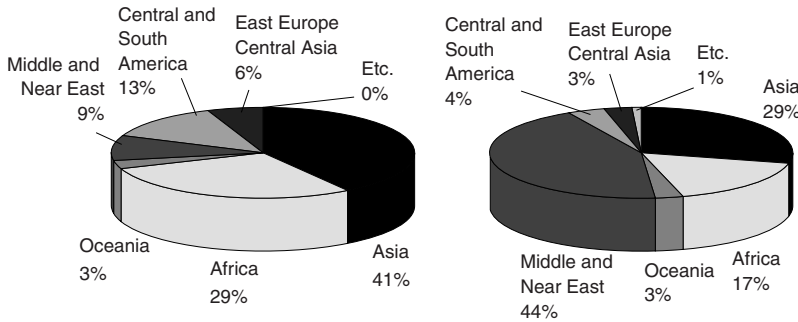
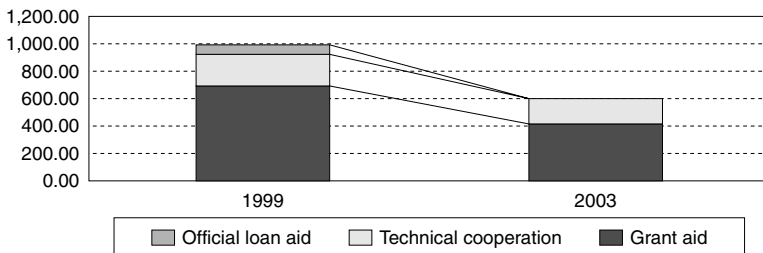


Figure 5-4. Breakdown of bilateral ODA patterns of Japan to Africa
(comparison between 1999 and 2003)



Source: Figure 5-3, 5-4 are extracted from ODA white paper 2005 and 2001, respectively.

region has also been significantly reduced. (see Figure 5-4)

(4) Planning and implementation systems

As the leading ODA ministry, the MOFA has responsibility for coordinating with other ministries and supervising implementation agencies. In actuality, the planning and implementation of ODA policies and budgets are scattered across many organizations. Japanese ODA is broadly divided into grant aid cooperation, technical cooperation (itself a form of grant aid), yen loans (concessional loans), and contributions to international organizations. Implementation of bilateral aid is divided among MOFA, which handles grant aid, the Japan International Cooperation Agency (JICA) and relevant ministries which handle technical cooperation, and the Japan Bank for International Cooperation (JBIC) which handles yen loans. Contributions to international organizations are divided between MOFA, which deals with UN-related organizations, and the Ministry of Finance (MOF) which deals

with development finance organizations including the World Bank.

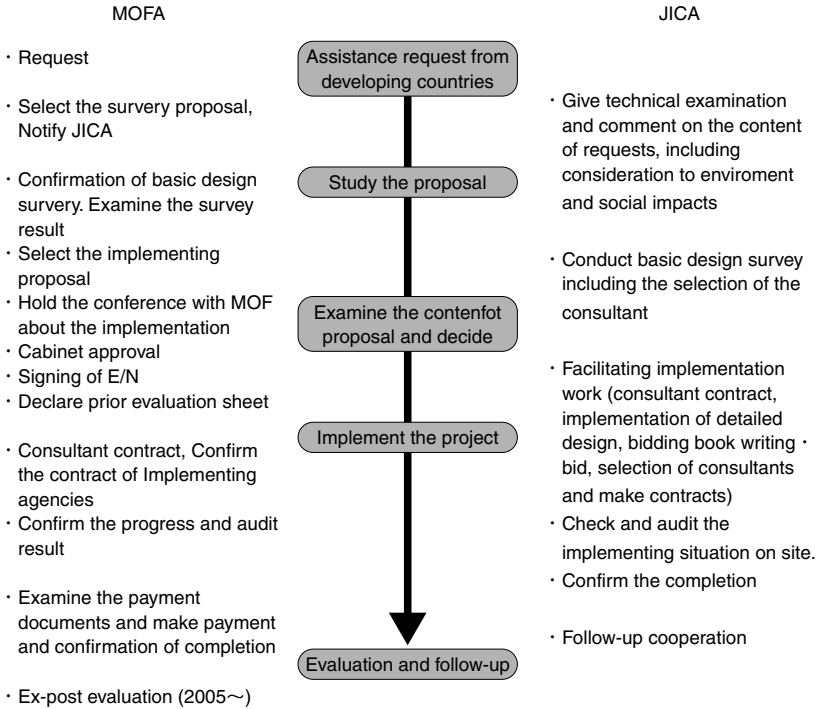
Grant aid cooperation is under the sole charge of MOFA which is responsible for overall policies and implementation. Nonetheless, as Figure 5-1 shows, JICA is in charge of general project grants, grant aid for human resource development scholarships, fisheries grants, cultural grants (building facilities and large-scale equipment procurement) as well as studies and implementation facilitation work for food aid and grant aid for underprivileged farmers. MOFA implements part of the non-project grants, emergency grants and cultural grants directly by collaborating and coordinating with procurement agencies and international organizations⁷. Japanese diplomatic missions play an important role in implementing grant aid for grassroots human security. They examine requests for assistance in the respective countries, select the candidate projects (to be approved by the central ministry), sign grant agreements with the requesting groups, disburse the funds, and implement and monitor the projects. The grant aid for Japanese NGO projects is a scheme with which MOFA directly supports Japanese NGOs.

JICA is involved in more than 50% of the grant aid budget (operational budget basis), including the general project grants which have the largest budget, through basic design and implementation facilitation work. Figure 5-5 is an operational flowchart of general project grants and fisheries grants that describes the roles of MOFA, diplomatic missions and JICA.

With regard to its implementation system, some aspects of Japan's procurement methods are relevant here. Within grant aid cooperation, primary contractors for general project grants, fisheries grants, cultural grants and food aid are limited to Japanese companies, a situation which often is criticized both domestically and internationally for increasing costs. The OECD Development Assistance Committee (DAC) also pointed out in the context of its 2003 Peer Review of Japanese ODA that Japan's grant aid is "de facto tied assistance" and that "such a system goes against the trends of promoting the ownership of recipient countries and integrating donors' procurement systems, and against the direction of reducing the aid administration burden of recipient countries." DAC recommended that "Japan should work with the

7. Both MOFA and JICA often use a procurement agent (typically Japan International Cooperation System (JICS)) to study necessary equipment and materials and manage the procurement based on a contract with the recipient government.

Figure 5-5. Workflow of grant aid: Role of MOFA and JICA
(in the cases of grant aids for general projects and fishery)



Source: Retro MOFA "Grant Aid Guideline (August, 2004)" and JICA website, "JICA and Grant Aid."

Note: JICA entrusts procurement management tasks to JICS

DAC on identifying concrete measures to progressively untie the use of grant funds for primary contractors in the spirit of the recommendation on untying ODA to the least-developed countries⁸."

The DAC agreement to recommend the untying of ODA to the least-developed countries with high levels of aid dependency occurred in May 2001, and the recommendation became effective in January 2002. (For untied projects donors are asked to report each project's amount, tender period, procurement system, etc., to the DAC secretariat.) MOFA reports grant aid projects subject to this recommendation, as untied based on the following reasoning: although primary contractors are Japanese companies, they are

8. MOFA ODA website, "DAC Peer Review of Japan, outline and evaluation" and "DAC recommendations to the Japanese government" (December 2003).
<http://www.mofa.go.jp/mofaj/gaiko/oda/index.html>

selected through competitive bidding and their contracts do not require them to procure Japanese equipment, materials or services (Shirai 2005). MOFA gives as the reasons for limiting the primary contractors to Japanese companies, the need to synchronize project implementation with the Japanese government's budget administration process (single-year budget system), the need to ensure the quality of assistance and the need to maintain continuity.

Many times in the cases of other donors who offer loans, one organization is in charge of both the grants and the loans forms of financial cooperation, and the same procedures are applied throughout the project cycle of project selection, appraisals, implementation, evaluations and monitoring. For example, the German Ministry of Economic Cooperation and Development is responsible for aid policies in general and the German Corporation for Technical Cooperation (GTZ) handles technical cooperation. But the implementing agency of financial cooperation, the German Development Bank (KfW) is in charge of both loans and grants, and changes the concessionality of funds (loans or grants) based on income level and other factors of the recipient country. (Bilateral financial cooperation with developing countries is only a part of KfW's operations. It also provides medium- to long-term financing for the advancement of the domestic German economy and export credits.) France reformed its aid organizations in 1998 so that aid policies are now managed by the Directorate General for International Co-operation and Development of the Ministry of Foreign Affairs (bilateral aid and contributions to UN agencies, etc.) and the Ministry of Economy, Finance and Industry (aid to developing countries other than former colonies and contributions to the EU and international development banks). But under the shared supervision of these two ministries, the French Development Agency (AFD) provides grant aid, technical cooperation (although the Foreign Ministry also implements a part of it), loan aid, and even semi-commercial loans and equity investments (recipients are Priority Solidarity Zones, ZSP, defined by the French government, overseas departments and overseas territories) (Japan Bank for International Cooperation 2004).

5-2. Domestic debates surrounding grant aid and recent initiatives

(1) Domestic debates

In response to the increasing need for public understanding with regard to the effectiveness of ODA under tight fiscal conditions and to the increasing demands for its reform following a series of scandals, in 2002 MOFA announced numerous initiatives centering on public participation, securing transparency and improving efficiency. These were also based on recommendations by the Second Council on ODA Reform (a private council convened by the Foreign Minister which submitted its final report in March 2002) and the MOFA Reform Advisory Board (which consisted of well-informed experts and was chaired by the Foreign Minister, and submitted its final report in July 2002). Many initiatives were launched from the perspective of strengthening strategy, including the following: establishment of the Board on Comprehensive ODA Strategy as an advisory body to the Foreign Minister (June 2002); enhancement of the country-by-country approach (establishment of local ODA Task Forces in March 2003, and expansion and improvement of Country Assistance Plans); revision of the ODA Charter (August 2003); and preparation of the new Medium-Term Policy (February 2005).

In response to the overall momentum for ODA reform, efforts toward gradual improvement took place in grant aid which had been criticized for some time for a lack of transparency, poor information disclosure, high procurement costs and inadequate evaluations. In 2005, the desirability of further improvements in the efficiency of grant aid was expressed in rapid succession, in the Basic Policies for Economic and Fiscal Management and Structural Reform 2005 (the so-called “Honebuto (muscular) Plan 2005”⁹ which was adopted in June by the Cabinet following the debates in the Council on Economic and Fiscal Policy, and in the budget administration study conducted by the Ministry of Finance. MOFA created a working group within the Board on Comprehensive ODA Strategy to examine the issue, and published a report in December entitled “Checking and Improving ODA — For Higher Quality ODA.” The following sections describe the main domes-

9. Cabinet Office “Basic Policy on Economic and Fiscal Management and Structural Reform” Cabinet Decision dated June 21, 2005 — The Fifth Basic Policy — “Realizing a small and efficient government”

tic debates and recent efforts toward improvement, with a focus on grant aid.

(2) Transparency, information disclosure and proper implementation

Council on the Proper Implementation of Grant Aid Cooperation: The final report of the MOFA Reform Advisory Board recommended measures to ensure transparency in the selection and implementation processes of grant aid, and measures to expand ODA evaluations to determine effectiveness. In response to the recommendations, MOFA created the Council on the Proper Implementation of Grant Aid Cooperation consisting of well-informed independent experts and reporting to the Director-General of the Economic Cooperation Bureau. The Council meets bi-monthly or so, exchanging opinions on cross-sectoral topics such as information sharing and examination during the main stages of a grant aid project cycle, submit for Cabinet approvals, bid tendering and actual project implementation (proceedings are published in MOFA's ODA website).

Grant Aid Cooperation Appraisal Guidelines: These Guidelines give perspective and procedures for the appraisals to be conducted to ensure the proper implementation of grant aid projects, including environmental and social considerations at each stage of the project cycle, from project identification and formulation to implementation and post-completion supervision¹⁰. The Guidelines are applied to general project grants and fisheries grants, except for general project grants implemented by international (or regional) organizations with different implementation methods (regional development grants, grants against infectious diseases, and part of child welfare grants) which are excluded. The guidelines were published as "Grant Aid Cooperation Appraisal Guidelines (Provisional Version)" in August 2004 (MOFA website), but are currently being used on a pilot basis. Necessary revisions based on the opinions of interested parties during this pilot phase will be made before these Guidelines are fully applied.

(3) Expansion of evaluations

In order to verify and receive better advice on the feedback of evaluations, in December 2001 MOFA created the Evaluation Feedback Committee consisting of independent experts (in 2003 the Committee was renamed the

10. JICA revised its Guidelines for Environmental and Social Considerations in April 2004, which also applies to JICA's preparatory studies for grant aid. Therefore, at each stage of grant project formation and implementation, MOFA basically applies JICA's "Guidelines for Environmental and Social Considerations" for its activities.

External Advisory Meeting on ODA Evaluation, and JICA and JBIC established their respective similar evaluation committees in June 2002). Based on a division of responsibilities wherein MOFA handles policy and program level evaluations and implementing agencies handle project level evaluations. JICA, which is in charge of basic design studies and encouraging implementation, has been conducting ex-post evaluations on the adequacy and effectiveness of the basic designs of certain individual projects (MOFA 2005a). However, this has not necessarily allowed MOFA to carry out its own ex-post evaluations of individual projects to improve at its own initiative both the quantity and quality of projects or more systematically to incorporate in future project formations the lessons learned from project implementation.

In 2005, the “Honebuto Plan 2005” (adopted by the Cabinet in June) and MOF’s budget administration study called for the establishment of a project-level grant aid evaluation system. In response, MOFA decided to build its own such system, to begin in FY2005. Specifically: (i) Evaluations will be conducted by the central Ministry and by diplomatic missions abroad; (ii) From the pool of about 110 projects with a cost exceeding ¥1 billion that have been completed three to five years previously, about 50 will be selected (one to two projects per diplomatic mission); (iii) Evaluation methods based on international standards (OECD-DAC’s five evaluation criteria, the Plan-Do-Check-Act cycle) will be employed and to the extent possible evaluations based on results orientation will be conducted; and (iv) To ensure objectivity, outside experts (Council on the Proper Implementation of Grant Aid Cooperation, External Advisory Meeting on ODA Evaluation) will be consulted with regard to evaluation criteria and findings. Evaluation results will be published on websites and other media. Looking forward, MOFA is aiming to implement full-fledged ex-post evaluations for as many projects as possible while utilizing development experts to acquire specialized and technical knowledge¹¹. Tables 5-2 and 5-3 show the recommendations to establish an ODA evaluation system and recent efforts to expand evaluations, respectively.

(4) Reducing costs and increasing efficiency

For many grant aid projects, primary contractors must be Japanese compa-

11. In the FY2006 budget, MOFA earmarked a new budget item (¥61 million) to enhance the evaluation methods and increase the number of evaluated projects, and to strengthen the implementation system by involving independent experts, etc.

Table 5-2. Remarks about ODA's evaluation system

Basic policies for economic and financial management and structural reform in 2005 (June, 2005, cabinet approval)	
<ul style="list-style-type: none"> Implement ODA in a proper way, based on the result of examination of account settlement in the diet. Conduct the third-party objective evaluation (including the cost-benefit analysis) on the outcome of ODA projects, announce the result, and establish the PDCA (plan-do-check-act) cycle reflecting in the 'plan' and 'do' in ODA policy. As for the grant aids, it is necessary to conduct the quantitative ex-post evaluation including cost required in the projects, reduce the procurement cost, and make the implementation more efficient. 	
MOF budget execution survey 2005	
<ul style="list-style-type: none"> We should set a cost reduction goal and start implementing such approaches. Therefore, we should take action in such ways as making the bidding system more competitive, selecting equipments and materials very carefully, and incorporating the system reflecting the local procurement price. Also, we should adopt the system to take the ex-post quantitative evaluation on each project as to how much it actually cost or whether it reached its original goal and to announce the result. 	

Table 5-3. Recent actions for the improvement of ODA evaluation

ODA ex-post evaluation targets		
levels	type of evaluation	main targets
Policy level	<ul style="list-style-type: none"> Country evaluation Main issue evaluation 	Country assistance policy (plan, principle) Assistance policy for main issues (main issues of ODA middle-term policy, sectoral initiatives)
Program level	<ul style="list-style-type: none"> Sector evaluation Scheme evaluation 	Assistance in general for one country, one sector
Project level	<ul style="list-style-type: none"> Project evaluation 	technical cooperation (JICA projects) Loan (JBIC projects)

Policy for project-level ex-post evaluation		
Technical cooperation	Loan	Grant aid
Using the consultant, evaluate the technical cooperation projects (40 or so) of more than a certain scale completed three years before	Using the consultant, evaluate all the projects (50 or so) completed two years before	<ul style="list-style-type: none"> Make an experimental evaluation on the projects (50 or so) more than one billion yen completed three to five years before through the Japanese overseas establishments from 2005. Aim to make a substantial, ex-post evaluation for as many project as possible involving the experts from a technical point of view from 2006 (currently under the budget request).

Source: MOFA reference

nies, but the involvement of Japanese consultants and constructors increases project cost compared to cases where goods and services can be obtained locally. Cost goes up as well if contractors rush to meet the deadline imposed by the one-year budget of ODA — projects in principle must be implemented and completed within the same year.

School construction is an area where this situation is particularly apparent. School construction accounts for a large share of education aid and criticism is often heard that schools built with Japanese general project grants are unnecessarily expensive. The recent thrust in aid requires that the criticism be taken seriously. Since the 1990s, various organizations have become involved in building primary schools, due partly to a trend of emphasizing support for primary education (the World Conference on Education for All at Jomtien, Thailand, and the UN Millennium Development Goal to “achieve universal primary education by 2015”, etc.). Moreover, primary education is one of the sectors where aid coordination is vigorously pursued. Especially in sub-Saharan Africa, new aid modalities such as budget support and pooled funds are becoming popular, and there is an increasingly strong trend for all donors to procure goods and services through the system of the recipient government (see 5-3 (3) below for details).

Table 5-4 is a comparison of school construction costs by aid implementing organization, prepared by a coalition of NGOs which provides assistance in Cambodia’s education sector (People’s Forum on Cambodia, Japan). Looking at construction cost only, schools built by Japanese general grants stand out for costing some three times more than schools built by NGOs and other organizations. A simple comparison like this may be somewhat misleading. Construction conditions and environments are not uniform across Cambodia and different aid organizations have different reasons and philosophies for building schools. However, this table raises the important question about how school construction is being financed by general grants (The International Development Journal 2004). Similar problems of higher costs have been pointed out in well-drilling projects.

More than a few governments of developing countries are willing to accept lower costs if more schools can be built and there have been efforts in recent years to bring the costs down. Through the adoption of appropriate specifications and scales, procurement from local and third country sources and other measures, the cost per square meter has been reduced substantial-

**Table 5-4. Situation of school constructions in Cambodia by each organization
(Made by citizen Forum in Cambodia, Japan)**

supporting organization		year	Simplified building cost per classroom
ODA/General grant aid projects		2004	3920thousand yen
NGO	ODA/NGO Grant aid project	2002	about600thousand yen
	Frame NGO (EU budget)	2001–02	about640thousand yen
	JHP-School Building	2003	about900thousand yen
	Association	2002	lest yhan1300thousand yen
	Shanti Volunteer Association (SVA)	1998–99	about1000thousand yen
		1997	about950thousand yen
	Foundation for International Development/Relief (FIDR)	1997	about600thousand yen
International Organization	Asian Development Bank (ADB)	2001–03	about670thousand yen

Source: MOF (2005), "International Development Journal" (February, 2004) P. 26

Table 5-5. Examples of school building projects on cost reduction

Philippines	1998	73,004 yen/m ²	→	2003	48,530 yen (about34%less)
Guinea	1998	59,400 yen/m ²	→	2002	46,800 yen (about21%less)
South Africa	1998	65,900 yen/m ²	→	2003	42,700 yen (about35%less)

Source: MOFA "Review and improvement of ODA" (December, 2005) P. 27

Table 5-6. Grant aid adapted to the recipient country's situation

Nepal	The Japanese side procures the construction materials, and the Nepal local people including parents of the students are in charge of building operations while the Japanese architecture companies manage the construction.
Afghanistan, Zambia, Laos	Local construction companies conduct the trial construction under the plan and design by Japanese architecture companies based on the basic design survey. Also data was collected for further cost reduction.
Vietnam	Flooding caused by monsoon destroyed most of the local schools except the ones made by Japan, which led, among Vietnamese, to the high reputation of the Japanese schools. The Vietnamese government adopted the Japanese standard for their school construction.

Source: "International Development Journal" (February, 2004) P. 29 and MOFA "Review and improvement of ODA" (December, 2005) PP. 26-27

ly (see Tables 5-5 and 5-6). On the other hand, some developing countries prefer the high technical abilities of Japanese companies and the durable buildings they provide. For this reason, the Japanese government currently has a policy of first confirming the preference of the partner country. If it prefers government-to-government assistance, Japan will offers a general pro-

ject grant with an emphasis on quality; if it prefers an NGO-implemented project, small-scale assistance will be offered through grant aid for grassroots human security or grant aid for Japanese NGO projects. A new aid scheme called “grant aid for community empowerment” was to be launched in FY2006 to allow locally-tailored designs and the use of local contractors in the construction phase. Within the next five years, there are plans to establish a cost reduction goal — to reduce the cost of primary and middle school construction projects in Africa by more than 30% — and to follow up on the achievement of this goal. At the same time, the government will consider measures to further reduce the costs of general project grants.

(5) Greater flexibility in non-project grants for emergency/reconstruction assistance

In the non-project grant scheme, funds are provided to a recipient country in one disbursement, then used to import goods necessary for development and poverty reduction. Non-project grants can be implemented more quickly and flexibly than general project grants, which require advance project formation work on the donor side. Since in principle non-project grants are untied, they also can be less costly.

In addition to these established characteristics, to respond adequately to the great devastation and urgency of the Sumatra earthquake and Indian Ocean tsunami, the Japanese government further eased the traditional principles of non-project grants so that added flexible and timely assistance could be provided to cope with the damage. Specifically, procurement methods and eligible areas were expanded to: (i) allow local procurement; (ii) allow service procurement for transportation and reconstruction work; and (iii) exempt recipients from an obligation to accumulate counterpart funds. Since traditional non-project grants basically provide foreign currencies for importing goods, and utilize counterpart funds — accumulated through the sale of these goods — to provide local currency support, these modifications added considerable flexibility to the scheme’s emergency reconstruction application¹². For Sri Lanka, one of the most affected countries, it has been reported

12. For detailed evaluation of emergency recovery assistance with flexible and timely use of non-project grants, see MOFA “Damages from Sumatra Earthquake and Indian Ocean Tsunami — Mid-Term Evaluation of Bilateral Grant Aid” (December 26, 2005) and “Report on Assistance to Sumatra Earthquake and Tsunami Affected Regions: Expansion of Methods and Applied Fields in Procurement” *International Development Journal* October 2005 issue (pp. 32-33) and “What Assistance Do People Want? — Japanese Aid to Indonesian Earthquake and Tsunami Affected Regions” *Diplomacy Forum* April 2006 issue (pp. 68-73).

that, when the non-project grants were used to build schools in accordance with local specifications, the unit cost was reduced by more than 50% (MOFA (2005a)).

When implementing the non-project grants in the affected countries, the Japanese government utilizes procurement agencies which manage funds and procure goods and services on behalf of recipient governments. The Japan International Cooperation System (JICS) signs a procurement agency contract with the government of an affected country, selects and executes contracts with consultants who manage the construction and contractors, and handles such responsibilities as progress management, financial management and completion inspections. In some cases, JICA conducts an emergency development study in advance to examine the design and technical specifications related to the selection of consultants and/or contractors.

These micro-level improvement efforts are certainly important and useful. However, these initiatives are taken largely as an answer to the following question: How can cost be reduced and efficiency increased under tight fiscal conditions, and how can better information disclosure and transparency be achieved under the current schemes, and planning and implementation systems? These initiatives are not necessarily prompted by changes in the international aid environment or by strategic thinking for realizing Japan's vision set out in the new ODA Charter. The significance of the ongoing improvement efforts is undeniable, but at the same time, it is important to reform grant aid cooperation from a macro-level perspective, so that strategic and policy-coherent overseas economic cooperation can be formulated and implemented.

5-3. International aid environment surrounding grant aid cooperation

(1) Changes in the international aid environment

Since the latter half of the 1990s, the environment for international aid has changed drastically. Globalization has widened disparities among developing countries, the debt problems of poor countries have worsened, and aid fatigue on the part of industrialized countries has deepened. Poverty reduction has come to be emphasized as the overarching goal of development, focus has shifted to support for the least developed countries, including

those in sub-Saharan Africa, and the share of grants in international aid has been increasing. International initiatives such as the Poverty Reduction Strategy Papers (PRSPs) introduced by the World Bank/IMF, Millennium Development Goals (MDGs) adopted by the United Nations and an aid effectiveness declaration by OECD/DAC are emblematic of the new aid environment.

These changing environment has great significance, directly and indirectly, for Japan's grant aid cooperation. Firstly, the increased reliance on grants, or "grantization" of aid, means that grants rather than loans are now the central tool for assisting the poorest countries. This has brought Japan's grant aid under increasing scrutiny. Secondly, with the adoption of PRSPs, changes in aid approaches, evident since the latter half of the 1990s, accelerated in terms of donor cooperation in policies, aid money and procedures as well as in policy dialogues with recipient countries. The situations these changes have created are beyond the coping capacity of the current project formation and implementation systems; for example, in overseas diplomatic missions there are vastly fewer personnel involved in project formation and supervision of grant aid than even those working at local offices of JICA, which provides technical cooperation on a grant basis. Thirdly, the increased focus on assisting the poorest countries has led to the marginalization of assistance to middle income countries. Japan, which over the years has directed its ODA toward lifting East Asian countries to middle income status, is now wondering how to move forward regional economic cooperation relationships and how to position its grant aid cooperation in the region. These three points will be explained in detail below¹³.

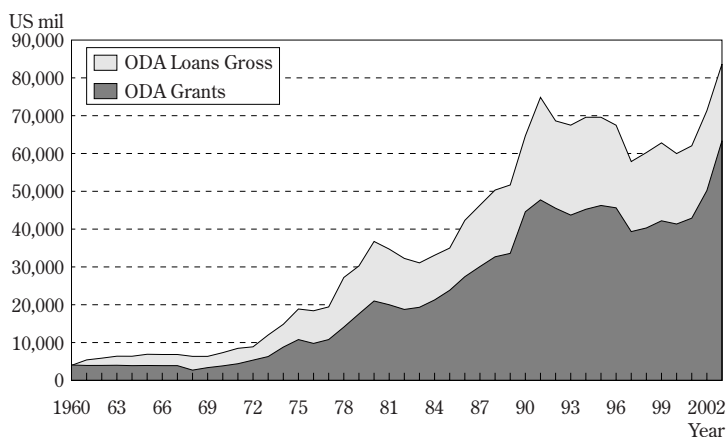
(2) "Grantization" of international aid

In recent years, many donor countries have switched their bilateral aid from loans to grants. Multilateral development finance organizations including the World Bank also have switched part of their concessional loans to grants. Figure 5-6 shows changes in the share of grants in international assistance. Numbers are shown on a gross basis (operational budgets) to show how much of new ODA commitments are allocated to grants. This trend became definitive when the IDA (International Development Association) decided to provide grants in its 13th replenishment. IDA is World Bank Group organiza-

13. For a discussion of the implication of recent changes in the international aid environment for Japanese economic cooperation in general, see Ohno (2002).

tion that provides concessional loans to low income countries. Those with 2004 income per capita of less than \$965 are eligible for IDA's assistance (this cutoff is for the Bank's operations in FY2006). The loans are provided with no interest, for a term of 35 or 45 years with a grace period of 10 years, but there is a service charge of 0.75% per year. The loans are funded by the contributions of developed countries that are solicited every three years ("replenishments").

Figure 5-6. Transition of International ODA Loans and ODA Grants

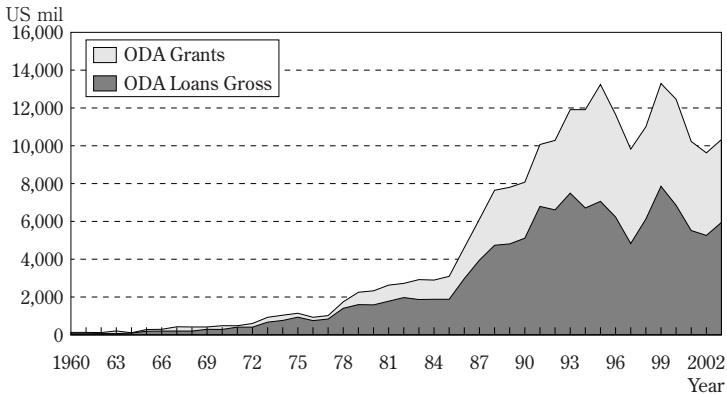


As international pressure mounted to provide debt relief to HIPC, the IDA-13 replenishment (for the three years beginning in July 2002) allowed for the first time the provision of grants, although only in certain cases (post-conflict, disaster relief, HIV/AIDS) and to certain countries (those with low debt sustainability). The share of grants was set at 18-21% of the total. For the IDA-14 replenishment (for the three years beginning in July 2005), the share of grants was increased to about 30%, and the extent of grant provision to each country became based on its policy performance and debt sustainability.

As Figure 5-7 shows, grants accounted for an overwhelming share in Japanese ODA during the 1960s when Japan began its foreign aid as postwar compensations. Thereafter, however, more yen loans were provided and the share of grants decreased. Since the latter half of the 1980s, the share of yen loans expanded, partly in connection with Japan's policy of "current account surplus recycling", and as the share of loans in Japanese ODA grew faster

than in that of other donors. In recent years the share of grants has been rising because assistance to the countries that have applied for the Enhanced HIPC Initiative is constituted mainly by grant aid and technical cooperation, as noted above in 5-1 (3). The average share of grant aid (including technical cooperation) between 2001 and 2003 was about 45%.

Figure 5-7. Transition of Japan ODA Loans and Grants



notes: Grants include technical co-operation. Loans are gross - based.

Source: Both figure 5-6 and 5-5 are extracted from OECD, Geographical Distribution of Financial Flows to Aid Recipients 1999-2003 (2005), CD vision

(3) Changes in aid approaches

PRSPs were introduced by decision of the IMF/World Bank Annual Meeting of September 1999. They are development plans that the developing countries themselves prepare holding poverty reduction as the ultimate goal with their own initiative (ownership) and stakeholder participation (partnership) as the two pillars. In reality, preparation of a PRSP has become a requirement for indebted countries to be eligible for debt relief under the Enhanced HIPC Initiative and for low income countries to receive concessional IDA (World Bank) and PRGF (IMF) loans. PRSPs now function to (i) determine access to aid money, (ii) drive the content of development strategies, (iii) establish a cooperation framework (aid coordination) among development actors, in addition to (iv) considered as a means to achieve international goals such as the MDGs. They have thus come to wield enormous influence over the development policies of the poorest countries.

The mainstreaming of PRSPs, together with the heightened international attention on improving aid effectiveness, has accelerated changes in aid

approaches. Donors are required, more than ever, to cooperate with each other in terms of strategic and policy frameworks, harmonization of aid procedures and integration of aid money (introduction of new aid modalities such as budget support and pooled funds¹⁴), among others. With regard to highly aid-dependent countries (typified by the least developed countries in sub-Saharan Africa) in particular, there is increasing international appreciation (including by those who work on the ground in developing countries) of lessons learned from the mistakes of past approaches: Unless individual aid projects are designed and implemented in line with the recipient government's own systems for development planning, budgeting, disbursements and procurement, etc., they may create wasteful redundancies, increase the cost of the development effort, and increase the burden of dealing with diverse aid procedures. As a result, they tend to reduce the sustainability of projects after aid has been completed.

An example of this is Tanzania in the mid-1990s where, the problem of aid coordination became so serious, that donors and local experts conducted a study. The report issuing from the study recommended that interested parties construct a new relationship between the government and donors, including a review of aid approaches¹⁵. The "Helleiner Report," as it is known, pointed out that about 40 donors were implementing more than 2,000 projects in Tanzania, creating a project deluge. Tanzania was shouldering great operational burdens trying to satisfy the different aid procedures required by the different donors, and there were serious problems associated with a lack of coordinating capabilities on the part of the Tanzanian govern-

14. Budget support is an aid modality which disburses aid money through the government's fiscal and accounting systems. It is differentiated from project-type aid which earmarks the use of funds or provision of goods and services to specific projects. With the introduction of PRSPs, European donors, the World Bank and other organizations are actively promoting it especially in sub-Saharan Africa. When budget support is provided, the government and donors have policy dialogues about high priority development strategy (PRSP) and budget allocation. Budget support can be categorized into two kinds: (i) general budget support which encompasses the government's entire fiscal and expenditure frameworks; and (ii) sector budget support which encompasses all projects included in a program for a specific sector. Pooled funds are an aid modality in which multiple donors pool their funds and share programs, disbursements and procurement conditions, etc. However, since budget support was introduced only a few years ago, it remains to be seen whether it is achieving its objectives (aiding the developing countries' poverty reduction efforts based on the PRSP and improving donors' aid effectiveness, etc.). Currently, donors are jointly evaluating general budget support (the final report is due in 2006).

15. Helleiner, et al.(1995) Report of the Group of Independent Advisers on Development Cooperation Issues between Tanzania and its Aid Donors, Royal Danish Ministry of Foreign Affairs. Takahashi (2003) discusses in detail the crises that project assistance brought especially to sub-Saharan Africa, including the review of past literature.

ment and donor-led project formation. The conclusion now widely accepted is as follows: To overcome such problems and to build developing countries' capacities, donors should not formulate projects outside the developing country's systems; rather, they should (i) share a policy framework, (ii) disburse funds predictably through the recipient government's systems and (iii) share the procurement procedures (all these are related to utilization of the government systems). Budget support and pooled funds have emerged as aid modalities that permit these initiatives.

(4) Shift in aid target countries

Closely related to the "grantization" of aid described above is the focus on the least developed countries and the concurrent marginalization of middle income countries. There is a belief that donors should provide grants only to least developed countries with low debt capacities. Middle income countries with access to international financial markets can in principle be left to private funding, with only limited provision of concessional loans.

A clear definition of middle income country is difficult, but in World Bank terminology, they are countries eligible for IBRD loans at market-based interest rates. This is a quite broad definition, from lower middle income countries with per capita income of about \$800 to upper middle income countries with per capita income of more than \$3,000, categorized as emerging market economies¹⁶. Within East Asia, where Japan considers the economic cooperation relationships to be important, there are low income countries such as Laos, Cambodia and Vietnam and middle income countries such as China, Indonesia, the Philippines, Thailand (lower middle income) and Malaysia (upper middle income).

About 80% to 90% of Japanese yen loans are for Asia. East Asian middle income countries, as listed above, account for a large share, 40% to 50% of the total for all regions in FY2002-04 on an approval basis.¹⁷ Thailand and Malaysia, which were important recipients of yen loans during the 1980s until the mid 1990s, including assistance following the Asian financial crisis,

16. For example the World Bank and DAC categorize developing countries based on their FY2002 GNI per capita as follows: (i) \$735 or less: low-income countries (LICs); (ii) \$736-\$2,935: lower middle income countries (LMCs); (iii) \$2,936-\$9,075: upper middle income countries (UMCs); and (iv) \$9,075 or more: high income countries (The World Bank and DAC documents).

17. See JBIC Yen Loans Activity Report (FY2003-FY2005) "Statistics and data: Actual Yen Loans by Country and Region." <http://www.jbic.go.jp/japanese/base/achieve/nenji/index.php>

achieved a certain level of economic growth and poverty reduction results and gained access to global financial markets. In the parlance, they have “graduated” from the World Bank (IBRD) and Asian Development Bank official assistance. These countries have also largely graduated from yen loans ; furthermore, the Japanese government intends to end new yen loans to China by around FY2008. These countries are now turning to domestic and private sources (both domestic and foreign) for infrastructure building. Future official financial assistance to East Asian middle income countries must respond to that region’s dynamic processes of economic development.

Traditionally, economic cooperation for East Asia has been described as a “trinity” of aid, trade and investment: ODA functioned as a catalyst to incorporate Japanese economic activities deeply into the region’s production network and at the same time contributed to the creation of a dynamic force that promoted the division of production within the region. Looking forward, to promote East Asia’s economic partnership and market integration, continuation of the economic cooperation relationships with these countries is important (see 5-4 (2) below for details). If the current international trend is moving toward a significant restriction in concessional assistance for middle income countries, and if middle income countries have a strong need for privately financed infrastructure, it would be worthwhile to consider creating a new concept for economic cooperation programs that is not bounded by the definition of ODA. (IBRD loan terms are “hard” (non-ODA), meaning that it raises funds at market interest rates by issuing bonds.).

(5) Challenges for Japanese grant aid posed by above factors

As described above, the grantization of international aid has progressed. In assisting sub-Saharan Africa countries and other least developed countries, there is increasing call for international coordination that will improve aid effectiveness and that will center on PRSPs in order to achieve MDGs. In Japan, too, the relative importance of grant aid assistance for the least developed countries has grown since it forgave yen loan debts under the Enhanced HIPC Initiative. Enhancing the competitiveness of grant aid is essential for improving the effectiveness of Japanese ODA, but there are three challenges to be dealt with.

The first challenge: The policy content in grant aid cooperation should be increased and its position in the project formulation and implementation

stages of the recipient country's policy system should be clarified. It is important also to actively participate in policy dialogues in the recipient country and construct support systems for that purpose. Beyond simply supporting projects indicated in PRSPs and development plans, coordination with other donors and complementarity with their assistance must be kept in mind. Also, to be kept in mind is that partnerships with diverse development actors insures the "localization" of aid. The implementation system should be strengthened by, among other things, building the necessary human resources capable of active participation in local aid coordination meetings and other discussions. However, even compared to JICA which is in charge of technical cooperation, local embassies involved in project formation and implementation supervision of grant aid are severely understaffed.

The second challenge: With particular reference to initiatives to improve aid effectiveness in the least developed countries, continued Japanese efforts are required for dealing with such issues as improving aid money predictability (on-budget), disbursements and procurement in accordance with the recipient government's system (untying) and cost reduction. With regard to the untying of procurement, a concern is often voiced that this goes against the principle of "aid with a human face," but even if Japanese companies do not undertake the projects, it is still possible to provide "aid with a human voice" through policy dialogue and through demonstration of Japan's aid philosophy. It is said that in general tied aid weakens competition among suppliers by requiring goods and services to be procured from the donor country, that it tends to encourage profit-motivated suppliers to charge high prices and fees. It is also said, that untied aid is preferable to tied aid because: (i) it allows greater freedom to the recipient country in the use of aid funds; (ii) it encourages the harmonization of procedures among donors; and (iii) the recipient is free to purchase goods and services and technologies that are cheaper and better suited for local conditions rather than capital-intensive technologies¹⁸.

The third challenge: It must be acknowledged that budget support and pooled funds are now well-established aid modalities, and that modalities pro-

18. The issue of tied and untied is related to the level of technology and quality required by the developing country, so which is better is not a simple matter. However, in general, there are many people who advocate the untying of aid from the perspective of economic efficiency. For details, see Shirai (2005) p. 299.

viding local currency in addition to the traditional non-project grants (foreign currency support) are similarly useful. Some efforts in this direction have already begun by Japan. The Japanese government has allowed flexible application of non-project grants for emergency/reconstruction assistance, accepting local and service procurement as well as exempting recipients from the obligation of accumulating counterpart funds. If local currency support schemes such as budget support and pooled funds are institutionalized, there will be more options for dealing with the high cost of grant aid cooperation. New aid modalities can be helpful for developing countries with strong tendencies toward emphasizing higher quantity and lower costs in building facilities in the educational, health and water sectors. Compared to the construction of facilities by grant aid for grassroots human security and grant aid for Japanese NGOs, utilization of new aid modalities can provide more funds. Local currency support schemes are likely to be useful also if the scale of project is increased and two-dimensional expansion and development are pursued. It is not yet clear how and to what extent the to-be-adopted grant aid for community empowerment will be applied; hopefully, it will meet the needs of developing countries and provide more options.

5-4. Formation of a comprehensive economic cooperation policy — Realizing the vision of “bisecting ODA” and the role of grant aid cooperation

(1) New ODA Charter and argument for “two-track ODA”

How should Japan provide strategic aid within the new trends described above while still responding to domestic calls for reform? Certainly, the recent aid trends are based on the realization that past approaches to supporting the poorest countries, including those in sub-Saharan Africa have failed. Japan has an obligation to honestly face the failures while helping these countries achieve sustainable growth and poverty reduction. With regard to East Asia, the picture is somewhat different. For many years Japan has cooperated with East Asian countries and provided them loans in a “trinity” of trade, investment and aid, effectively, incorporating them into a dynamic production network. Some East Asian countries have already been “graduated” from aid. Deepening economic collaboration with this region, should benefit not only Japan but the other countries as well. This relationship remains important despite the trend of directing international aid toward the poorest countries¹⁹. It is also true that East Asia consists of diverse countries

in different stages of development and that the North-South problem exists within the region. If dynamic development of the entire region is to be sustained and market integration promoted, the issue of bridging intra-region gaps must be addressed, and in that sense, Japan's aid to the less developed countries has an important role in the East Asia region (Miura 2005).

Indeed, the new ODA Charter, revised in August 2003, is based on these concepts, stating "The objectives of Japan's ODA are to contribute to the peace and development of the international community, and thereby to help ensure Japan's own security and prosperity." The new ODA Charter, in other words, is based on the idea of "two-track ODA." Specifically, Japan's aid strategy can be described with two pillars. The first is cooperation from the perspective of "regional contributions," including designating Asia as the priority region, and promoting market integration, especially with East Asia, through enhanced economic collaboration, and reduced intra-region disparities. The second pillar is cooperation from the perspective of "global contributions," including support for BHN (basic human needs), which directly contributes to poverty reduction, and assistance for peacebuilding and reconstruction.

In the "Honebuto Plan 2005" adopted by the Cabinet in June 2005, ODA is positioned with a policy objective of "enhancing global strategy" with "initiatives to usher in a new dynamic era." This document proposes promoting economic collaboration mainly with East Asia, and strategically utilizing ODA and private resources within that framework.

At this juncture, there is little need to define the geographic areas of "regional contributions" and "global contributions" too rigidly. Japan may

19. The Ministry of Economy, Trade and Industry released an interim report of the Economic Cooperation Subcommittee of the Trade and Economic Cooperation Committee of the Industrial Structure Council in July 2005, which described Japan's economic cooperation experience in East Asia as follows: "The economic cooperation method, which is clearly different from those of other developed countries that center on grant aid and which aims for independent development by drawing on the vitality of the private sector of the partner country, is something we can be very proud of, considering its achievements as the "Japan ODA Model." Now that we are in the 21st century, we believe that its importance is growing even more." With the premise that the recipient country has achieved appropriate governance, the Japan ODA Model activates the dynamism of economic growth through (i) building the base for economic development, which comprises building hard and soft infrastructure and nurturing industrial human resources; (ii) implementing economic cooperation while utilizing yen loans and technical cooperation as main tools; and thereby (iii) promoting the production, trade and investment activities of the private sector in the recipient country.

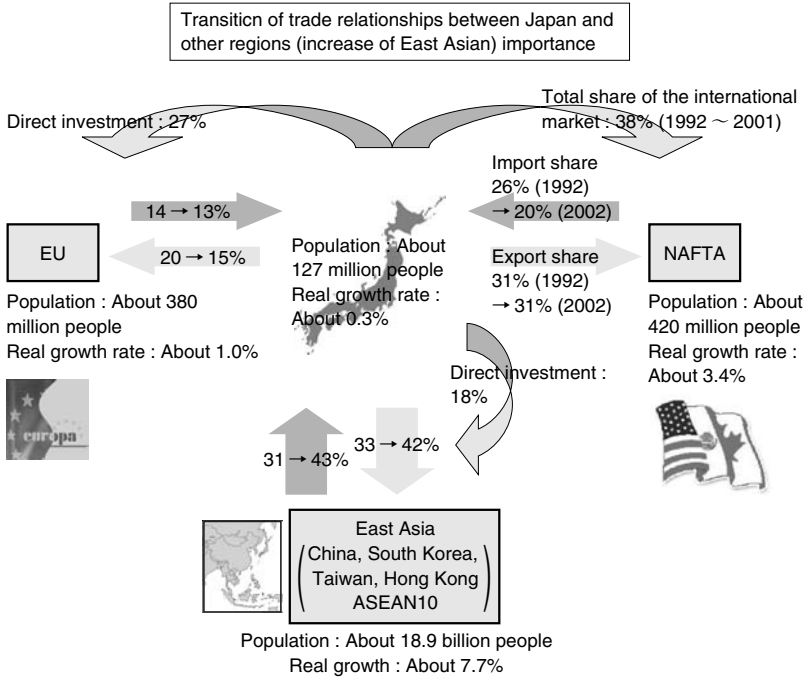
interpret regional contributions” flexibly and adopt a policy to selectively provide assistance that is designed to achieve “poverty reduction through economic growth” to countries outside of East Asia if they meet certain criteria. Given that economic collaboration is deepening with South Asia, an emphasis on greater Asia should be at the core of the regional strategy. With regard to Africa and other regions, it is meaningful to assist countries that meet certain governance criteria — such as political and economic stability — in a way that suits the local conditions and energizes the private sector. However, in the case of Africa, the role of yen loans is more limited than in Asia (at present grants and technical cooperation play a central role). In addition, in the short term it would be difficult to increase direct investments in the African manufacturing industry as rapidly as was done in East Asia. Therefore, except for a few countries with natural and energy resources, it is likely that Japan will, for the time being, focus its efforts on strengthening the linkages between agriculture and industry, and promoting basic industrial development through industrializing rural communities by utilizing the local agricultural produce and developing local industry.

The following sections discuss how to formulate and implement economic cooperation policies that consider the needs of both Japan and the international community, based on dual perspectives for strategic aid and the vision of “two-track ODA”: (i) attend to economic integration in East Asia through PPP support to more developed countries and development assistance support for less developed ones (“regional contributions”); and (ii) effective initiatives for reducing poverty in the poorest countries, as part of international cooperation (“global contributions”).

(2) “Regional Contributions” — Economic collaboration in East Asia, reducing intra-regional disparities

Over many years, Japan has built a close economic cooperation relationship with East Asia, and the trade and investment relationship has deepened even further in the last decade. As Figure 5-8 shows, East Asia (including China, Korea, Taiwan and the 10 ASEAN countries) has a population more than four times that of NAFTA and the EU, and is the most important trading partner of Japan in terms of both imports and exports. As these trade and investment relationship deepens, it creates strengthened demand for economic cooperation to promote economic collaboration.

Figure 5-8. Transition of trade relationships between Japan and other regions (increase of East Asian) importance



material : METI

Note: If the years are not listed, follow the example. Population and real growth rate are the data of 2002.

In order to sustain dynamic development in East Asia, economic cooperation to improve trade and investment in the areas of infrastructure building should be continued in terms of hardware, software, and human resource development, etc. At the same time, attention must be paid to the fact that countries in the region are at different levels of economic and industrial development, and that contents and focus of economic cooperation should differ accordingly. For example, for advanced ASEAN countries that have already built industrial infrastructure, such as Thailand and Malaysia, it is important to build “hard” infrastructure by supplementing private resources with public assistance, to build “soft” infrastructure for building more advanced institutions, to develop industrial human resources centering on highly skilled specialists, and to help improve their international competitiveness through promoting private investments even further. Relatively developed countries that have achieved a certain level of development, such as Indonesia, the Philippines and Vietnam, need assistance that promotes indus-

trial accumulation by improving the investment environment, including hard and soft infrastructure building, promotion of SMEs, and human resource development for supporting industries. The least developed ASEAN countries such as Cambodia, Laos and Myanmar (CLM) require assistance in basic “hard” infrastructure building, institution building for more efficient distribution of goods, and cooperation for reducing economic disparities in the region (Ministry of Economy, Trade and Industry (2005b)).

The Ministry of Economy, Trade and Industry (METI) and JICA each has recently published a noteworthy report on adopting PPP for infrastructure projects (see chapter 8 of this volume for details). In certain areas where private companies can enter without government financial support, infrastructure can be built with PFI (Private Financial Initiative) or through privatization. In areas where private companies cannot enter without government support, projects are not commercially viable unless the government and private companies share the costs and risks appropriately. The PPP method, which utilizes fiscal and aid resources, can be especially helpful in building infrastructure in developing countries (see Figure 5-9). PPP can be positioned between ODA and commerce and be expected to create commercially viable areas where corporations have previously not entered (market failures)

Figure 5-9. Definition of PPP

Commercial viability	Measures	
Sectors where commercial viability can not be created at all	Government finance (including loans)	
Sectors where commercial viability can be created through public-private partnership	PPP	Involvement of the government
Sectors where commercial viability already exists		Privatization of private enterprises

Finance package : developing countries' finance, grant aid loan, technical cooperation, commercial loan

Source: Report of the Asian PPP study Group METI (April, 2005)

notes: Private financial initiative PFI means private enterprises operate the whole market mechanism when it is commercially viable. On the other hand, PPP enables private enterprises to make profits, by having both the government and private enterprises share the proper cost and risk, in the project where private enterprises might lose their profits if they operate alone. Also, PPP is the methodology even when private enterprises can make profits, increase the efficiency through market enhancement.

through “market enhancing measures” such as government built infrastructure in the project site vicinity, corporate subsidies and user fee subsidies.

To promote infrastructure building with PPP, it is essential to establish appropriate financing mechanisms. Both the METI and JICA reports propose financing mechanisms that combine different schemes such as grant aid, yen loans (concessional loans), export credits and commercial loans.²⁰ (for details, see Figure 4-12 in Chapter 4). In addition, the JICA report contemplates utilizing technical cooperation to build institutions necessary to promote PPP and conducting development studies (sector studies) to formulate financing packages for PPP. This is significantly different from the traditional concept of development studies (feasibility studies for specific grant aid or yen loan projects), and includes analyses of power demand, project plans, fund-raising and post-completion budgeting as well as the design of financing packages. With regard to budgeting, the business management point of view would take account of construction costs and the beneficiaries’ and residents’ ability to pay to determine the amount of subsidies (grant aid and yen loans).

(3) Effective efforts to deal with “global issues,” aid to the poorest countries

From the perspective of “global contributions,” i.e., assisting the poorest countries in BHN centered on basic living conditions, peacebuilding and reconstruction, etc., it is especially important to attend to the issues raised in Section 5-3 above, “International aid environment surrounding grant aid cooperation,” and try to establish an effective aid approach and the requisite systems.

It is believed that many of the poorest countries in sub-Saharan Africa are having difficulties in achieving the MDGs, and that there is an extremely urgent need for BHN assistance in such areas as basic education, health and

20. Report of the Asian PPP Study Group of the Ministry of Economy, Trade and Industry (April 2005); JICA’s “Project Research on Infrastructure Building and Management Projects by PPP” (April 2005); and “Basic Research on Supporting the Introduction of Public-Private Partnership in Development Projects in Developing Countries” (March 2005). METI’s report proposes the creation of an “Asia Development Revenue Bond” based on project finance. In addition, it points out the ways to utilize ODA such as (i) providing yen loans to local governments (sub-sovereign), (ii) enhancing yen loans and technical cooperation for infrastructure management and administration, (iii) market enhancement measures by sector loans and grant aid (cost compensation), and (iv) using yen loans and CDM for ESCO (Energy Service Company) and urban transport projects, etc. JICA’s report examines the possibility of introducing PPP in JICA projects including development studies.

the fight against infectious diseases. These countries are highly dependent on aid. Especially in the areas mentioned above, there is active coordination between governments of developing countries and donors, as well as among donors. Considerable efforts is being made to improve aid effectiveness (such as sharing of policy frameworks, disbursements and procurement through the government's systems, higher predictability through aid budgets, as described in 5-3(3)). Therefore, when countries under these conditions are helped through grant aid, it is necessary to understand the reasons behind the emergence of international debates surrounding the improvement of aid effectiveness and then to work to improve the effectiveness of grant aid in terms of both contents and procedures.

In terms of contents, it is important to position each individual project within a policy and institutional framework, and to pursue program assistance which utilizes pooled funds and budget support through monetary and policy inputs so that the benefits of aid projects will spread to different areas even after completion. To accomplish this, the policy contents of grant aid cooperation must be enhanced, the processes of project requests and appraisals must be improved, different aid schemes such as technical cooperation and yen loans must be coordinated, non-project grants and counterpart funds must be strategically utilized, and aid modalities that institutionalize budget support and pooled funds must be formulated, among other things.

In terms of procedures, there must respond to the increased demand for putting aid money on-budget (disclosure of disburse amounts, budgeting the funds in the developing countries' accounts), and improve predictability of grant aid cooperation. The demand is expected to intensify for untied procurement that utilizes the government's systems and reduces costs. Given the recent improvement efforts described above (5-2 (4) and (5)), flexible use of non-project grants should be considered for countries which prefers more quantity with lower costs when it comes to building educational, health or sanitation facilities. In some cases, a decision to untie contracts (in phases) should be considered for general project grants, even if initially this is limited to the poorest countries and social sectors.

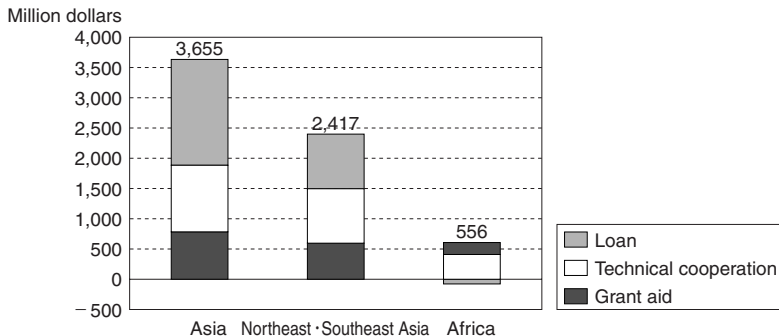
(4) More strategic and effective grant aid cooperation

Based on the above, the distinction between "regional contributions" and "global contributions," make it necessary to position grant aid cooperation

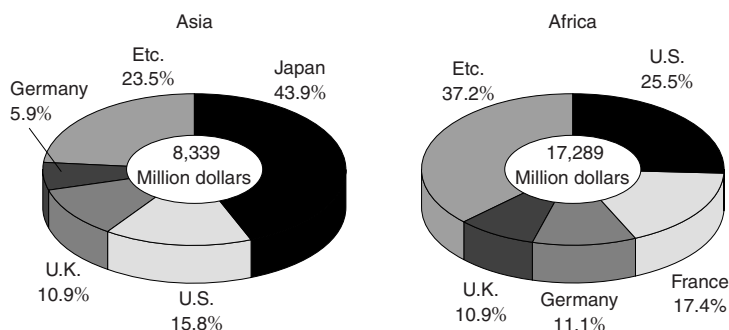
strategically within Japan's comprehensive vision of economic cooperation, and to take measures to enhance its effectiveness. In doing so, the following three points are recommended for government consideration: First, Japan is providing more grants to Asia than to sub-Saharan Africa. According to Figure 5-10, the average ODA for FY2002 and FY2003 (net expenditure basis) shows the amount of grant aid provided to East Asia alone exceeds that to sub-Saharan Africa. Second, in East Asia the effectiveness of grant aid must be considered while paying critical attention to its complementarity with yen loans and technical cooperation because various aid schemes are being used there. In contrast, grant aid itself is the central tool in Africa, so enhancing its effectiveness is important to the overall effectiveness of Japan's ODA (Figure 5-10). Third, while Japan is by far the largest donor in Asia, its presence in Africa is smaller than that of Western donors (at least in terms of aid amounts), so coordination with other donors is essential (Figure 5-11). These points should be considered in addition to the different needs of developing countries and the positioning of aid within their economic relationship with Japan, as described above; utilization of grant aid should be re-examined in each region and country. Based on such a comprehensive review of grant aid cooperation, it is appropriate to think about concrete measures such (i) fundamental revision of the aid schemes themselves and (ii) further reform of aid planning and implementation systems.

Fundamental revision of aid schemes: First, under strategic thinking and to change the scheme itself to facilitate use toward the desired objectives, grant aid should be combined with other Japanese aid schemes (packaging). For example, in economic cooperation with East Asia, grant aid could be

Figure 5-10. Regional allocation of Japan's bilateral ODA patterns
(On average of 2002 to 2003, net disbursement basis)



Source: MOFA (2004) ODA white paper

Figure 5-11. Percentage of regional disbursement DAC leading countries

Source: FOFA (2005) ODA white paper

incorporated, together with yen loans and commercial loans, into financial assistance for infrastructure building as part of PPP financing packages. That would be one way to utilize grant aid effectively. When grants are used as part of the PPP methodology (as user fee subsidies and corporate subsidies, etc.), untied schemes such as local currency assistance (budget support, pooled funds, etc.) by non-project grants might be the main modality, instead of conventional general project grants. On the other hand, in the BHN assistance for the poorest countries in sub-Saharan Africa and other regions, an effort would be needed to position grant aid within the policy system of the recipient country represented by the PRSP, and packaged with Japanese technical cooperation and other donors' assistance. In so doing, different schemes should be used such as general project grants, non-project grants and grant aid for grassroots human security based on the needs of the recipient country. At the same time, the introduction of new aid modalities that can provide local currency assistance, could be considered, as necessary.

From the introduction of grant aid in the late 1960s until now, many and various schemes and sub-schemes have been created, and the budget items have become increasingly segmented (see Table 5-1 above). This was undoubtedly caused by an opportunistic, short-sighted "approach" of government agencies which, in their budgetary requests to MOF, proposed new schemes or sub-schemes every time a newly emerged theme attracted international attention. However, at this time there are domestic and international demands to enhance the competitiveness and effectiveness of grant aid. Drastic rethinking of various existing schemes is called for, including the possibility of integration, scrap-and-build, and changing the schemes them-

selves.

Further reform of aid planning and implementation systems: Changes such as the “grantization” of international aid and the popularization of policy assistance to the poorest countries stimulated by the introduction of PRSPs mean that grant aid is more closely linked to the policy assistance framework, in which the former OECF (reorganized into JBIC) was involved through structural adjustments in the period before the Enhanced HIPC Initiative came into existence. Diplomatic missions (and JICA, JBIC) are required more than ever to be aware of the local policy framework represented by the PRSP and to deal with it by enhancing policy content and other measures. Moreover, given the results of the IDA 14 Replenishment, the World Bank is establishing the practice of providing aid based on policy performance and debt sustainability, and providing both grants and loans to the same country in line with the priorities of the PRSP. With regard to the future aid policy of Japan, the central ministries and agencies must build a system that can organically combine grants and loans based on the needs and debt repayment capacities of developing countries. Closer coordination among the MOFA, MOF, JBIC and JICA is required. With regard to strengthening the country-by-country approach, there have been important developments in recent years, such as the establishment of local ODA Task Forces and improvement and expansion of Country Assistance Plans. However, a mechanism or system should be created to ensure that grant aid is incorporated into these initiatives (both at the local level and at headquarters). To do so, the mandates of each division within the MOFA Economic Cooperation Bureau should be reviewed, Country Assistance Plans should be strengthened, allocated budgets should be coordinated strategically with local ODA Task Forces. Coordination among different aid schemes should be ensured.²¹

Finally, while the perspective based on “two-track ODA” emphasized in this chapter will become extremely important as grant aid cooperation is

21. On this point, the more comprehensive institutional reforms have been underway since 2006. These include: (i) the establishment of the Overseas Economic Cooperation Council — a ministerial meeting chaired by the Prime Minister and supported by the Cabinet Secretariat — to strengthen strategic planning of ODA (April); (ii) the establishment of the MOFA International Cooperation Bureau by integrating several divisions handling multilateral development into the Economic Cooperation Bureau (August); and (iii) the decision to integrate ODA loan operations (currently under JBIC) and substantial part of grant aid (currently under MOFA) into JICA by October 2008.

reviewed in a comprehensive manner, this does not cover all issues, and there may be other perspectives that should be considered. Although not covered in depth in this chapter, adequate consideration must be given to support for peace-building and reconstruction, which Japan is strengthening in response to recent international developments. To what extent should Japan get involved through bilateral aid, and what approach is appropriate? There are many issues to be coordinated such as the relationship with the current Constitution, the role of the Self-Defense Forces and international peacekeeping operations. How Japan deals with peace-building and reconstruction assistance will have a huge effect on the status of grant aid cooperation. Furthermore, in relation to the division of roles with technical cooperation, different aspects will be important, such as how to build a cooperative relationship with countries in East Asia which have “graduated” from aid and are now becoming emerging donors, and how to utilize grant aid.

Currently grant aid budgets are segmented, complicated and diverse, which limits the scope for strategic improvement described in this chapter. Now that its effectiveness and competitiveness are being critically examined, grant aid cooperation warrants a drastic overhaul and consolidation. This should be, based on the needs of recipient countries and Japan’s strategic thinking, from perspectives such as (i) assistance for low income (the poorest) and lower middle income countries (project, non-project assistance); (ii) PPP assistance and cooperation with emerging donors taking upper middle income countries into account (non-project assistance); (iii) assistance for peace building and reconstruction; and (iv) support for activities at the grass-roots level and NGOs. When this has been done, other issues should also be discussed, such as tied aid, the single-year budget system, and introduction of budget support-type schemes in non-project assistance (which currently conform to balance of payments assistance). To do this, a consensus should be formulated involving not only MOFA, but also MOF, METI, the Board of Audit, aid implementing agencies such as JICA and JBIC, and the business community and public. The recent debates on the restructuring of the ODA organizations, which was spurred by the reform of government-affiliated financial institutions, offers a great opportunity for a return to the basics and to think about the ideal future of Japanese economic cooperation, including grant aid.

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JICA and Future Technical Cooperation

Koichi Miyoshi¹

6-1. Introduction

The Japan International Cooperation Agency (JICA) has its roots in the Asia Society, an organization that was established in 1954, later to become the Overseas Technical Cooperation Agency in 1962. The name was changed to JICA in 1974, and in 2003 it was reorganized as an independent administrative institution.²

Japanese Official Development Assistance (ODA) includes bilateral grants (technical cooperation and grant aid), governmental loans, and contributions and capital subscriptions to international organizations. Among them, JICA is in charge of technical cooperation and grant aid that includes bilateral donations. The budget for grant aid belongs to the Ministry of Foreign Affairs, but JICA plans grant aid projects and supervises their implementation as part of its technical cooperation. In FY2005, JICA implemented grant aid and technical cooperation of ¥160.1 billion and ¥101.5 billion, respectively (JICA, 2005). JICA controls about 50 percent of technical cooperation funds and 60 percent of grant aid coming from the Japanese government.

A large part of technical cooperation not undertaken by JICA is government-financed foreign students from developing countries, mainly in Asia. Also included in technical cooperation are the activities of corporations and foundations such as the Association for Overseas Technical Scholarship and

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2. In addition, the government intends to integrate yen loans currently implemented by the Japan Bank for International Cooperation and grant aid implemented by the Ministry of Foreign Affairs into JICA as government-affiliated financial institutions are privatized and consolidated.

Japan Overseas Development Corporation that receive trainees and dispatch experts, among other things, as executing agencies for the technical cooperation budgets of related ministries.³

This chapter discusses JICA's technical cooperation and looks at its future by focusing on its institutions.⁴ When the author was involved in technical cooperation at JICA, he was most concerned with the relationship between technical cooperation activities and institutions. What JICA does or does not do is highly dependent on its institutions. In general, institutions are created to achieve specific objectives, but once established, they adapt to the changes in the environment. Changes are made to implementation methods and organizations, and institutions shape the activities of the organizations.

These changes, however, are largely defined and influenced by the nature of institutions when they were originally created. This is why it is important to look at JICA's institutional changes when we think about its future. Of special importance are the original technical cooperation methods and changes in institutions that were created based on them. Also important are the adoption of country-specific and thematic approaches in connection with the creation of Regional Departments in 2000 and the reorganization in 2003. Institutions created at the very beginning of technical cooperation and as a result of the 2003 reorganization define much of JICA's activities. This chapter describes these characteristics and examines JICA's technical cooperation. In this chapter, the term 'institution' is used as a broad concept that includes norms, rules, operational methods, and organizational arrangements.

The following section examines the institutional characteristics of JICA's technical cooperation. First we examine the characteristics of operational methods and institutions that are based on JICA's technical cooperation (schemes). JICA's aid schemes influence its technical cooperation, especially its organizations and operational methods, thus I would like to focus on them and highlight the changes in JICA's technical cooperation and their significance. Section 6-3 discusses organizational reforms, budget restructuring, delegation of authority to overseas offices, preparation of Country Implementation Plans and Thematic Implementation Guidelines in connec-

3. For example, the Association for Overseas Technical Scholarship receives executives, managers, and engineers from developing countries to Japanese companies for practical and management training with the objective of achieving economic growth and stability in developing countries.

4. The content of this chapter owes much to the author's involvement with planning, research, study, discussions, and consultations with involved parties, and observations of projects during his work at JICA from 1971 and 2003 and thereafter. The content of this chapter depends much on Miyoshi (2005).

tion with changes in the aid environment. It also surveys adoption of country-specific and thematic approaches. In Section 6-4, clarifies these changes are clarified by discussing specific examples of JICA's technical cooperation. The organizational changes caused by the adoption of country-specific and thematic approaches are beginning to change JICA's technical cooperation projects actually. Section 6-5 summarizes the changes in JICA's institutions based on discussions of the previous sections, and finally, suggests future directions.

6-2. Genesis of technical cooperation and elements that shaped JICA

(1) JICA's technical cooperation

The most prominent and broadly-recognized characteristic of JICA's technical cooperation is cooperation modalities, or schemes. While each aid organization has its own, JICA's schemes are unique in that they have defined how projects are implemented in detail and shaped JICA's technical cooperation. The schemes largely depend on how Japanese technical cooperation began. JICA's technical cooperation can be traced back to the Asia Society, JICA's predecessor, which began to accept trainees in 1954 when Japan joined the Colombo Plan and started to dispatch experts in 1955. Since then, JICA has used this modality oft to dispatched experts as its operational framework. It also accepted trainees and provided equipment as one element of technical cooperation. Schemes have dictated the daily operation of technical cooperation and JICA's organizational structure. Budgets were prepared, written requests from recipient countries were submitted, project selection methods were defined, and organizations were created on a scheme-by-scheme basis. Moreover, by dispatching experts and later accepting trainees and providing equipment in association with these experts, the schemes offered in-kind aid instead of providing money to the recipients.⁵ The operational systems were structured to fit the schemes.

5. Technical cooperation from other aid agencies is mainly based on experts and training, the same as in Japan, but in many cases it is implemented with fund-provision-type procurement methods. Also, based on recent criticism of the use of foreign experts, some donor countries are reviewing their activities. The United Kingdom and the Netherlands, for example, are reducing the number of domestic experts, which relates to untying technical cooperation. On the other hand, Canada, the US, and France are emphasizing project-oriented cooperation. Technical cooperation by the World Bank and regional development banks often employs advisors for studies that prepare plans for loan projects and formulate policies.

These schemes were defined in detail in budgetary requests and associated explanations, and in JICA's various operational procedures.⁶ While the schemes have changed based on the evolving development needs, the changes have been gradual — necessary changes would be made to an existing scheme and the scheme would be then be reorganized into a new scheme. Implementation methods that centered on dispatching experts and accepting trainees never changed. When a new scheme is requested and approved as a new budget item, the budget and implementation scheme are in effect inseparable.

More specifically, JICA created new schemes such as the project type technical cooperation and development studies, which now account for the majority of its activities. These meet the needs of development cooperation by expanding the older schemes of dispatching experts and accepting trainees, but these new schemes are essentially a combination of dispatching experts, accepting trainees, and/or providing equipment, and are an extension of systems that existed at the beginning of technical cooperation.

The main schemes for technical cooperation took several forms. Characteristically, each scheme is further divided into smaller activities.

Acceptance of trainees. This scheme is divided into group training courses where training is established for specific themes — individual training based on a developing country's specific requests and long-term training where trainees study for more than a year to obtain an academic degree. Detailed implementation methods are designed for different types of trainees: general technical trainees, governmental general requested trainees, third country trainees, second country trainees, paid trainees, international organization trainees, development cooperation trainees, immigration trainees, invited junior trainees, Japanese descent trainees and regional proposal-type trainees. Group training courses are carried out at 12 international centers located in various parts of the country, with cooperation from training implementation agencies based on the common needs of developing countries. Training is administrated by the instructors sent from cooperating organizations. Overseas training is divided into third country training and local domestic training (second country training). Third country training a country within a region that shares a social and cultural background is conducted in and has better technology in a certain area and provides training that suits regional conditions. Local domestic training is provided in the

6. For details, see JICA's internal rules and implementation guidebooks.

recipient country to meet its specific development challenges by developing human resources within the country. These training programs are implemented by cooperating organizations based on JICA's technical cooperation activities.⁷

Dispatch of experts. This scheme dispatches individual experts and project experts. As for project experts they will be described later. Individual experts are dispatched to administrative agencies and research institutions in developing countries as advisors etc. and transfer technology to engineers or administrative officers who are designated as their counterparts. Sometimes a team of several experts is dispatched to provide technical guidance, research assistance, or policy recommendations in a certain field or for a certain issue. In this case the cooperating agency is appointed and the cooperation is implemented in a way that is similar to a project. Depending on their activities, experts fall in a number of categories: general experts, third country experts, overseas technical training instructors, international organization experts, grant aid experts, disaster assistance experts, country-specific project planning experts, thematic project planning experts, and grassroots technical cooperation experts.

Project-type technical cooperation. To increase its effectiveness, project-type technical cooperation combines the dispatch of experts, acceptance of trainees, and provision of equipment. This scheme covers four broad sectors — social development; healthcare, population and family planning; agriculture, forestry and fishery; and economic and industrial development. This scheme consists of primarily human resource development, dissemination of technology, and research and development. And it is implemented by counterpart agencies such as universities, training centers, and research institutions. This type of cooperation has been implemented in conjunction with grant aid, for example, the Jomo Kenyatta University of Agriculture and Technology Project in Kenya. Project period is typically five years, and the typical budget is between ¥300 and ¥500 million.

Development studies. Development studies support public development plans in developing countries covering social development, agricultural and forestry development, and industrial development. Depending on content of study and the project phase, the scheme is also divided into master plan studies, feasibility studies, and preparation of basic data such as topographic maps. The studies are conducted by a team of consultants who com-

7. Many training implementation agencies administer training courses as domestic training or educational organizations. JICA's training is often implemented as a customized version of such courses.

pilesummarize their work in a report. These reports are used by developing countries for their policy decisions, and also by JBIC and international financial institutions as basic data for iudging whether they should provide loan or not.

Grant aid. Grant aid falls in six categories: general grants, fisheries grants, aid for increased food production, food aid, cultural grants and disaster relief grants. As part of its technical cooperation, JICA administers the implementation of general grants, fisheries grants, and grant aid for the increase of food production, all of which have close connection with technical cooperation. General grants cover healthcare, education, agriculture, and transportation and include construction of hospitals, schools, water supply and irrigation facilities, as well as provision of construction equipment, materials, and buses, etc. 50% of project type technical cooperation is implemented in conjunction with grant aid. Currently, the dispatch of experts, project-type technical cooperation, development studies, and third country training are unified into a new operational modality, Technical Cooperation Projects, but their original divisions remain. This will be discussed later.

(2) Technologies to be transferred and utilized — Experience of experts and that of Japan

What concepts were behind the creation of these schemes? First, JICA's technical cooperation was based on a method that aimed to develop human resources and to strengthen organizational capacity in developing countries by transferring Japanese technology. That is why the dispatch of experts abroad and training in Japan by expert instructors have been important components of JICA's technical cooperation.

Saito (1979, pp.37-38) discusses the channels of technology transfer and makes the distinction between technology that is embodied in capital and technology that is embodied in people. Under this classification, one characteristic of JICA's technical cooperation was that it relied mostly on technology that was embodied in people, or experts, and aimed to transfer and use technology through experts who were engineers. Equipment and facilities were also provided at the same time, but they were considered only as a means to transfer and use the experts' knowledge and skills.

In this type of technical cooperation where main actors are technology that is transferred and utilized are mostly in the form of personal experience, subjective insights, and even gut feelings of the experts, or what we might call 'tacit knowledge'. In JICA's technical cooperation, advice and training by

experts that creates reciprocal communication become an important factor. Technical cooperation requires face-to-face activities, and for this reason expenses for sending experts and accepting trainees accounts for much of JICA's budget. During in FY2004, JICA dispatched 4,340 experts. The number is even larger if 7,548 members of dispatched study team are included. JICA accepted 20,089 new trainees in FY2004 in the same year. Technology transfer through Japanese experts is considered most important.

The emphasis in this type of technical cooperation is the technology embodied in Japanese experts and Japan's experience in development. Therefore the experts are principally Japanese. Most JICA experts were sent from public organizations such as the central government, local governments, public foundations, as well as universities, research institutions, and training centers. Their work based on 'hard' technology that supported implementation of Japanese development policies, but a few programs based on 'soft', such as legal system improvement.⁸

(3) Technology transfer to specific organizations as projects

Next, let us look at the implementation of technical cooperation. Technical cooperation was initially aimed at a person-to-person level. Japanese experts were sent as technical advisors to organizations that needed technology and transferred their knowledge and skills to their counterparts. It is expected that these counterparts then share the transferred technology with others which results in taking root in developing countries.

Technology transfer which started as dispatch of individual experts and receiving trainees has now expanded to specific organizations, especially research institutes, universities, and training facilities. Project-type technical cooperation was introduced as a scheme to enable efficient technology transfer for specific organization. Organizations or agencies were selected or newly established for technology transfer, which was expected to be systematically transferred to engineers and researchers who were counterparts of the Japanese experts.

The scheme's evolution from the dispatch of individual experts to project-type technical cooperation had a significant impact on the development of JICA's technical cooperation and organizational structure. These schemes were considered an effective way to implement technical cooperation with educational and research institutions such as universities and vocational

8. In recent years legislative cooperation has been emphasized and is being attempted as a new thematic area.

training schools. From 1954 to 2003, 246,277 trainees were accepted and 70,694 experts were dispatched.⁹ A considerable number of them were mainly trainee received from these projects and experts dispatched from these cooperating educational and research institutions. Between 1953 and 2002 there were 916 project-type technical cooperation.¹⁰ There were many 'model' projects that were part of the effort to strengthen capacity of recipient organizations.

These schemes have their roots in the Technical Cooperation Center Initiative advocated by Prime Minister Kishi in 1957 when he visited Thailand, East Pakistan (Bangladesh), Ceylon (Sri Lanka), and Iran. Technical training centers were built in Thailand (for telecommunications), East Pakistan (for agriculture), Ceylon (for fisheries), and Iran (for small and medium enterprises), and they became the prototype for project technical cooperation. The ASEAN Human Resource Development Project, advocated by Prime Minister Suzuki in 1981 during his visits to the five ASEAN countries, tied technical cooperation to grant aid and strengthened this approach. The ASEAN Human Resource Development Project, which included the Human Resource Development Center in the Philippines, Primary Healthcare Training Center in Thailand, Vocational Training and Advanced Skills Training Center in Malaysia, Training Center for Vocational Training Instructors and Small-Scale Industry Promoters in Indonesia, and Productivity Improvement Project in Singapore, showed such characteristics as well (JICA, 1999a). King Mongkut's Institute of Technology Ladkrabang in Thailand, the Higher Education Development Plan in Indonesia, Jomo Kenyatta University of Agriculture and Technology in Kenya, and Vocational Training Center in Senegal, among others, are often cited as typical JICA projects.¹¹

(4) Emphasis on ensuring output — Project based approach by schemes

What was emphasized during project implementation? One of the criteria used to select projects is consistency of the recipient country's policies and development plans. Projects were considered as a means to support the policies, but the policies themselves were not discussed very much between

9. Based on JICA documents.

10. The number 916 is an approximation. It includes 692 between 1954 and 1997 (Reference Section of the JICA 1998 Annual Report) and 224 projects started in the five years between 1998 and 2002 derived by searching projects using the CD-ROM of JICA 2003 Annual Report.

11. On many occasions this has been described as a typical JICA project.

recipient country and Japan. Policies were treated as a given because interventions are considered to be an interference in domestic affairs. Another reason is that traditionally developing country's policies were often little more than project lists and were not constructed as a policy structure.^{12,13}

Such tendencies were also found in development studies. A development study is a scheme that dispatches teams of experts to developing countries to prepare development plans, but many studies took the existing policies as a precondition and focused on making plans for infrastructure. The result is that many plans proposed by development studies involve infrastructure such as roads and transport networks, water supply facilities, waste disposal systems, and power generation and distribution facilities.¹⁴ In this sense we can say that JICA's technical cooperation has been based on a project based approach and emphasized output. Given the lack of a clear policy structure in developing countries, this was an effective way to cope with the situation. JICA's scheme-based institutions were formulated in this environment and produced results.¹⁵

(5) Scheme-based operational departments

The implementation of scheme-based technical cooperation reflected on the organizations as well. When the Overseas Technical Cooperation Agency, JICA's predecessor, was established in 1962, its main components were the Domestic Operation Department that implemented training programs, the Overseas Operation Department that dispatched experts, and the Development Studies Department that dispatched study teams. Subsequently, technology transfer to specific organizations in recipient countries was implemented by creating the Sector Operation Department that combined the dispatch of experts, acceptance of trainees, and provision of

12. Here, the term 'policy structure refers to the relationship between a series of objectives and the means to reach those objectives as indicated sequent levels of policy, program and project.

13. In aid meetings and on other occasions, aid requests were often presented in the form of project lists.

14. Many development study reports focus their analyses and discussions on facilities and not on the changes in policies and program or, measures, organizations and, or institutions that affect condition of the facilities.

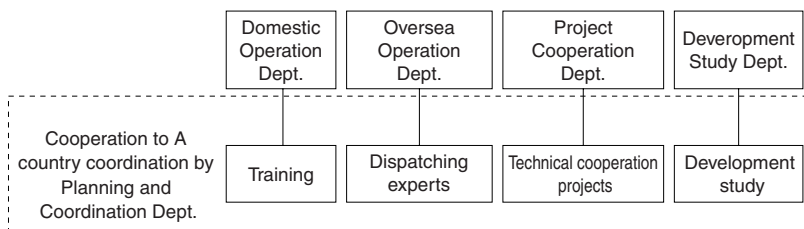
15. *Effectiveness and Challenges of Japanese International Cooperation* (2003) attempted to verify aid effectiveness by looking at the Cebu Socio Economic Empowerment and Development Project in the Philippines, the Improvement of Educational Achievement in Science, Technology and Mathematics in Basic Education Project in Ghana, Pharmacy Project in the Philippines, High-Yield Rice Cultivation Technology Research Institute Project in the Philippines, Training Services Enhancement Project for Rural Life Improvement in the Philippines, Nursing Education Enhancement Project in El Salvador, and Reproductive Health Project in Vietnam, among others, as JICA model and its results show the same tendency.

equipment and materials which were implemented by these operational departments. By the time JICA was established, the Sector Operation Department had developed into five sectoral departments (social sector, agriculture, forestry, industry, and healthcare), and became the main department for JICA's operations.

These five sector operations were implemented with separate budgets and different procedures and departments in charge were generally arranged by operational modalities and sectors, thus they effectively promoted JICA's scheme-based methodologies. This organizational arrangement would continue until the shift to a country-specific approach in 1999, which will be discussed later.¹⁶ The emphasis on schemes led to standardization of operations which in turn made it easier for staff to learn and execute efficiently. It also made it easier to maintain close communication with domestic cooperating agencies (mainly the line ministries at central level). For these reasons, we can say that the emphasis on schemes worked as an effective mechanism during the period of aid expansion.

Figure 6-1 shows the cooperation for a specific development issue in 'Country A' under this organizational system. In the scheme-based operational department system, each department selected and implemented projects. Each operational department examines the feasibility of projects based on requests from the country and make decision. Projects are then coordinated during annual consultations with the country. Next, based on this coordination, the decision to implement the projects would be communicated,¹⁷ and as a result, cooperation with Country A became what is shown inside the

Figure 6-1. Cooperation to A country and measures to individual schemes



16. At the time it was established, JICA had other operations such as technical cooperation including the above mentioned activities, the Japan Overseas Cooperation Volunteers, development cooperation, and emigration. Subsequently, grant aid and operations related to disaster relief emergency femergency rescue teams were added, and the scope of operations was further expanded.

17. Traditionally, annual consultations with developing countries were conducted on a scheme-by-scheme basis.

broken lines — collection of scheme-based aid projects. Each project was implemented separately by each operational department.

6-3. Reorganization as an independent administrative institution and introduction of country-specific and thematic approaches

(1) Creation of Regional Departments

The creation of regional departments triggered drastic changes in JICA's scheme-based aid system. With its organizational reform in January 2000, JICA created four regional departments (I for Southeast Asia; II for the East, Southwest, Central Asia, the Caucasus and Oceania; III for the Middle East, Africa, and Europe; and IV for Latin America and the Caribbean). Regional Departments were formally promoted from regional divisions that belonged to the Planning Department, but they had a significantly different impact on JICA. In addition to country-specific project planning, coordination, project identification, and formulation, Regional Departments became responsible for overseas training and dispatch of individual experts. This change in jurisdiction shifted JICA's project implementation system from scheme-based where Operational Departments selected the scheme and individual projects to country- and region-based where Regional Departments were in charge. Creation of the Regional Departments strengthened the country-specific approach and changed operational implementation methods. Country Implementation Plans and Thematic Request Surveys began a systematic process of clarifying and positioning turning schemes as into the means of development cooperation.

(2) Country Specific Implementation Plans and Thematic Request Surveys

Country Implementation Plans were prepared to implement the government's aid policies described in the Country Assistance Plans and other documents. Plans were written for all of JICA's operational schemes in countries where it has overseas offices. The plans were prepared in the following order: (i) confirmation of the country's priority sectors and issues through policy dialogues at the government level; (ii) consolidation of development issues and clarification of JICA's operational cooperation policies; and (iii) establishment of concrete goals and preparation of systematic input plans for each operational modality to achieve these goals. Through this process, JICA

was expected to accumulate the practical consultations with counterparts of the recipient country and formulate a consensus on prioritized development issues and specific projects.

The plans included: (i) basic policy of JICA's cooperation based on the recipient country's development goals and priority areas, priority aid areas of the Japanese government, and the government's policies themselves; (ii) a development issues matrix (which analyzes development issues and areas and extracts JICA's cooperation programs), an operational rolling plan (which lists a planned combination of projects in chronological order over five years for each development issue), and an input plan for each scheme (which lists the number of projects on the rolling plan for each scheme); and (iii) cautions related to the implementation structure of the recipient and safety issues, lessons learned from past evaluations, and activities by other major donors.

Thematic Request Surveys evolved from surveys of developing country requests for technical cooperation that used to be implemented for each operational scheme. They are an attempt to identify the recipient country's problems and the aid that is necessary to address them. Thematic Request Surveys have been adopted in phases since FY2000. In the surveys, each scheme is considered as a means to address specific issues in the recipient country. They are expected to match the country-specific thematic approach that JICA is trying to promote under the Regional Departments system, and align with the operational program planning process that addresses development issues.

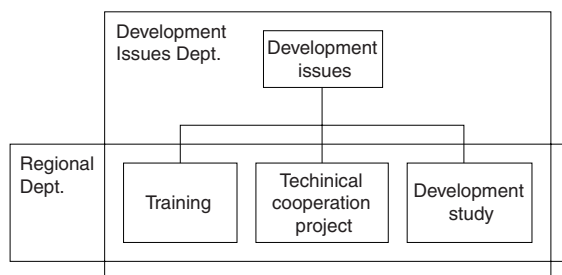
(3) JICA as an independent administrative institution with Regional Departments and Development Issue Departments

The effort to turn schemes into means was accelerated by the 2003 reorganization of JICA as an independent administrative institution and by consolidation of organization system consisting of with Regional Departments and Development Issue Departments. The new JICA inherited the old operations and organizations, but JICA was given a certain level of autonomy to administer its operations effectively and efficiently. Parts of its operations were abolished or changed — development loans and investments and emigration support operations were abolished, peace-building support was explicitly added as an objective, and supporting civil cooperation activities was recognized as an official activities. Other changes include more autonomy and flexibility in the administration of operations, organizations, and budgets, and increased

emphasis on results through the adoption of medium-term targets and performance evaluation systems. In this new framework, budgetary systems, operational methods, and organizations were reviewed and reformed.

In April 2004, the four Regional Departments were reorganized into five by creating a department in charge of Africa separating from Department III. Also, the eight Operational Departments that had been organized in accordance with schemes (five in charge of project-type cooperations and three in charge of development studies) were reorganized into five Thematic Departments (Social Development, Human Development, Global Environment, Rural Development, and Economic Development). Development issues had been tackled by each scheme, but this reorganization established a matrix system based on regions and issues that tries to resolve issues by combining various inputs and assembling projects (Fig. 6-2).¹⁸ This was a huge change for JICA. Old scheme-based operational methods and organizational structures came to an end, and they were reorganized by country and by development issues. Schemes are now clearly positioned as a means to solve these issues.

Figure 6-2. Development issues of A country and measures by the scheme formation



(4) Preparation of Development Issue Guidelines

To strengthen the thematic approach, Development Issue Guidelines were prepared along with the Country Implementation Plans. Development Issue Guidelines are prepared by the Sectoral and Thematic Network that was established based on thematic teams composed of JICA personnel and thematic support committees that include external experts. The guidelines include (i) current situations of the development issue and trends in international aid; (ii) trends of Japanese aid and lessons learned; and (iii) JICA's

18. The World Bank and the US Agency for International Development (USAID) were each reorganized into a matrix structure in the late 1990s.

cooperation strategy, and prepared as guidelines for future planning and implementation of cooperation activities. The Country Implementation Plans and Development Issue Guidelines are expected to support planning and implementation of problem-solving programs of developing countries based on JICA's country-specific approach, combine the three pillars (country- and region-based approach, development issues, and operational schemes) systematically, and enable highly-qualified cooperation activities specifically tailored to solve the issues of developing countries.

(5) More flexible budget structures and delegation of authority to overseas offices

JICA has been trying to shorten the lead time of projects, remove the barriers between different budget items, and reorganize and consolidate budgets. For example, overseas training, dispatch of individual experts, development welfare support programs, and development partner programs were consolidated under overseas cooperation activities. In this manner, budget structure was converted so that funds can be shared among different schemes. When JICA was reorganized as an independent administrative institution in FY2003, the budgets for the primary operations of technical cooperation such as training, technical cooperation projects, and development studies were consolidated into technical cooperation projects. This consolidation of budget items, together with the establishment of Thematic Departments in April 2004, provided flexibility to the preparation and implementation of country plans, laying the groundwork for dealing more effectively with thematic issues.

This added flexibility in budget structure also accelerated the delegation of significant authority from headquarters to overseas offices. Traditionally, operational departments in JICA's headquarters were responsible for project implementation and overseas offices were only partially responsible for project supervision. In the new system, overseas offices bear responsibility for the entire project cycle, from project identification and project formation to planning, implementation, and evaluation. This devolved system became possible by changing JICA's scheme-based project administration.

6-4. New changes and their potential

These institutional changes are beginning to have an effect on JICA projects. Four project trends reflect these changes.

(1) Water Supply System Capacity Building Project in Cambodia: Cooperation for an entire administrative organization

The Water Supply System Capacity Building Project in Cambodia was implemented from October 2003 to October 2006. The counterpart organization was the Phnom Penh Water Supply Authority (PPWSA) within the Water Supply Bureau of the Ministry of Public Works. This project is an example of technical cooperation that was designed for an existing administrative organization. It was implemented as a project that was deeply embedded as a basic component of Cambodia's policy system. In similar projects in Thailand, Vietnam, Indonesia, and Egypt, JICA established independent organizations, usually a central training center, and trained personnel based on the idea of establishing a project. In reality there were more than a few cases that had sustainability problems — in some cases budgets were cut after the project was completed because those training centers were organizationally distant from the target administrative agencies. In the Cambodian project, the training center was incorporated into the administrative agency (which was also the implementing agency). This was an expansion — from limited assistance designed to transfer water supply technology to a specific training agency in the water supply sector to assistance designed to bring about changes in the entire water supply system.

This kind of technical cooperation requires compliance and strict consistency with Cambodia's water supply sector policies and strategies. In fact, the project was designed to contribute to human resource development that supports institutional reform in the water supply sector and expansion of water supply systems to meet the demand. Organizational capacity building through human resource development was essential. Coordination with other aid agencies was required, and the project used multiple schemes in a more programmatic approach.

Water supply facilities have been built with assistance from donors, and there is an urgent need to train personnel to operate and maintain new facilities efficiently. In Phnom Penh, the Chroy Changwar Water Supply Facility, which was constructed with a loan from the World Bank, began operation in 2002. Expansion and rehabilitation of the Phum Prek Water Treatment Plant, which was financed by Japan's grant aid, was completed in 2003. With completion of these two facilities the gross water treatment capacity of PPWSA almost doubled from 120,000 cubic meters per day (supplying water to about 332,000 users) to 235,000 cubic meters per day (about 545,000 users). Also, rural water supply systems outside of Phnom Penh that fall under the juris-

diction of the Water Supply Bureau of the Ministry of Industry, Mines, and Energy, are being administered in 28 cities (as of 2002, the gross water treatment capacity was 38,000 cubic meters per day, supplying water to about 126,000 users). New water supply facilities are being built by Japan's grant aid in Siem Reap City, loans from the Asian Development Bank are rehabilitating six facilities, and loans from the World Bank will finance 149 facilities.

This project educates and trains employees of the PPWSA, the Water Supply Bureau of the Ministry of Industry, Mines, and Energy, and rural water supply agencies. It is also expected to expand training of prefecture water supply departments, part of which is currently outsourced. A training center has been established to train rural water supply engineers and trainers are trained there.

The project team includes three Japanese long-term experts. In addition, short-term experts from Japan provide on-the-job training to senior officers. Employee training programs are being conducted both in Japan and Thailand. The training programs in Japan are tailored for each recipient agency after consultations between experts and agencies, and are producing good results. Kitakyushu City is the implementing organization of the project in Japan. Training at the Metropolitan Waterworks Authority's Waterworks Technology Training Institute (MWTTI) in Thailand focuses on project management. The programs are implemented based on a contract between JICA and MWTTI. Japan has before never before implemented systematic human resource development using training centers, but now the training at MWTTI is an effort to learn how to run training centers. This project has a study component to prepare a water supply sector master plan that is being implemented simultaneously. With regard to developing human resources in subjects closely related to water supply such as water chemistry control, the development study currently being conducted will reveal real needs for human resource development. JICA plans to prepare a long-term plan based on the results of this study.¹⁹

(2) Use of overseas resources: Exploiting overseas technologies and experience

As authority has been delegated to overseas offices, some JICA projects are using local operation budget and other resources available from neighboring countries. Examples include the Water Supply Human Resource

19. Based on the JICA thematic evaluation, *Assistance for South-South Cooperation*.

Development Project in Laos, the Water Supply System Capacity Building Project in Cambodia, Project for Strengthening Health Services for Children in Laos, and Health Services Assistance Project of the Maternal and Child Health Project in Cambodia (Phase II).

These Japanese technical cooperation projects use related agencies in Thailand and Malaysia, establish training courses, and build systems that compliment Japanese technology and experience. Water supply projects incorporate training at the Waterworks Technology Training Institute in Thailand, and health projects incorporate training at Khon Kaen University and Chiang Mai University in Thailand and Sarawak General Hospital in Malaysia, respectively. The implementation itself was undertaken under the contracts between JICA offices in Laos and Cambodia on one hand, and the training implementation or expert dispatching organizations. The characteristic here that training courses are designed according to the will of each project which is the beneficiary of the training. Training participants are selected deliberately based on the outcome expected by the organization that sends the trainees, so that the training implementation organization and trainee dispatching organization clearly recognize it and confirm its manifestation.

For example, the objective of the Water Supply Human Resource Development Project in Laos is to improve the technological and administrative capacity of water supply agencies in Laos and seeks to improve capacity in water pipe installation and management, operation and management of water treatment facilities, and water quality control by water supply agencies throughout Laos. Resources in Thailand were incorporated in the project during the planning phase. For example the plan incorporates training in Thailand at the Waterworks Technology Training Institute, invites Thai and Japanese experts, in addition to counterpart training in Japan. Training content was determined after consultations with the implementing agencies.

While these projects are similar in form, their training approaches are different because the countries' development and languages are different. In the Water Supply System Capacity Building Project in Cambodia, the training courses were conducted under a contract between the JICA Cambodia Office and the Waterworks Technology Training Institute in Thailand. Because there were not many trainees, the major training was conducted in Japan, and unlike the initial plan, only the training on issues unique to developing countries was conducted at the Waterworks Department of Thailand.

In the Maternal and Child Health Project in Cambodia-Phase II, between 2000 and 2002 13 people were sent to Khon Kaen University in Thailand and

four people to Sarawak General Hospital in Malaysia. These training courses were created based on the needs of Cambodia identified by Japanese experts. The experts accompanied the trainees so they could assess and adjust parts of the training.²⁰

(3) Asia-Africa Knowledge Co-creation Project: Program-oriented training projects

The Asia-Africa Knowledge Co-creation Project exploits the region-specific training framework to encourage Asia-Africa cooperation based on the needs and initiatives of African countries. Participating organizations in Asia and Africa work as partners to create and share projects such as policy proposals for development issues, proposals for organizational improvements, manuals for practitioners, and project proposals.

This is an attempt to convert a training operation that was traditionally a scheme into a project. This project includes seminars and symposiums as training schemes and research activities as Policy Research Projects (PRP) in participating African countries. The scheme (training) is used as a means to an end. One of the characteristic is that the project is based on Asian technology particularly Thai and Indonesian.

The first phase was introductory seminars in Japan and Thailand to share the Asian experience and project objectives. In the mid-term seminar in Thailand, participating Asian and African organizations discussed proposed policy research projects prepared by the African organizations based on the introductory seminars with the purpose of creating projects. Through this work organizational partnership were established to implement the policy research projects. Four groups of PRPs were established:

Group 1 — Poverty reduction through processing agricultural products and income-generating activities.

- Kenya: PRP for making a food processing manual
- Malawi: PRP for making an extension officer manual using ‘one village one product’.

Group 2 — Natural resources management

- Senegal: PRP for making a water resource management plan
- South Africa: PRP for Soil conservation

20. Based on the JICA thematic evaluation, *Assistance for South-South Cooperation*.

Group 3 — Capacity building for farmer associations and extension systems

- Uganda: PRP for Capacity building for extension officers in irrigation
- Zimbabwe: PRP for Improving extension systems

Group 4 — Indigenous knowledge, local resources, changes in behavior

- Ethiopia: making an extension officer manual using area studies
- Tanzania: PRP for Community-based AIDS management

Participating organizations included those involved in rural community development in eight African countries (Ethiopia, Kenya, Malawi, Senegal, South Africa, Tanzania, Uganda, and Zimbabwe), equivalent organizations in Thailand and Japan, the African Institute for Capacity Development (AICAD), and a JICA technical cooperation project in Indonesia, Community Empowerment Program with Civil Society in Indonesia (PKPM Project). JICA participants included external advisors for this project, people in charge in domestic and overseas JICA organizations, and consultants.

The policy research projects are being implemented by the respective African countries and related organization of the Asian counterpart country with financial assistance from JICA. Final products were prepared through collaborative work between the related organizations in both African and Asian countries based on the dispatch of African experts to Thailand and Indonesia as well as dispatch of Asian counterpart organizations to Africa.

The final seminar is expected to be held in Africa to share the results, and subsequently, projects will be implemented based on those results.²¹

(4) Education Project in Honduras: Promoting the program approach

Since Hurricane Mitch hit the country hard in 1998, Honduras has prepared several strategies — the Master Plan for National Reconstruction and Transformation (PMRTN), Poverty Reduction Strategy Paper (PRSP, 2001), the Government Plan by the Maduro Administration (2002), Ministry of Education Action Plan (2002), and Education for All—Fast Track Initiative (EFA-FTI, 2002). Most recently, the EFA-FTI Plan was prepared based on these strategies and projects are underway.

More than 90 percent of the government's education budget is allocated to teacher salaries, thus implementation of the EFA-FTI projects depends on donor assistance and education plans are influenced by donors. Major activi-

21. Descriptions here depend on the author's participation in JICA's Asia-Africa Knowledge Co-creation Project. Ethiopia's PRP was not implemented at all.

ties include improving the efficiency of basic education such as developing educational materials and teacher training. While the EFA-FTI plan receives financial assistance from the common fund established by the World Bank, Canada, Sweden, Germany, and other donors, project technical cooperation is also recognized as an aid modality. Each donor cooperates based on its their own aid modality.

Since support for reconstruction after Hurricane donor coordination is arranged through donor meetings. Under this circumstance, JICA is implementing the Basic Education Enhancement Program that includes the Arithmetic Instruction Improvement Project, Model Projects, and policy advisors, which provides an example of a program approach.

The Basic Education Enhancement Program aims to improve the efficiency of basic education and the quality of teachers. Many donors support teacher training and making teaching materials to improve graduation rate, which is one of the goals in EFA-FTI. One important component of the program is to improve arithmetic capacity which is overall goal in EFA-FTI. Developed teaching materials are distributed nationwide and other donors provide funds or use them for training. While JICA's Basic Education Enhancement Program and Spain's project support training for incumbent teachers, Germany supports training for new teachers. The US has offered to develop standardized, common achievement tests to verify academic improvement. All of these activities considered to be complementary.

To support educational policies, two long-term experts have been dispatched to coordinate aid in the education sector and to formulate educational projects. These experts are involved in the JICA program and Honduras basic education sector to prepare programs and promote aid coordination, and have played an important role in the development of JICA's program. The aid coordination expert has contributed to preparing and implementing the EFA-FTI Plan as chairperson of donor meetings in the education sector. This is why the basic education program that was prepared before the EFA-FTI Plan was ensured a position and was able to play an important role in achieving aid coordination in the Basic Education Enhancement Program. Both of these experts had been Japan Overseas Cooperation Volunteers in the Honduras education sector before, and their expertise and experience were of considerable help (JICA 2006).

6-5. Sustainability of JICA's institutional changes due to its reorganization as an independent administrative institution

JICA's technical cooperation structure has changed since Japan began providing aid based on scheme, but pivotal changes occurred in 2000 when Regional Departments were created. The reorganization as an independent administrative institution made these changes more obvious (Table 6-1).

Table 6-1. Institutional change of JICA before and after the transformation into independent administrative institutions

	before	after
Approach	<ul style="list-style-type: none"> · Active use of schemes · Segmented · Independent 	<ul style="list-style-type: none"> · Development issue-oriented activity · Country oriented and issue-oriented approach · Consider schemes as measures · Formation of different scheme
Method of technical assistance	<ul style="list-style-type: none"> · In-kind · Procurement from Japan 	<ul style="list-style-type: none"> · In-kind · Use of contracts · Procurement from Japan and outside Japan
Concept of development assistance	<ul style="list-style-type: none"> · Technical transfer to the counterpart · Technical transfer by the expert · Emphasis of Japanese technology and experiences · Emphasis of setting the place 	<ul style="list-style-type: none"> · Capacity development of counterpart institution · Combination and use of technology and experiences both inside and outside Japan
Organizational structure	<ul style="list-style-type: none"> · Scheme based management style · Initiative by the head quarter 	<ul style="list-style-type: none"> · Issue based management style · Initiative by the overseas offices
Level of Intervention	<ul style="list-style-type: none"> · Output-oriented · Purpose is to transfer the technology 	<ul style="list-style-type: none"> · Outcome-oriented · Purpose is to realize the outcome

In its former configuration, JICA's technical cooperation, project implementation methods, and organizational systems were based on schemes, and projects were implemented in accordance with the schemes. Each scheme had the authority to execute its budget independently and to implement projects, and projects were implemented within the framework of schemes. A scheme was an independent entity and each one adopted a project approach with an output that it can manage itself as an objective. In scheme based approach Japanese technology and experience were treated as resources, resources that depended on Japanese experts. The main objective was to transfer technology to a counterpart, and the project was considered complete when the output was confirmed.

Amidst significant changes in the aid environment, however this former

configuration met institution fatigue. The creation of Regional Department was to address this problem. It promoted turning schemes into means for development cooperation. They established a process where projects are based on country-specific implementation plans and Thematic Request Surveys from recipient country. Such moves provided an opportunity to consolidate the budget and created momentum to combine multiple schemes. Under this circumstance, JICA was reorganized as an independent administrative institution. Introduction of the thematic operational system, which was implemented along with the reorganization as an independent administrative institution, accelerated the process of turning schemes into means. Delegation of authority to overseas offices also promoted this process.

Procurement procedures also changed. Procurement based on contracts made it easier to use foreign technology and experience. All these changes have made it easier to implement country-specific and thematic approaches. More outcome-oriented operations are now possible.

6-6. Conclusion — strengthening country-specific and thematic approaches

This section takes a new look at the framework of JICA's technical cooperation, discusses its challenges, and discusses the future of technical cooperation.

(1) Reorganization of the framework of technical cooperation: Policy structure of developing countries and technical cooperation

Government activities are generally divided into levels such as policies, measures, and projects that emerge as a series of policy structures. Figure 6-3 shows a policy structure of a developing country with three levels. Causal connections formulate policy structures, for example, final outcomes (changes in the target society), intermediate outcomes (changes in the target groups, including people and organizations), outputs (goods and services produced by activities), activities (a series of acts that use inputs to produce outputs), and inputs (human resources, materials, equipment, administrative costs, facilities, funds, expertise, time, etc.).

Figure 6-4 shows such a policy structure in a matrix.²² Recently, developing countries have implemented various reforms in fiscal and financial management, organizations, education, health, and decentralization, and consequently their policy structures are clearer. On the other hand, donors are

Figure 6-3.

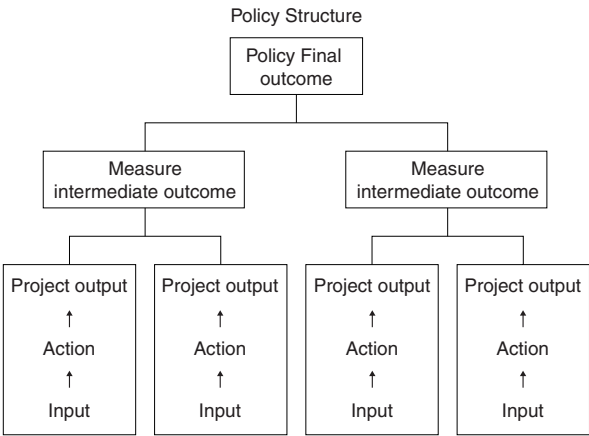
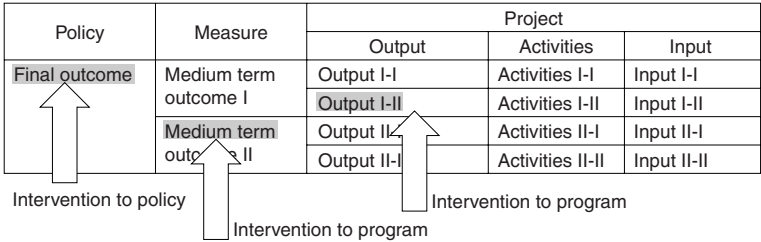


Figure 6-4. The policy system and Intervention to the policy, program, and project in developing countries



increasingly involved as stakeholders in policy formulation through policy dialogue and policy supporting activities. As a result, aid activities can now be divided into two large categories — assistance at the policy and program level and traditional assistance for projects. In Figure 6-4, arrows show the positioning of a donor’s assistance and interventions through technical cooperation in the policy structure of a developing country. Technical cooperation at the policy and program level deals with effective ways to distribute resources to establish goals, legal systems, organizations, institutions, or selection of projects to achieve the final and intermediate outcomes. There emphasis would be placed on overall capacity building by using a combina-

22. Turning a policy structure into a matrix enable it to be controlled. For such conceptualization of policy structures by matrices, see JICA Planning and Coordination Department (2004) and Miyoshi et al. (2003).

tion of organizations and technologies that already exist within the recipient country, instead of technology transfer to specific organizations.

Technical cooperation for projects emphasizes producing outputs, and supports efficient implementation of projects as measures of policy and program implementation — planning, implementation, and evaluation. Within such a framework, donors would be required to clarify which parts of the developing country's policy structure they address, support and intervene. In this case, projects would look very different when they are implemented as part of a program that aims to ensure outcomes compared to when they are implemented as individual and independent projects.

(2) Future challenges

With such a framework for technical cooperation and based on our examination in the previous sections, the author would like to point out the challenges faced by JICA's technical cooperation.

Turning schemes as into means for development cooperation.

Traditionally, implementation of JICA projects has been dictated by schemes, but this scheme-oriented system has been shifting to a system that turns schemes into means for development cooperation. Now it is based on country-specific and thematic approaches as a result of institutional changes that accompanied the creation of Regional Departments. Traditionally, JICA developed its operations to fit the schemes, but the turning of schemes into means allowed selection of means that fit the development issue. Such a trend promotes a shift from a project-based approach to a program-based approach. It becomes possible to combine schemes and provide support in accordance with the outcome. To promote this trend, we need to pursue the path of turning schemes as into means even further to include grant aid and yen loans. From now on, we need to include these in our pursuit of turning schemes into means. Based on our examination, an effective way would be to consolidate all schemes under Regional Departments. The author believes that the introduction of such an institution would be effective.

Reforming procurement for more effective use of resources. Use of various resources is becoming especially important in JICA's technical cooperation because, while we examined JICA's institutional changes in this chapter, JICA's in-kind procurement method remains unchanged. Such a procurement method has been appropriate for technical cooperation that implements Japanese technology and experience through the dispatch of Japanese experts. It legitimized securing experts from Japanese public organizations,

however, the scope of technical cooperation is expanding.²³ It is impossible to deal with such circumstances with JICA's traditional scope of activities. It is important to construct a broader mechanism that uses the various resources that exist in Japan and abroad.

Partnerships with domestic universities and other organizations will be an important factor to expand resources for technical cooperation. One approach would be to incorporate foreign universities into JICA projects by using the domestic network of universities. It will be essential to seek resources broadly outside from Japan. Up to now JICA has provided technical cooperation to many organizations and agencies many of whom have already graduated from being recipients. JICA should use these resources that have close relationship with JICA. To do so, the in-kind procurement method needs to change into contract-based and further to budget finance-based. The current in-kind provision of experts and training opportunities gives and constraints on cooperation and interventions. More flexible procurement methods will make it easier to use a wider range of resources.

Selection and clarification of approaches. When selecting technical cooperation projects, it is important to clarify whether the objective is cooperation for the policies and programs of a developing country, or cooperation for projects and through what kind of approach the technical cooperation should be implemented. As Figure 6-4 highlights, it is important to recognize the differences between these two approaches. For the policy and program based approach, important factors include the ability of aid agencies to analyze policies as well as consultation and coordination with various stakeholders. In recent years JICA has been implementing the policy and program based approach under the name of cooperation for policy support assistance, but it still does not have a clear assistance concept, and it has not accumulated sufficient experience. Especially, for project-type cooperation, JICA is required to clarify its position about which projects will contribute to the recipient country's policy structure. It is necessary to take a program based approach which, unlike the traditional project-based approach, positions technical cooperation projects within the policy structure and supports the overall implementation of policies together with other projects. And under this program based approach, it is necessary to support projects that aim for outputs that ensure outcomes, instead of aiming for the outputs themselves.

On the other hand, such cooperation for policies and programs will have

23. For example, see Chapter 9 for constraints in Africa.

a strong connection to the previously discussed methods for procurement and fund provisions as well. For cooperation to policies and programs, the dispatch of experts, support for symposiums and seminars, studies to formulate policies and programs, and joint evaluations to assess effects will be important. These activities require flexibility because they must be implemented by aid organizations under the leadership of developing countries, however, JICA has had little experience in these policies and programs based approach. This is a significant disadvantage, and in addition the current methods of procurement and fund provision do not have the flexibility that facilitate this kind of cooperation and interventions. Rather, these procurement and fund provision methods restrict activities and make it difficult to capture appropriate opportunities and act in a timely manner. A system that allows flexible actions is required.

Strengthening an outcome orientation and emphasizing evaluations. The shift to a project program based approach means that the focus of assistance shifts from outputs to outcomes. To emphasize outcomes, we must identify the desired outcomes and clarify the logic of project activities. Moreover, implementation capabilities are required. It is important to position JICA's projects in the policy structure of the developing country by asking such questions as what are desired outcomes, what kinds of project activities will produce those outcomes, and what kinds of capabilities are required. Only after we clarify the logic in the policy structure and implement the project can we expect to see the effects of JICA's technical cooperation. To ensure such outcomes, it is essential to incorporate various stages of evaluation from *ex ante* and *ex post* evaluations in the project management cycle. Moreover, program based evaluations with a focus on policies and programs need to be implemented.

Emphasis on aid coordination. Aid agencies' project implementation methods have changed significantly due to the introduction of strategies that aim to reduce poverty in developing countries and efforts to clarify the policy structure. There is new recognition that it is difficult for individual aid agencies to produce satisfactory outcomes, and agencies are moving to identify areas in which they can cooperate. JICA will also be required to identify where it could contribute, and this will lead to share roles with other donors. During implementation JICA will be required to coordinate progress. To do so, it is necessary to emphasize aid coordination more than ever.

This chapter examined the characteristics and changes of JICA's technical cooperation with a focus on its modalities or schemes, as well as the insti-

tutional changes which have taken place. Creation of Regional Departments diminished the superiority of schemes that had defined JICA's technical cooperation and instead brought the country- and issue-oriented program approach. This is a paradigm shift in JICA's technical cooperation. The issues discussed in this section are to further strengthen these institutional changes and are mutually linked. They will affect the future of JICA's technical cooperation, and more broadly the future of Japanese technical cooperation. And, discussions on JICA's changes and institutions will intensify under the integration of yen loans with JICA's operations. The author hopes that the results of this chapter's examinations will also provide some insights to such future discussions.

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Human Security and Aid from the Perspective of an Aid Practitioner

Koji Makino¹

People tell me that they don't quite understand the concept of human security. Some even dismiss it merely as an abstract slogan or advocacy, but it is a practical concept that can be useful to us all.

We are constantly exposed to many hidden and unpredictable risks — traffic accidents, sudden illness, unemployment, fires, and earthquakes, for example. In developing countries with suffocating poverty and poor governance, people face far greater risks than those in industrialized countries, and the consequences are more serious because their ability to cope with them is limited (The ultimate and worst outcome could be mega-death). Those especially vulnerable to crises are the extremely poor and the socially disadvantaged. In various crises, the combination of 'fears' and 'deficiency' can become a vicious spiral that in turn causes livelihoods to deteriorate (downside risks). The concept of human security focuses on those downside risks and attempts to find a comprehensive solution.

This chapter attempts to interpret the concept of human security as plainly as possible from the development perspective of an aid practitioner, and then discusses its implications for aid.

7-1. Background and history

7-1-1 Human security

In recent years people, goods, money, and information have traveled frequently across national borders, and societies have become increasingly interdependent. Concurrently, regional conflicts, terrorism, and infectious

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diseases (HIV/AIDS, avian flu, for example) are also crossing borders and threatening people more than ever. In some cases, states themselves have become a threat to people (such as Iraq and Sudan). Traditional conceptual frameworks that consider states as the smallest units, including national security, are inadequate to cope with these new and grave international threats. What is needed today is the concept of 'human security' that focuses directly on people.

7-1-2 History

The first appearance of human security in a public document occurred in the 1994 Human Development Report of the United Nations Development Programme (UNDP). Subsequently, the Japanese government's advocacy at the UN Millennium Summit in September 2000 led to the creation of the Commission on Human Security, co-chaired by Sadako Ogata (now President of JICA) and Amartya Sen (now a professor at Harvard University). After five meetings, the Commission submitted its report to UN Secretary-General Kofi Annan in May 2003.

The Japanese government considers human security as one of the pillars of its diplomacy. In 2003, the government revised the Official Development Assistance Charter, the core of Japanese aid policies, and positioned human security as one of five basic principles. The Medium-Term Policy on Official Development Assistance (New Medium-Term ODA Policy), adopted in 2005, positions human security as a core philosophy of substantive aid and states that it is "a perspective that should be reflected in all of development assistance." To promote the achievement of human security, the Japanese government created the Trust Fund for Human Security in the UN in 1999.

At the G8 Summit in June 2003 (Evian Summit), Prime Minister Koizumi's statement led to the inclusion of this sentence in the Chair's Summary: "We took note of the report of the Commission on Human Security." In addition, the Leaders' Declaration at the 11th Asia Pacific Economic Cooperation (APEC) Economic Leaders Meeting mentioned their commitment to "enhancing human security."

In Africa, an NGO network, African Human Security Initiative (AHSI), was created to monitor the human security efforts of the governments of leading member countries of the African Union (AU). More developing countries are launching concrete initiatives. For example, Thailand created the Ministry of Social Development and Human Security and Bolivia may position human security as a pillar of its new national development strategy.

According to the final document of the UN World Summit in September 2005, the world leaders made a commitment to “discussing and deepening the notion of human security in the General Assembly.”

7-2. Human security

7-2-1 Definition

What is the concept of human security? The report of the Commission on Human Security defines it as “to protect the vital core of all human lives in ways that enhance human freedoms and human fulfillment,” and to construct the systems necessary to do so.

In addition to this definition, the Japanese government complemented the approaches to realizing human security that are mentioned in the Commission’s report, such as “protection and empowerment” of people. It defined human security in the New Medium-Term ODA Policy (February 2005) as “focusing on individual people and building societies in which everyone can live with dignity by protecting and empowering individuals and communities that are exposed to actual or potential threats.”

As examples of threats to people, the Medium-Term Policy lists fears, such as conflicts, terrorism, crime, human rights violations, displacement, epidemics of infectious diseases, environmental destruction, economic crises, and natural disasters; and deficiency, such as poverty, hunger, and lack of educational and health/medical services.

7-2-2 Interpretation of human security

To rephrase these definitions, human security (i) guarantees the bare necessities and essentials for people’s lives and livelihoods; (ii) ensures that those guarantees will not be lost in the future; and (iii) builds mechanisms to do so. To simplify even more, we can say that human security is a “framework for building a society where people can live in peace.”

The content of (i) above corresponds to the “vital core of all human lives” in the official definition, but even the report and other related documents state that human security is difficult to define because it is different depending on the country, region, and situation in which people find themselves. However, we can interpret it to include basic human needs such as minimum income, education, healthcare, and water, as well as political and social rights. It can be interpreted as an approach to deal with the problems of poverty in a broad sense.

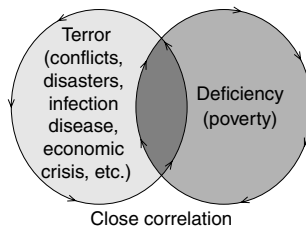
Even if (i) is temporarily secured, people can lose it due to political unrest, unexpected natural disasters, accidents, and illness because they are always in an unstable condition. Therefore, (ii) states the necessity to take measures so that it will not be lost.

For (iii), the Commission's report aims to build an integrated system of politics, society, environment, economy, military, and culture (building the mechanism), and concludes that to do so, we need to not only improve the capabilities of the state, but also build strong partnerships with other players such as NGOs, international organizations, regional organizations, and civil societies. The objective of mechanism building is to promote two approaches at the same time — one to 'protect' people in the form of governments and other actors providing various (social, economic, political, military) services, and the other to 'empower' people.

7-2-3 Freedom from deficiency and freedom from fears

The added value of human security as a concept in comparison to other concepts, theories, and strategies of development lies in the fact that it focuses on downside or downturn risk. People, especially those in developing countries, are always exposed to risks that may turn worse — what we call downturn risks. That is why we have emphasized not only the relatively static point of (i) guaranteeing the bare necessities and essentials for people's lives and livelihoods, but also the dynamic aspect of (ii) ensuring that those guaranteed things will not be lost in the future.

Figure 7-1. Concept of human security



What are the factors that give rise to those downturn risks? While it is impossible to present an exhaustive list, people are negatively and severely affected by various risks categorized as fears in human security, including conflicts, terrorism, crime, human rights violations, epidemics of infectious diseases, environmental destruction, economic crises, and natural disasters.

In human security, broader issues of poverty such as hunger and lack of educational and health services are categorized as deficiency. The true worth of the concept lies in the fact that it attempts to correlate and analyze these issues of deficiency and fears, and thereby find comprehensive solutions to these problems. In our interpretation of human security, (i) guaranteeing the bare necessities and essentials for people's lives and livelihoods corresponds to solutions to the problem of deficiency, whereas (ii) ensuring that those guaranteed things will not be lost in the future is related to the problems of fears.

7-2-4 New aspect of poverty — perceived risks

(1) Findings of participatory poverty assessments

Various participatory poverty assessments (PPAs) in many countries including the Voices of the Poor project of the World Bank, have recently revealed that people are extremely concerned about the uncertainty of their future. Poverty includes not only the state of few or low-level possessions, but also the precarious situation (vulnerability) where people can lose even the few things they have (the ultimate misfortune being a sudden death). In some cases the poor consider the uncertainty of lives and livelihoods due to potential shocks more serious because of lack of access to income and social services (Meier and Stiglitz, 2001).

Aspects of fears such as vulnerability and shocks are very closely correlated to the aspects of deficiency or poverty. Those who are most severely affected by various shocks are the vulnerable people who suffer from broadly-defined poverty or other deficiency, including the extremely poor, the illiterate, those who cannot maintain physical health, those who lack social and political rights, and the socially disadvantaged (elderly people, widows, pregnant women, children, and the handicapped). In developing countries we often observe a situation where those who suffer from deficiency are pounded repeatedly by significant external shocks such as conflicts and natural disasters as well as smaller shocks, and spiral down into a more severe state of poverty. The perspective of human security focuses on this serious situation where the already poor are exposed to risks that can make them even poorer.

(2) Vicious cycle of fears and deficits

Let us consider the case of a poor farming family in rural Africa. Usually they

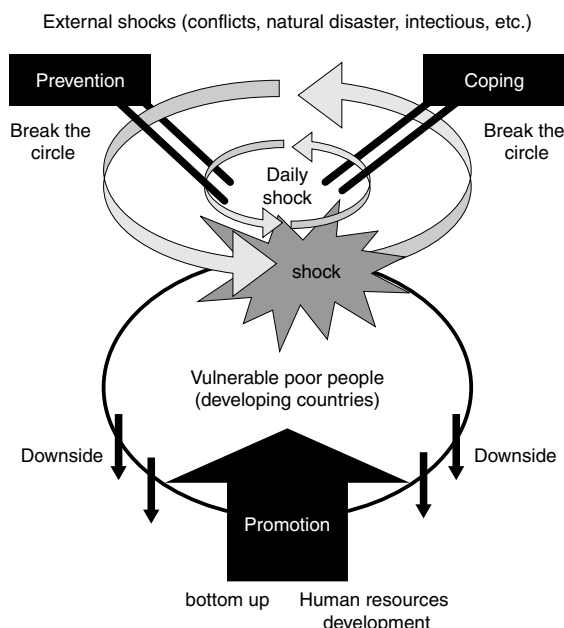
cultivate a small parcel of land to produce mainly maize and several other vegetables to eke out a scanty livelihood. If this poor peasant family was hit by a serious natural disaster in the form of a drought (e.g., a 'fear'), what could they do? If this household were hit by severe damage that could not be mitigated by eating all their stored food and receiving help from an informal network of the community and nearby relatives, this family, which does not have any savings in the bank or benefits from a non-existent governmental social safety net, would be forced to sell their means of production such as cattle or part of their land. We have seen situations where they stop sending children (mostly girls) to school. The Voices of the Poor report points out that the poor have very limited options to cope with these shocks, and they face difficult trade-offs to simply survive until the next day.

Even if the drought ended and the next wet season provided enough rain for cultivation, the family would be poorer because they already sold their cattle and must rely on manpower, or they sold a part of their land and crop yields would be reduced. If parents cannot provide a decent education for their children, the next generation is likely to be just as poor as its parents, thus poverty is inherited. This example depicts a vicious cycle where an already poor household that suffered from deficiency is hit by a fear in the form of a drought that makes the situation worse and the household poorer. One can easily replace the drought with any other element of fear such as a conflict, sudden illness of parents or an accident. These vicious cycles are widely observed in developing countries.

7-2-5 Development strategy that incorporates human security

Based on recognition of the situations described above, assistance strategies in developing countries that incorporate the perspective of human security should aim to end this vicious cycle of deficiency (poverty) and fears (risks). We need to think about three aspects of risk management: (i) prevention/mitigation of fears (threats and risks), (ii) coping with human security crises, and (iii) promotion of medium- and long-term abilities to cope with risks in order to reduce chronic poverty. The figure 7-2 is a visualization of this concept (JICA IFIC, 2005).

A basic measure to promote poor-sensitive growth aims to support the poor through human development and improved governance. In addition, we need to complement it with (i) prevention/mitigation through measures that prevent fears or reduce risks, and (ii) coping, adequate measures to deal with fears when they arise.

Figure 7-2. Human security's perspective incorporated development (assistance)

For example, in a case dealing with HIV/AIDS, one would first take measures to prevent the shock of being infected such as education, provision of contraceptives, and improved testing based on the reality that there is no cure for AIDS at the moment (prevention/mitigation). If people are actually infected with HIV/AIDS, one would take reactive measures such as treatment to delay the onset of the disease, counseling, and caring for patients who develop AIDS (coping). However, given that those who are vulnerable to the fear of HIV/AIDS are the poor, these direct measures against HIV/AIDS are insufficient. In fact, it is important to have a broader effort to increase their income and improve basic healthcare, education, and political participation (promotion).

Once a natural disaster — an external shock — such as an earthquake, flood, drought, or typhoon strikes, it causes extensive damage. However, according to the report of the Commission on Human Security, *Human Security Now*, in the 1990s the number of reported natural disasters was more than twice the number in the 1970s, but due to preventive measures (prevention and coping), the number of victims in the 1990s was only 40 percent of the 1970s figure. The rate of fatalities from natural disasters in coun-

tries with good performance in human development is estimated to be 1/13 of the rate in countries with bad performance. These statistics provide evidence that promotion, prevention, and coping are effective.

7-2-6 Approaches to achieving human security — protection and empowerment

As actual approaches to achieving human security, protection and empowerment are considered important. The government and other organizations safeguard people from serious threats of fears and deficiency through various services (protection), and at the same time ensure that they can cope with the threats by increasing their ability to act for themselves or others (empowerment). One can liken this process to a person who not only wears armor to fortify his or her surface, but also obtains true strength by training his or her mind.

The Human Security Report states that protection and empowerment complement and strengthen each other, and empowered people not only avoid immediate dangers but also demand improvements in the mechanisms to protect them. Specific examples would include a case where empowered people warn the government of a food shortage in its early stages, encouraging the government to act and prevent a famine before it happens; or a case where they protest human rights violations by the state and pave the way for a better legal system.

In reality, the ‘place’ where protection and empowerment take place would be the community. The safety of an individual cannot be separated from the functions of a social community to which he or she belongs. In other words, to achieve human security it is essential to strengthen the community through protection and empowerment.

For example, a technical cooperation project that JICA is implementing in Niger is designed to improve governmental ‘protection’ in the form of basic education services, but it also encourages parents and local residents to actively participate in school activities in an attempt to create better schools. This is leading to empowerment of communities that creates a virtuous cycle.

7-3. Relationships between human security and MDGs, PRS, human development, and other aid strategies

7-3-1 Millennium Development Goals (MDGs)

Human security is considered a concept that supports the achievement of the

Millennium Development Goals (MDGs). Human security emphasizes the importance of freedom from fears and empowerment that are not expressly stated in the MDGs.

Among the several agendas of the Millennium Declaration,² MDGs focus mainly on those related to development and poverty reduction. The Millennium Declaration contains other agendas such as “peace, security, and disarmament;” “human rights, democracy, and good governance;” and “protecting the vulnerable.” These agendas are closely related, and unless we tackle them comprehensively, achievements in individual agendas will not be sustainable. Human security, which focuses on people and brings all of the various threats people face into view, is positioned as an important concept for realizing the visions of the Millennium Declaration.

To achieve the MDGs or the visions of the Millennium Declaration, it is essential for people in developing countries to improve their ability to solve their own problems. For this to happen, it is important to not only increase the amount of aid, but also to support human resource development, organizational enhancement, and institutional building through aid.

7-3-2 Poverty Reduction Strategies (PRs)

Human security does not replace the existing frameworks or agendas of international coordination such as Poverty Reduction Strategy Papers (PRSPs), but complements and strongly supports them. Human security approaches the prerequisites for the proper functioning of international coordination frameworks or the achievement of international agendas.

It is no exaggeration to say that development/aid agendas have been consolidated into a single goal of poverty reduction. Under this poverty reduction rubric, some donors in the international community have tended to shift most of their resources to social development sectors that would directly lead to poverty reduction. However, the Japanese government has advocated an approach of supporting sustainable poverty reduction through growth. To reduce poverty, we need to balance the distribution of social development measures and growth-oriented measures centering on improving productivi-

2. In September 2000, the United Nations Millennium Summit in New York brought together 189 heads of states who adopted the Millennium Declaration which states the goals of the international community in the 21st century. The Declaration contains an agreement of the international community to collaborate and coordinate on seven themes in order to achieve fair and sustainable world peace: (i) Peace, security and disarmament, (ii) Development and poverty eradication, (iii) Protecting our common environment, (iv) Human rights, democracy and good governance, (v) Protecting the vulnerable, (vi) Meeting the special needs of Africa, and (vii) Strengthening the United Nations.

ty and competitiveness, all of which is underpinned by improved governance. All aid activities boil down to a strategy of supporting that direction.

This direction is now largely supported by the PRSPs of various countries and the IMF/World Bank joint review of the PRSPs. By focusing on people and introducing the dynamic aspects of poverty such as threats, risks, and vulnerability into the paradigm of poverty reduction, which includes social development and growth-oriented measures, the concept of human security has established a new axis. Another characteristic of human security is that in order to cope with risks, it requires stronger public actions from the international community, governments, and NGOs, including 'horizontal' collaboration among development actors, 'vertical' collaboration between governments and communities, and comprehensive approaches.

For example, in agricultural development, PRSPs prepared under the strong influence of IMF/World Bank tend to adopt market-oriented approaches, but from the perspective of human security, they must be balanced with the concept of food security which requires that minimum food supplies are ensured. It is vital that promotion of technological innovations, increased production, and a stable food supply through sensible use of market functions goes hand in hand with increased income and food purchasing power of individual farmers. This ability to present policy alternatives to PRSPs is another strategic contribution of human security (Takahashi, 2005).

BOX 7-1: Human security and economic development

Some may believe that economic development projects and human security have not much in common, but they would be wrong. One major reason why the Japanese government began to take serious initiatives in human security was the Asian currency crises. In his speech in Singapore in May 1998, then-Foreign Minister Obuchi called for consideration for the effects of the Asian currency crises on the poor and other vulnerable people and pledged support for human security-related efforts.

In the concept of human security, not only are prompt and appropriate actions after a currency crisis considered important, but also reduction of risks and prevention of future crises. In the context of economic development, for example, one would promote measures that contribute to macro-economic stability. At the same time, pro-poor growth is considered extremely important from the perspective of human security.

Chapter 5 (Economic Security) of the report of the Commission on Human Security identifies four policy action priorities to promote human security:

- Encouraging growth that reaches the extreme poor,
- Supporting sustainable livelihoods and decent work,
- Preventing and containing the effects of economic crises and natural disasters, and
- Providing social protection for all situations.

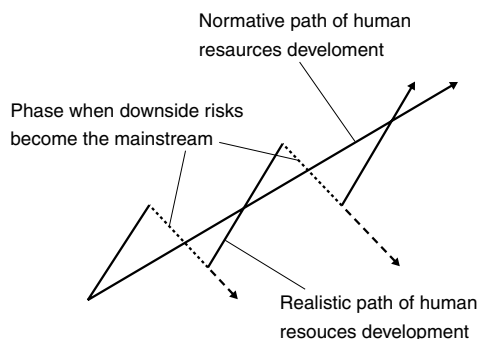
7-3-3 Human security and human development

Human development and human security have a complementary relationship. Sen, who was the co-chair of the Commission on Human Security together with JICA's President Ogata, clarified the relationship:

Human development focuses on “progress and expansion” and has an “upward-oriented, optimistic quality,” whereas human security is a concept that focuses on “guarding the rear in order to defend what must be defended” and pays attention to the “risks of sudden distress,” while attempting to empower people so that they can overcome these risks (Mine, 2005). “Human security” complements the optimistic and expanding nature of human development by deliberately focusing on downside risks (JICA IFIC, 2005).

Figure 7-3 is a visualization of this distinction (Mine, 2005). While human development aims for upward development, in the real world of developing countries various shocks such as conflicts, economics, and natural dis-

Figure 7-3. Human resources development and human security



asters occur and put downward pressures to people and countries. The concept of human security attempts to face and cope with these negative dynamics.

7-4. Incorporation and use of human security in development assistance

7-4-1 Basic concept

To incorporate the concept of human security into development assistance, it is helpful to divide the process into two stages or levels — the aid strategy stage (strategy level) and practical application stage (project or program level).

(1) Aid strategy level

The first step is to review the existing aid strategy or the national development plan (such as PRS) of the recipient developing country from the perspective of fears and deficiency to determine if existing aid priorities adequately deal with these issues. Even if they do, are they connecting the two elements?

Depending on the situation, different questions should be asked. For example, in the area of fears, one could ask whether the aid priorities consider or are effectively dealing with the impact of civil war, military threat from a neighboring country, ethnic conflicts, unstable economy, natural disasters such as droughts, infectious diseases such as AIDS and malaria, and organized crime. In the deficiency category, the main question would be whether existing aid is effectively addressing the issues of broadly-defined poverty such as income, basic healthcare and educational services, water and shelter, etc.

Aid can only address a portion of the needs of a recipient country, so existing aid may not cover all the fears and deficiency of the country in question, or it addresses either one or the other. The point is that when we review or formulate an aid strategy, this perspective helps us identify elements that are otherwise easy to miss so that we can modify the plans accordingly (especially fears that are often overlooked).

Another point to keep in mind is that many efforts seemingly in the area of deficiency can simultaneously address fears. For example, if aid priority is a stable water supply and the specific aid components are construction of a dam, building supply networks, and institution building, the project will not

only address the lack of water supply (a deficiency issue), but also some issues of fears by controlling the river and thereby preventing floods and alleviating the effects of drought. While we should initially look at things from the perspectives of fears and deficiency, we need to think deeper and avoid automatic categorization.

Next, if we examine an existing aid strategy in its three aspects described in Section 7-2-5 — (i) prevention/mitigation of fears (threats and risks), (ii) coping with human security crises when they occur, and (iii) promotion of medium- and long-term abilities to cope with risks — the concept of human security will be more deeply incorporated into the strategy. The following cases are based on these three aspects.

Case 1. As a result of reviewing the issues of Country E from the perspective of human security, JICA decided to incorporate into the country assistance strategy (i) assistance for ethnic minorities that have enormous social and economic problems and do not receive timely care from the government (narrowing the target of promotion); (ii) assistance to improve the safety of citizens because organized violence is rampant and the activities of citizens are severely affected; and (iii) assistance to cope with typhoons that cause tremendous physical damages and human suffering every year (prevention and coping).

Case 2. Country M is an underdeveloped country where a 30-year civil war ended 10 years ago but its scars are still visible and a high incidence of HIV/AIDS is a problem. JICA's country assistance strategy incorporates (i) efforts to promote peace building such as education for conflict prevention, coping with land mines, and revitalizing and improving the mass media; (ii) coping with HIV/AIDS (prevention and coping); and (iii) improving the job situation for the poor through the development of small enterprises (promotion).

Case 3. The priority in Country G has always been assistance for math and science education. From the perspective of human security, the revised priority now reads “math and science education that is sensitive to the weak” and incorporates measures to help the weak and the handicapped, including hearing-impaired children.

(2) Practical application level (program/project level)

This section discusses a review at the level of actual aid approaches such as programs and projects. It specifically looks at projects in the planning stage or those being implemented from the perspective of human security. The

review should focus on people and check whether the project (i) works with the community to empower people and with the government to ensure the sustainability and dissemination of aid impacts (improving vertical relations); (ii) maintains close collaboration with the government, NGOs, private companies, and other donors (improving horizontal relations); and (iii) pays sufficient attention to the vulnerable.

JICA has come up with seven principles of human security to actually incorporate the concept when formulating and implementing its projects and programs:

- (i) Reaching those in need through a people-centered approach
- (ii) Focusing on the most vulnerable people whose survival, livelihood, and dignity are at risk
- (iii) Empowering people as ‘actors of development’ as well as protecting them as recipients of aid
- (iv) Comprehensively addressing both ‘freedom from deficiency’ and ‘freedom from fear’
- (v) Responding to people’s risks (threats) by assessing and addressing threats through flexible and inter-sectoral approaches
- (vi) Working with both central government and local communities to achieve sustainable development of the country and local society
- (vii) Strengthening partnerships with various actors in developing countries, including other donors and NGOs to achieve a higher impact from assistance

7-4-2 JICA’s action on human security

The first Phase of the JICA Reform Plan, announced in March 2004, lists human security as one of the three key elements of JICA’s reform, along with “field-based management” and “effectiveness, efficiency and speed.” With this in mind, JICA is taking four actions on human security.

(1) Incorporating human security in JICA’s country and regional aid policies

JICA analyzes key issues related to human security at the national and regional levels in order to incorporate the concept into its Country assistance plans and other implementation policies.

(2) Incorporating human security in projects and programs

Under implementation policies at the national and regional levels and based

on the seven principles described above, JICA explores ways to put human security into practice in its programs and projects. Good practices in terms of human security are discussed and shared within the entire organization.

(3) Improving development instruments and implementation procedures

JICA is addressing a number of issues including (i) speeding up the project/program cycle of planning, design, and implementation; (ii) assessing social, political, and economic conditions surrounding individuals and communities, including their vulnerability; and (iii) implementing, monitoring, and evaluating projects and programs in a flexible, tailored manner based on the conditions of individuals and communities.

(4) Mainstreaming the concept of human security

JICA is proactively exchanging views on how best to put human security into practice, not only within JICA, but also with its partners, including developing country governments, other donors, NGOs, consultants, and scholars. Progress has already been made in developing partnerships with other donors including projects of the UN Trust Fund for Human Security and the social development strategies and programs of the World Bank.

7-4-3 Effects on JICA of adopting the human security concept and remaining issues

(1) Effects on JICA

More than two years after JICA announced its commitment to practicing the concept of human security, what changes have taken place in JICA? Adoption of the concept is certainly causing both tangible and intangible changes, including these examples:

- (i) Mainstreaming of locally-initiated projects led by overseas offices (Timely and tailored responses to local needs. According to estimates, start-up time and costs for some projects were substantially reduced.).
- (ii) JICA is taking risks and providing assistance to countries affected by conflicts (Sudan, Gaza, Sri Lanka).
- (iii) Both communities and governments are involved in more projects.
- (iv) Active involvement with natural disasters and infectious diseases (tsunami, earthquake, influenza).

- (v) JICA has become more sensitive to vulnerable people and regions.
- (vi) Human security is reflected in Country or Regional Plans (mentioned as a basic country policy or priority area).
- (vii) More projects based on the concept of human security are being formulated.
- (viii) Progress in institutional reforms (speeding up the process of peace-building and disaster relief, including the 'fast-track' system).
- (ix) Building common ground (values) with other actors including NGOs.
- (x) JICA is now able to better express its ideas to other donors (strategic communication).
- (xi) Progress in specific collaborations with international organizations and other donors (the UN Trust Fund for Human Security, World Bank, UNDP, etc.)

(2) Remaining issues in practicing human security

JICA understands the concept of human security, has identified effective approaches, and has begun to incorporate them in its projects and programs. We are now beginning to see the results. To enhance this practice in the future, JICA needs to address following issues, among others:

- (i) Win the understanding of more people and organizations.
- (ii) Improve approaches and methods.
- (iii) Produce more sophisticated analyses (measure social vulnerability, downside risks, etc).
- (iv) Review evaluation and monitoring methods.
- (v) Collaborate more with actors in non-aid sectors (emigration, trade, etc.)

7-5. Case studies

7-5-1 Bolivia — Good practice in the pursuit of human security

(1) Background

Half a century after the 1952 revolution, Bolivia is again at an important turning point socially, economically, and politically. While various reforms have improved some social development indices such as infant and child mortality rates, the income level remains low, ethnic inequality and income gaps are widening, and social discontent is growing against a background of a long

period of economic stagnation and issues around the indigenous people.

The social discontent has caused repeated acts of social unrest such as roadblocks and riots, protesting government policies such as the privatization of public corporations, a ban on coca cultivation, and changes in the natural gas development laws. Against this background, Evo Morales, the representative of coca-growing farmers and leader of the Movement for Socialism Party, was elected in December 2005 as the first president of Bolivia from an indigenous group.

As one of the poorest countries in Latin America, Bolivia is considered to be an important aid recipient by many donors who are keen to coordinate their activities. Considering the serious poverty, a community of Japanese emigrants and their descendants, and Bolivia's traditional affinity to Japan, the Japanese government has been providing substantial aid to the country.

(2) JICA's action

In Bolivia the concept of human security has not only become the basic principle of Japanese government aid but also one of the pillars of the country's draft national development strategy. This is extremely noteworthy and probably the first in the world. The fact that human security is systematically reflected — from aid strategy to projects in the field — should be highly praised as a best practice in the pursuit of human security.

This move originated with JICA's 2004 study, "Country Study for Japan's Official Development Assistance to the Republic of Bolivia." The study team looked extensively at human security as a core concept, and their presentation at a local workshop had a tremendous impact on government officials. Subsequently, active encouragement by the Japanese convinced the Bolivian government to draft a new national development strategy in which human security is positioned as one of its core principles. The new strategy was announced by then-President Mesa in May 2005. The government, which had been suffering from serious problems of social unrest that stemmed from issues of indigenous people, felt an affinity for the concept of human security that focuses on downside risks and systematically addresses the issues of both fears and deficiency (poverty).

In an economic cooperation policy consultation meeting in August 2005, the government of Bolivia, the Embassy of Japan, and JICA agreed to try achieving the MDGs through aid based on human security. This agreement positions human security as an overriding vision, and identifies "social development," "support for productivity improvement," and "support for institu-

tions and governance” as three aid priorities. Under this aid strategy, various projects that strongly reflect the concept of human security are being planned and implemented. One example is the Support for Achacachi Rural Development project, which focuses on the indigenous people who suffer from long-standing discrimination and poverty, and aims to promote development with initiatives from the residents. Other examples include the Water Is Vital project that aims to empower communities by supplying drinking water to poor areas, and assistance for development of small- and medium-sized enterprises that lead to increased employment and economic stability.

Also, JICA has agreed to collaborate on the dissemination and realization of human security and signed a Minutes of Understanding with the World Bank Bolivia Office. JICA is actively pursuing coordination with other donors and international organizations (UNDP, UNICEF, etc.).

Thus, in Bolivia, JICA is working with the government and other donors to promote the realization of human security systematically, from the macro level of policies to the micro level of projects.

7-5-2 Myanmar — Project to eradicate opium poppy cultivation and reduce poverty in Kokang Special Region³

(1) Background

The Kokang Special Region in Myanmar is located on the border with China where the Chinese language and culture are dominant and even renminbi yuan are circulated. The region is inhabited by ethnic minorities, primarily the Kokang people. More than 100 years ago poppy cultivation was brought to this area, which has been known as part of the Golden Triangle since then. Due to environmental conditions such as precipitous terrain, cold climate, lean soil, and lack of water, the area is not suitable for production of any agricultural products other than poppies, and there are no distinguishing industries. Armed ethnic minority groups in the Kokang Special Region were in conflict with the government of Myanmar until the peace agreement of 1989, so the basic social infrastructure and public services such as education and healthcare were not well developed.

Under such circumstances, 130,000 farmers depended on poppy cultivation for their livelihood. However, in 2003 when the Special Region decided to ban poppy cultivation that had accounted for 70 percent of farmer income,

3. Quoted from JICA's website

these farmers suddenly lost their means to earn cash. The rapidly deteriorating economic conditions put the livelihoods of poor farmers in turmoil. In addition to a serious food shortage, malaria broke out in 2003, affecting more than 4,000 people, of whom more than 270 died, leading to the closure of one-third of the primary schools. This was a serious threat to human security.

(2) JICA's action

The response was a project that targets farmers who suddenly fell into extreme poverty and provides assistance to help them find a way out of life-threatening situations in the areas of agriculture, health and medical care, improved livelihood, and education. Particularly at the initial stage, the focus was placed on emergency assistance to directly alleviate poverty, such as supplying seeds and fertilizer and distributing mosquito nets soaked in insecticide. JICA also promotes human resource development and livelihood improvement from the mid- and long-term perspectives.

Moreover, as part of efforts to address the global issue of illicit drugs, JICA will seek ways to spur regional development after eradication of opium poppy cultivation while fostering mutual trust between the central government and the Special Region, which once had a hostile relationship.

(3) Viewpoint of human security

Emergency assistance to respond to critical conditions (downside risk) after termination of poppy cultivation became the entry point. JICA is also addressing structural issues of the Special Region through activities in various sectors with the involvement of both the central government and the Special Region, and with a focus on communities.

7-5-3 Afghanistan — project on women's economic empowerment in Balkh, Bamiyan, and Kandahar provinces⁴

(1) Background

After the Taliban regime took power in 1996, cruel constraints were imposed on Afghan women. They were deprived of freedom of speech and movement, and had to wear burqua, which covered them from head to toe. In addition, there were educational and employment constraints.

Even today, it is difficult for women to find employment as men do, and

4. Quoted from JICA's website

those who lost their husbands in internal conflicts or are very poor continue to have few opportunities to acquire the means to sustain their livelihood. After the establishment of the interim government headed by Hamid Karzai, the Ministry of Women's Affairs was created to reclaim women's rights and upgrade the status of women.

(2) JICA's action

Immediately after the creation of the Ministry, JICA supported capacity development of its officers and organizations and policy formulation. In 2005, a new project focusing on economic empowerment of poor rural women was launched. The purpose of this project is to bring the opinions of women in rural areas to the Ministry of Women's Affairs through the provincial women's bureaus (regional offices of the Ministry) so that the Ministry can submit proposals to other ministries and organizations for policies and measures that meet the needs of women.

To that end, in addition to strengthening the capacity of the Ministry to formulate and implement economic policies, small-scale model projects aimed at the economic empowerment of women in Balkh, Bamiyan, and Kandahar provinces are being implemented in cooperation with the provincial women's bureaus, as well as local and international NGOs. The provincial women's bureaus are able to understand the needs of rural women more effectively through the monitoring process of these model projects.

There are wide varieties of model projects — skills training for handicrafts, kitchen gardens, livestock husbandry and food processing, vocational training incorporating literacy education, support for training of women's groups, and information sharing on education, healthcare, law, and economy.

Workshops will help provincial women's bureaus understand current situations and challenges of economic activities for rural women through these model projects, and can share information and lessons learned with the Ministry of Women's Affairs and other provincial women's bureaus.

(3) Viewpoint of human security

JICA is taking a direct approach to women who will play a leading role in future development, focusing on poor rural women who are in socially disadvantaged positions, in cooperation with NGOs and other actors. JICA is supporting capacity development of the local and central governments to operationalize policies that lead to women's empowerment.

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The Private Sector and Development

A Review of the Development Role of Developed Country Private Enterprise

Mizuho Kuga¹, Keitaro Aoyagi², Takamasa Akiyama³

8-1. Introduction

8-1-1 Why international development needs the private sector

There has been mounting concern within the development assistance community about how to increase both the quantity of development funding and the quantity of assistance. The search for additional sources of quality effort has drawn attention to the private sector and to the development potential of its activities.

At the Monterrey Mexico Financing for Development (FfD) Conference (2002), an aid funding increase in the amount of \$50 billion was calculated to be necessary for attainment of the Millennium Development Goals (MDGs). Major donors, such as the U.K., responded to this by pledging dramatic increases in their ODA volume. But when the necessary underlying infrastructure is factored in, it is doubtful that official assistance from donor countries can realistically provide sufficient money. There is a growing recognition that private sources should be mobilized. And the resources are there. According to Organization for Economic Cooperation and Development (OECD) data, enormous amounts of private money already are flowing into developing countries, to the degree that money from the private sector now surpasses official funds (e.g., ODA), accounting for almost 90% of the total flow in 2004.

At the same time that the development community has been searching

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for additional financial resources, there has been heated debate on how to improve aid quality. One way is through increased aid efficiency; that is, reducing waste and duplication by harmonizing and aligning to deliver expanded services to the poor more consistently. To this end, assistance methodologies are being sought that will incorporate the private enterprise and transmit its qualities of financial strength, technical expertise, and management skills.

For these two reasons — quantity of financial resources and quality of economic know-how, integrating the private sector into development-related programs has become a pressing concern.

This Chapter describes the role in development that can be played by donor country private sectors. It explores two types of private sector activities — government-related activity and independent private activity — to understand how best to encourage the implementation of development-friendly projects by private enterprise. Particular attention is given to a mechanism known as PPP — public-private-partnership.

A presentation of the broad context in Section 1 is followed by more detailed analysis and explanation of the concepts and their implications in Section 2. After this comes a fuller discussion of PPP in Section 3. This includes thoughts on how it might intersect with FDI (foreign direct investment), how it is currently being used in development assistance. Section 3 also discusses PPP in Japan. Finally, Section 4 broadly analyzes the material and more narrowly summarizes the implications for PPP in the Japanese government's ODA strategy.

8-1-2 Flow of foreign capital into developing countries

The importance of private funds is undeniable, particularly when there are insufficient development funds. Figure 8-1 shows the transition of the net official and private fund flows into developing countries, as noted above, private funding being considerably greater than official funding. Until the 1980s, official funds from developed country governments or international institutions constituted a large share of capital flows. However, in the early 90s, the absolute amount of private funds increased dramatically so that in 2004, official funds accounted for only 11.8% of all capital inflows, and private ones accounted for almost 90% (see Figure 8-2).

As seen in Figure 8-1, this surge in private funds is largely attributable to increased FDI. While the FDI inflow is considerable, the amount from private nonprofit organizations also is non-negligible. The role of FDI and trade

Figure 8-1. Net flow into developing countries

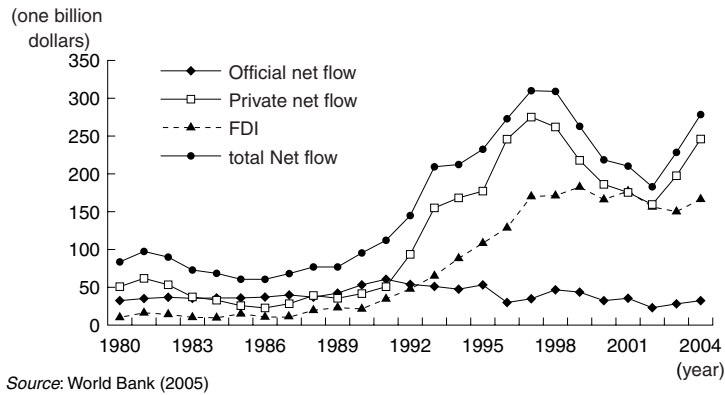
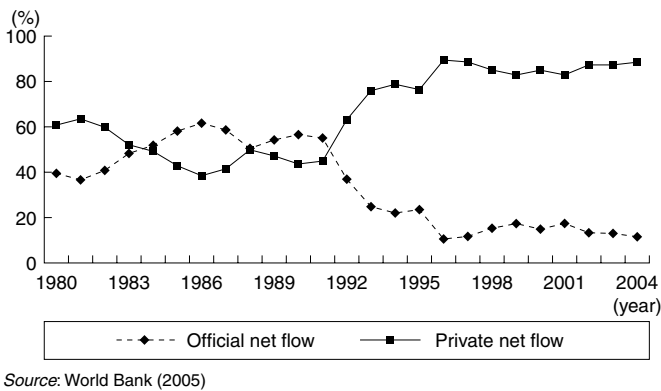


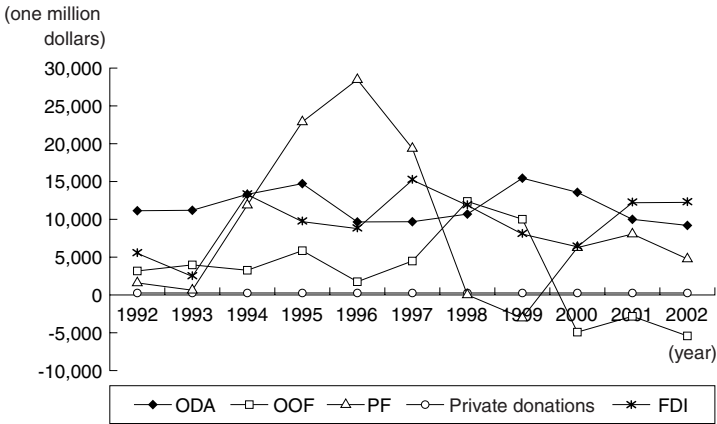
Figure 8-2. Net flow into developing countries



is important, not only for their funding volume, but also because they have significant impact on the development of poor countries regardless of private enterprise intent.

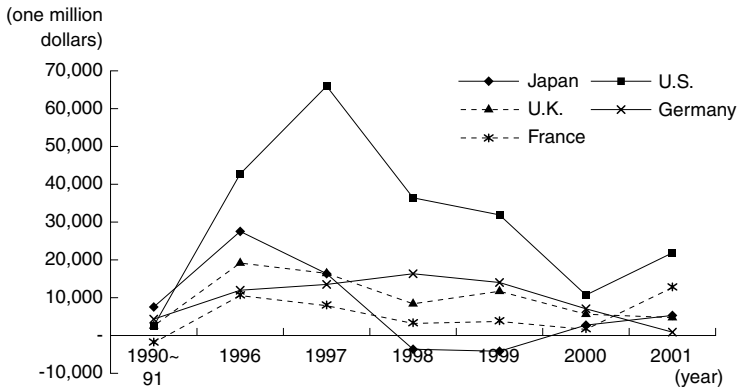
The inflow of Japanese private funds compared to other developed nations is small and stagnating, contrary to the total ODA amount (see Figure 8-4). Private funds from Japan were on the increase until 1997 but have been on the decline since the Asian economic crisis of that year (see Figure 8-3). Contributions from nonprofit foundations remain at a lower level and bilateral securities investment has decreased. Japanese FDI, however, has been continuing steadily, which matches the trend of other developed nations.

Figure 8-3. Fund inflow breakdown from JAPAN into developing countries



Source: JBIC institute

Figure 8-4. Private funds to developing countries and international organizations



Source: JBIC institute

8-1-3 Background and concepts

The private sector under discussion here is that of developed countries, not developing ones. This is not to suggest that the private sectors of developing countries are not vitally important. They are, and that importance is emphasized by the Private Sector Development (PSD) programs of the World Bank involving donors and NGOs. But their role, which will be touched on below in relation to the World Bank, is tangential to the main topic of this chapter.

By its nature, the private sector is not monolithic so that with respect to development impact, a number of distinctions can be discerned about it and

Table 8-1. Involvements of private enterprises into the developments

Development expectations for private enterprises	Incentive for private enterprise to be involved in development	
	Profitoriented motivation	Unprofitoriented motivation
Volume of fund	① FDI	② Donation through corporate foundation
Technique · know-how	③ BOP business	④ Development-related activities such as poverty redaction through the establishment of CSR

its motivations. The broadest distinction is between government-related private sector involvement and non-government-related private sector involvement. Government-related private sector involvement commonly takes the form of “public-private partnership,” or PPP.

Four types of independent, non-government-related private sector involvement are considered in this chapter, all of which can impact on the development process. They are foreign direct investment (FDI), corporate social responsibility (CSR), bottom-of-the-pyramid (BOP), and donation/grant. These four can be cross-categorized into four patterns based on motive (two motive categories) and content (two content categories). The motive categories are 1) profit-making and 2) other-than-profit-making; the content categories are 1) money and 2) technology/expertise. The four possibilities yielded are shown in Table 8-1.

8-1-4 Government link: PPP and development

Companies will expand their overseas business even into poor countries of low level economic development if profitability seems feasible. Often, however, investment in developing countries and commercial pursuit carry so much uncertainty and high risk that business engagement will be deterred. Obstacles such as incomplete information, inadequate legal systems and infrastructure, and weak protection of intellectual property rights may be too daunting to face without strong support. Supportive mechanisms become necessary to insure against risk and create an investment climate sufficiently favorable that profit is not only considered possible, but also probable. PPP is such a mechanism.

Public and private enterprises have separate comparative advantages and roles to play in smoothing the way for development. There is, however, a potential for synergy between them that can be triggered by cooperation.

Governments can signal private enterprise to intensify commitment to development by compensating for risks or by creating attractive business opportunities. The private sector can respond to these inducements by restructuring business-driven projects to complement public ones. PPP embodies this synergy.

Profit motivation need not exclude business activity from contributing to positive development outcomes if it is pursued within a carefully designed system supporting development-friendly business activities. PPP is in place in developing countries and some Japanese projects use this mechanism.

Though the term is widely used, PPP does not have a universally accepted definition. The most general definition is government and private enterprise cooperatively engaged in development efforts. A more pedantic definition is “every involvement between the public and private sectors where all or part of traditional public sector activities are transferred to the private sector.” For the purposes of this Chapter, a working definition of PPP is from the Japanese Ministry of Economy, Trade and Industry (METI): “cooperative partnership where both public and private sectors share the purpose of realizing favorable public services”. This interpretation of PPP was manifested by the government of Junichiro Koizumi in its drive toward privatization of public services.

PPP was conceptualized in the 1990 in the wake of New Public Management (NPM) in U.K., following the Blair government’s administrative reforms. PPP has had significant influence on administrative efficiency in western countries and has been studied in Japan, including at METI since around 2001. A parallel move toward administrative reform in developed countries complemented a global trend toward PPP in development assistance, a field which traditionally was strictly limited to the public sector.

Among donors, the World Bank and the United States (USAID) were early adopters of the PPP concept. They introduced PPP initially to extend donor country PPP to private trade and technical assistance, whereby the government offers subsidies to provide the support system for private projects already planned. Eventually PPP came to involve all parties capable of engaging as service providers in development, not only private enterprise, but also NGOs, foundations, universities, etc.

One reason why PPP is not yet definitively defined is because there are several permutations and combinations involved: various combinations of developed country and developing country governments, and developed country and developing country private sectors. The focus here is on partner-

ship between the donor government and private enterprise in the donor country.

8-2. Private funding and developmental financing

There are four main categories of independent (non-government linked) private sector activities that affect the economic development of poor countries: FDI, CSR, BOP and donation/grant. Profit motives apply to FDI and BOP business; non-profit motives are applied to CSR and donation/grant. : the former is the purely economic pursuit of profit; and the latter incorporates also a purposeful contribution to development. The motivation of the first is the normal business goal of achieving a healthy bottom-line. The approach of the second is seen in business activities that are deliberately designed to have a social contribution and development component.

8-2-1 FDI

FDI by multinational companies of developed countries represents the largest source of private funding into developing countries. The importance of FDI is well documented in analyses of the economic growth of East and South East Asia. However, FDI is not a development tool and the primary purpose of FDI is not the development of target countries. Private firms invest in foreign countries, even poor countries, for cost reduction and profit maximization in the target company.

The East Asian situation clearly illustrates the contribution of direct investment to economic development. That region's high economic growth was almost certainly achieved by organically linking FDI and trade, which is often called the Japanese development model. The development of the private sector, along with ODA, activated the latent mutual dependence of investment and trade (Urata (2004)).

East Asian countries and South Asian countries have actively been inviting foreign direct investment since the late 80s and the early 90s due to the externalities carried. The following two externalities have been identified by economic theory. First, the high technology, knowledge, and management resources of developed countries have spill-over effects (technical externalities) on companies in developing countries. Second, the purchase by investing companies of intermediate materials from companies in developing countries leads to increased demand for industries (monetary externalities).

Direct investment helps to transfer the capital investment funds, tech-

nologies, and management skills severely lacking in most developing countries. Furthermore, countries receiving FDI can utilize the sales and procurement network of foreign companies, expanding trade (both imports and exports) to acquire foreign currency. This allows them to import technologies, intermediate materials (semi manufactures) and capital goods necessary for their economic development. The increase in exports attracts direct investment and further helps exports. It is this symbiotic, mutually dependent relationship between direct investment and trade that led to the economic development of the East Asian countries.

In addition to external effects, there is a considerable effect of job creation expected from greenfield investments. In Malaysia in the late 1980s, for example, the number of employees hired by foreign companies rose by 20% each year. However, this type of job creation effect is limited and in general a comprehensive effect has not been documented.

However, FDI can also have unfavorable consequences for target countries. Firstly, there is the issue of transfer pricing. It is possible to transfer earnings by rigging the transaction prices among affiliated companies and lowering the tax paid on site. This intentional price rigging often distorts international resource allocation. Secondly, when multinational companies do not offer much learning potential, direct investment may delay change in the dynamic comparative advantage, thereby worsening economic growth. Thirdly, increases in imports and capital repatriation can destabilize the balance of payments. Also, some countries fear that foreign companies might gain political control over their economy by driving out local firms.

8-2-2 CSR

Even while doing business, some companies also pursue activities that reinforce corporate social responsibility (CSR), demonstrating that doing business and making social contributions are not mutually exclusive. While their scale and impact is relatively small, such CSR activities can be positive for the development of poor countries and for the development assistance framework as a whole.

The CSR business activities discussed here are limited to those that acknowledge the support of developing countries as an objective. These business activities differ from activities by foundations whose financial contributions embody an aspect of development assistance as discussed in 8-2-4. CSR activities are intended to provide the poor with services with each project. CSR is likely to contribute to development at a more micro level than FDI.

It was not until in the 1990s that CSR drew international attention. CSR is characterized as a major structural change in corporate management. Previously, corporate social contributions meant the allocation back to society of some of the profit gained through business, arguably somewhat similar to assistance by foundations. However, the CSR which attracted attention in the 1990s is a new corporate strategy, a management shift to the attitude that in all business processes environmental and social aspect should be considered along with profitable ones. CSR strategies are aimed at 1) improving risk management, 2) enhancing brand value, 3) attracting quality employees, and 4) improving evaluation by the market.

CSR is a very broad concept, including such business activities as law compliance and consumer protection as well as development in poor countries. CSR began to be discussed in conjunction with development in the late 1990s. In 1998, World Bank President James D. Wolfensohn proposed a plan, Business Partnership for Development (BPD), with a British international NGO, the Prince of Wales International Business Leaders Forum. Soon after, at the 1990 World Economic Forum in Davos, U.N. Secretary-General Kofi Annan introduced a business principle called the Global Compact which was officially inaugurated in July, 2000. The Global Compact is aimed at spreading responsible corporate activities internationally while solving the problems caused by globalization.

An example of CSR by a western company is offered by the UK-based Cadbury Schweppes. Cadbury Schweppes took the international initiative of addressing child labor on cacao beans. It built a partnership with an NGO to promote cacao plantations in Ghana and to conduct a pilot business for eco-tourism. Another example is offered by TPG, an international transportation company in the Netherlands. Since December 2002 TPG has worked in cooperation with the World Food Programme (WFP) to apply its specialized skills in transportation and distribution to food assistance for African farms.

Some companies view their trade structure as a CSR activity and practice Fairtrade in cooperation with NGOs. Starbucks Coffee has a partnership with Conservation International, an international environment NGO with activities in over 30 countries. Starbucks Coffee is cooperatively developing high quality standards for buying coffee, taking into consideration environmental, social, and economic aspects, so that the coffee farmers at the top of the supply chain can produce high quality coffee consistently. Preferences, such as financial incentives and preferential purchases, also are provided to farmers meeting the standards. In addition, Starbucks Coffee is contributing to the

coffee farms by selling Fairtrade coffee in its outlets.

Some Japanese private enterprises have opened departments specializing in CSR and are engaged in overseas assistance. The Ajinomoto Group, for one example, set up the Ajinomoto international cooperation network on food and health in 1999 as a global activity on the principle of making social contributions in the fields of food, health and healthcare, mainly in South East Asia and South American countries. It works to clarify and solve the food problems that these countries have. In doing so, the Ajinomoto Group cooperates with NGOs, international organizations, official institutions, education and research institutions, local communities, etc. It has thus far completed 10 projects in the Philippines, Indonesia, Cambodia, and Peru, and in 2005 had six new projects underway.

In most cases, contributions by Japanese companies are made through donations which tend to be automatically channeled through business groups into well-known assistance organizations. Following a round of supportive assistance after the major 2004 earthquake off Sumatra, however, Japanese companies started to change their attitudes toward assistance. Not only do they now offer funds, but they have built supportive styles into their own businesses. For example, in 2006 the Sumitomo Group offered ¥40 million for school constructions and repairs in Africa, choosing World Vision Japan as the implementing organization. It is becoming more common to find an NGO that fits the need rather than as a means for making support more publicly evident.

8-2-3 Bottom-of-the-Pyramid (BOP)

The concept known as "bottom of the pyramid" (BOP) finds compatibility between profitability and poverty reduction by viewing poor people as consumers, that is, as business opportunities. It is a business pattern that considers the poor as clients. It is designed to strengthen poverty reduction while pursuing business profit. The interest of private enterprises, typified by multinational companies, in the markets of developing countries has generally been limited to newly emerging markets with a rising middle class. Profit motivated businesses generally do not touch the poverty issue. By contrast, BOP oriented businesses seek profits even while contributing to poverty reduction. Their strategy is to serve the poor profitably by treating poor people in poor countries — the biggest population in the world — as customers. The bottom of the pyramid referred to by the term BOP is, in fact, the poor who have been given this distinction because they are at the bottom of the

economic pile. Many of the companies in BOP businesses operate in cooperation with official institutions such as governments or international organizations. These can be categorized as PPP. However, in most cases, BOP companies conduct their business without official support.

Companies motivated by profit recognize the poor to be a new market but they need incentives to venture into that market. Two sources of incentive have been indicated in earlier business administration studies. The first is access to a market with the world's biggest population. The BOP market covers business activities of four billion people, two thirds of global population. If companies can attract these as customers and create acceptable business models, they will have access to a huge population and associated profit. The second incentive is acquisition of knowledge. By applying the knowledge gained in the BOP market elsewhere in developed or emerging markets, they can learn more about bringing innovations to conventional business styles.

The entry of private enterprise into the BOP market allows the poor access to a variety of goods and services that otherwise would be difficult to obtain. But in transforming the poor into consumers, more can be provided through market activity, for example, raising awareness of healthcare and sanitation, than can be provided simply by goods and services. Furthermore, with the active involvement of consumers themselves in business activities, a win-win relationship between companies and the poor can be built, making it possible to improve their standard of living. BOP demonstrates business know-how to developing private enterprises and consequently can contribute to fostering them.

8-2-4 Donations/grants

While they do not seem to be as significant as business sources, private foundations have enormous amounts of money at their disposal which they dispense as donations and grants. They are a major, if sometimes low-profile, source of money for development, especially in the United States. According to OECD data, funds from that source account for 1.5% of U.S. development assistance.

As of 2003, there were 66,398 private grant-making foundations in the United States, with total assets amounting to as much as \$476.7 billion and annual assistance funds amounting to \$30.3 billion. One of the most prominent is the Bill & Melinda Gates Foundation, founded in 2000. The amount of its assistance is approximately \$1.2 billion, currently ranked first in the world

Table 8-2. Breakdown of development finance in the U.S.

	US\$ (one billion dollars)	Percentage (%)
ODA	9.9	18
Other official funds	12.7	22
Private funds	33.6	60
Foundations	1.5	
Enterprises	2.8	
Private and voluntary organizations (PVOs)*	6.6	
Universities	1.3	
Religious organizations	3.4	
Individual remittance	18.0	
Total	56.2	100

Source: USAID (2003)

* In U.S., NGO is usually called as PVO.

in annual private foundation assistance. The Gates Foundation puts particular emphasis and spends large amounts of money on assistance to healthcare and sanitation projects, closely related to poor country development. In 2005 it donated \$750 million (60% of all funds) to support the activities of the Global Alliance for Vaccines and Immunization (GAVI).

The American social climate in support of developing countries has been favorable, with a contribution culture based on religious values, and a social system that promotes the involvement of private enterprises by establishing preferential taxation. As can be seen in Table 8-2, private funds in the U.S. are sponsored by a variety of organizations — foundations and private enterprises, private and voluntary organizations (PVOs), higher educational organizations (e.g., universities), religious organizations, etc.

Data for Japan in the OECD category of contributions by private nonprofit organizations show a leveling-off over the past ten years at around \$200 million per year. In the United States, on the other hand, as of 2001 such contributions reached as much as \$4.5 billion.

There is a huge gap in private grant-making foundations between the U.S. and Japan. According to the Japan Foundation Center, as of 2004 there were 1,105 such groups in Japan with total assets of some ¥1.5 trillion and project expenses of about ¥49.5 billion. Of these, only 98 are groups with international programs. Foundations with a focus on international cooperation do exist, such as the Sasakawa Peace Foundation, but the contribution of international programs is relatively small in terms of funds flow.

8-2-5 Section summary

Thus far, patterns have been reviewed where companies engage in development. As explained, there are two types of motivation: profit motivation and nonprofit motivation. It is clear that the companies play an indispensable role in the development of poor countries whether for profit or not. Contributions through FDI and by foundations are important in terms of their scale. FDI especially has role in the developments of target countries for jobs creation, export expansion and acquisition of foreign currency. Attention to CSR has come not only in western countries but also in Japan. Methods for contributing to development have been shifting from simple donation to practical projects in cooperation with NGOs which are more tailored to development support. BOP business that facilitates development is effective as a starting point and can be expected to contribute to poverty reduction, although only a few such examples can yet be seen.

These corporate activities may vary depending on the nature of the business involved. It is important, however, to connect these corporate patterns with effectiveness in developing countries. One way to draw more private enterprises into development is PPP. As its name suggests, public (i.e. government) private (i.e., business) partnership (i.e., collaborating) is a logical mechanism for magnifying the positive effects of each.

8-3. Role of PPP

One characteristic of FDI is that it tends to focus on only a few countries. Figure 8-5 shows the regional breakdown of countries receiving foreign direct investment. Private funds tend to flow into developing countries that are expected to have high growth. They flow little into African countries, which continue to depend on official funds. To further increase investment and trade, the environment of private business activities should be improved, but efforts in this area have been limited. One way to address this problem might be to utilize ODA to mobilize private funds in developing countries and to support the business activities of advanced private enterprises in regions that lack satisfactory investment environments; in effect, PPP. In this regard, the idea that PPP should be strengthened is being well received.

Figure 8-6 shows a diagram of the relationship between public projects (with official funds) and private ones. The horizontal axis represents the source of funds; the vertical axis represents the commercialism of the project. Low value commercial projects are located in the ODA field covered by

Figure 8-5. Regional breakdown of foreign direct Investment recipient countries

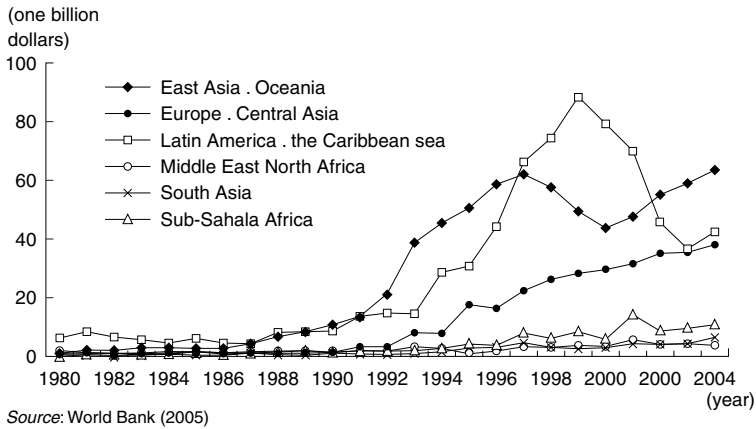
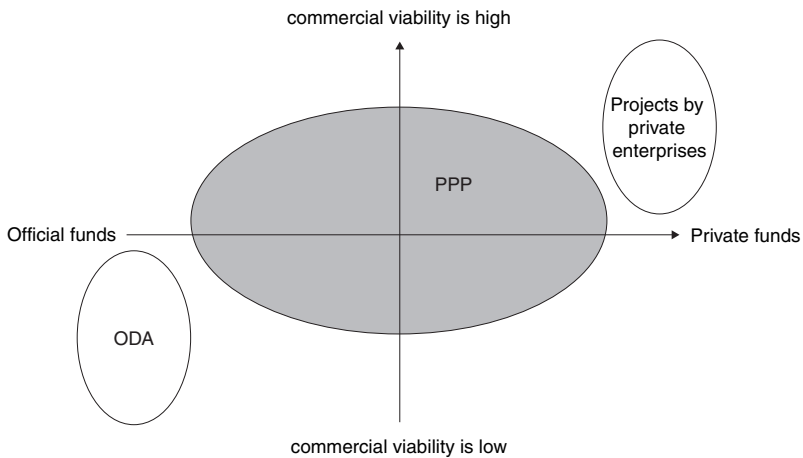


Figure 8-6. Image of PPP



official funds whereas high value commercial projects are in the private enterprise field. The activity field located in the middle between ODA and private projects is noteworthy because it allows private enterprise to function if the public and private sectors cooperate. The PPP approaches of the World Bank, USAID and Japan below show some of the variations being used.

8-3-1 World Bank approach

(1) *Business Partnership for Development*

To improve the efficiency of development funds, the World Bank works with

private enterprises under the framework of Business Partnership for Development (BPD). BPD is thought to be a turning point to promote CSR, as mentioned in 8-2-2, but it also has an aspect of promoting partnership. To further development assistance, BPD projects regard three parties, private firms, governments, and NGOs, as World Bank partners in implementing cooperative programs. With the tri-sector partnership, the BPD aims to maximize both the profit of each party and the developmental effect, bringing such advantages as cost reduction and new markets while promoting CSR. BPD projects also bring momentum and financial merits to NGO activities. It allows bilateral donors and multinational developmental institutions to cooperate with NGOs in understanding the needs of local parties and to benefit from private funds as new assistance money. BPD projects, – often in 1) natural resources (oil, gas, and mining companies), 2) water and sanitation, 3) human resource development, and 4) traffic safety – have been conducted by 30 partnerships with 120 organizations in 20 countries between 1998 and 2001, using the Development Grant Facility.

World Bank BOP projects attempt to give private enterprise the responsibility for development, involving all its staff and making full use of its strengths (i.e., expertise and funds). This method was created by a British NGO and by World Bank President James Wolfensohn so that it contributes to the spreading of CSR. For this reason, BOP projects often adhere to the concept of corporate responsibilities at the expense of profitability.

(2) Private sector development strategy

In 2002, the private sector development (PSD) strategy was introduced to realize poverty reduction while taking advantage of private funds. The private sector is typically considered to be a service provider for the poor. PSD focuses on two points — improvement of fundamental service access for the poor and improvement of investment environments.

① The improvement of fundamental service access for the poor
In the past, the role of the private sector was the production and delivery of goods and/or services. PSD changes this by extending the role of its business activities to the final outcome. It is seldom economically feasible to provide the poor with basic services. However, if the associated deficits are borne by development fund subsidies, then private enterprise participation can be promoted. Subsidies are paid only when the result of the project has been satisfactorily confirmed, that is, when service has reached the end user (e.g., teachers at work in schools; public phones connected; water flowing

from taps). With this private sector perspective, PSD allows companies to draw highly efficient road maps that insure accountability because the subsidy funds are disbursed only when output has been confirmed, and this can be factored into the plans from the design stage.

② **The improvement of the investment environment**

Another important focus of the PSD strategy is to diagnose and evaluate the investment environment properly so as to promote direct investment into developing countries. There are two ways to diagnose: one is "Doing Business," the other is "Investment Climate Assessment." The World Bank's "Doing Business" ranks 155 countries around the world with respect to rules and reforms related to business climate indicators such as companies, employment/unemployment, contracts, taxes, and registration of capital. "Investment Climate Assessment" was discussed in World Development Report 2005, "A Better Investment Climate for Everyone.: That report presents results from a survey of 26,000 companies in 53 countries and offers valuable information not only for development professionals but also for the general business person. The World Bank recognizes the key role that private enterprise plays in the pursuit of growth and poverty reduction. It also recognizes that earlier reform regarding investment climate has not borne fruit. Applying objective analysis, it proposes concrete measures to improve the situation.

The World Bank only recently began to emphasize improved investment climate in developing countries. It may be correct to say that discussion of PPP is being shifted away from partnership on projects toward investment climate improvement.

(3) Security function and political risks

Since the World Bank now focuses on investment climate, the risk guarantee concerning World Bank investment will be touched upon. The most serious risk hindering private investment in developing countries is related to government policies, including inconsistent policies and unstable macro-economic conditions. With the call for improved investment climate, the importance of guarantees against these political risks is increasingly being recognized. The Multilateral Investment Guarantee Agency (MIGA), part of the World Bank Group, guarantees against political risks associated with direct investment in developing countries. Even business people who fulfill their contractual responsibilities may be unable to cope with accidents, natural disasters, government confiscation, infringements of rights, insurrections,

Table 8-3. The World Bank group aid scheme for private sectors

1	Investment guarantee to private investors, finance for project enterprises	IBRD / IDA : Finance the developing country government and strengthen its guarantee capability. The government guarantees investors indirectly through the payment guarantee to the third party guarantee organization. IFC : Finance 5 to 15% of issued stocks.
2	Debt guarantee to bank loans, syndicate loan to project enterprises	IBRD / IDA : Support the guarantee business of GuarantCo through the contributions to PIDG trust fund. IFC : Lending the project loan not exceeding 25% of the total costs. form two-step loan to financial mediators, and Syndicate loan by private banks.
3	Funding assistance to advisory services of private procurement	IFC : Give necessary advice to project formulation or project restructure. Give grant aid for feasibility study by private enterprises through the project development facility.
4	Political risk guarantee	MIGA : Give political (non-commercial) risk guarantee directly to investors.

Source: IFIC in JICA (2005)

riots, acts of terrors, or civil disturbances. Unanticipated political risks make it difficult to stipulate responsibility for losses contingent on the risks associated with contracts between private enterprises in developed countries and governments in developing countries. They also are likely to inhibit the progress of FDI itself. MIGA compensates directly losses caused by such events. Other organizations in the World Bank Group, such as IFC, have other schemes but it is MIGA which provides insurance against political risks (Table 8 – 3).

8-3-2 USAID Approaches

In the United States, the government has designed a system that supports active involvement by private enterprise in development. This is an advanced example of PPP assistance where effective developmental support associated with private funds is needed.

In the US the involvement of private enterprise in development assistance is relatively high. Official funds account for 40% of all assistance from the U.S. while private funds accounts for 60%. Private funds come from foundations, PVOs, religious groups, and universities. With this magnitude of private enterprise involvement, USAID has been promoting partnerships with private enterprise. In the U.S., the form of PPP used is referred to as Public-Private Alliance (PPA), “a new business model of USAID in the 21st century.” PPA aims to address development problems beyond the scope of USAID by integrating through alliances of more than two parties. PPA’s main character-

istics are 1) shared developmental problems that cannot be solved individually, 2) sharing resources, risks, and outcomes for a common purpose or problem, 3) comparative preferences of each party, and 4) promotion of private enterprises involvement in assistance with both funds and materials.

In 2001, the Global Development Alliance (GDA) was founded as a department under the direct control of the Administrator to control USAID PPA strategies. GDA's role is to find partners and to be sure that they clearly understand USAID policies. Partners submit proposals, called Annual Program Statement (APS). A main role of USAID is to manage the GDA Incentive Fund, a foundation used as seed money to encourage PPA projects and promote relationships with private enterprise. USAID also carries out evaluations of the partner candidates, ranks supporting programs, and monitors project reports and surveys.

PPA builds a variety of partnerships, including with foundations, NGOs, governments, research institutes and private enterprise in developed and developing countries. As of 2004, 290 PPAs had been concluded with 339 companies and 89 foundations, and the number is increasing annually. The amount of money supplied to GDA also is increasing. The amount of private funds supplied to the program is larger than that supplied by USAID itself. In 2002 more than \$1 billion out of \$1.2 billion was from the private sector and in 2003 more than \$1.2 billion out of \$1.5 billion came from that source. PPA projects cover a range of sectors: education, healthcare, environment, occupational training for young people, information technology, small- and medium-size business development among others, and many of them targeted at African countries.

The GDA approach is conceptually similar to the Development Partnership pursued by the World Bank in the sense that it focuses on the importance of involving various staff and typically focuses on visible outcomes for individual sectors.

8-3-3 Partnership example — the GAVI case

The Global Alliance for Vaccines and Immunization (GAVI), which notably includes the United Nations and the Bill & Melinda Gates Foundation, is the representative case of PPA under USAID. The GAVI initiative began in 2000 to tackle the problem that more than two million unimmunized people die annually in poor countries from diseases for which immunizations are available. GAVI has worked to improve the intake rate of fundamental vaccines, promote the introduction of new vaccines, and strengthen the vaccine distrib-

Table 8-4. Breakdown of GAVI funds (as of March, 2005)

	(one million dollars)	
	Disbursement	Pledged amount
Canada	12.67	149.44
Denmark	4.49	0
France	6.03	12.06
Ireland	1.78	0
Netherlands	71.26	17.33
Norway	101.94	282
Sweden	12.52	14
EU	1.26	17.28
Luxembourg	0.61	0
U.K.	50.78	13.58
U.S.	218.73	64.48
Donor governments sub total	482.07	570.17
Bill&Melinda Gates Foundation	758.5	750
Other privates	4.23	0
total	1244.8	1320.17

Source: GAVI Website

ution system in the poorest 72 countries, thereby saving 670,000 infants born between 2001 and 2003.

GAVI partners include the international organization (United Nations, UNICEF, WHO, World Bank), foundations (Bill & Melinda Gates Foundation), NGOs (International Pediatric Association: IPA), vaccine makers (Merck Vaccines and Bio-Manguinhos/Fiocruz), developing country governments (Benin, Cambodia, Ghana, Bangladesh), technology and health-care institutes (Health Canada), research institutes (University of Gothenburg in Sweden), and developed country governments. The breakdown of these funds is seen in Table 8-4. As can be seen, the amount from the Gates Foundation is the largest, surpassing those of developed countries.

8-3-4 PPP in Japan

As noted above, in Japanese PPP refers to the partnership between the Japanese government and Japanese private enterprise. The Japanese version of PPP has three notable characteristics. First, it has been oriented toward building an environment that allows the development effect of private enterprise to flourish by encouraging FDI endeavors by Japanese companies in the economies of developing countries. Second, it creates commercialism while intervening in the market to induce the development impact of private sector involvement. In this, it differs from the western PPP approach of con-

necting governments with existing private business activities. Third, PPP projects are centered on the construction of infrastructure demanded in developing countries. The Japanese government might subsidize or compensate private companies to enter public projects previously financed by ODA. One reason that such infrastructure projects receive attention is that METI, responsible for infrastructure projects, has taken initiative in PPP.

(1) Characteristic of PPP in Japan

METI and JICA have released their respective research reports on PPP. Both reports discuss how to promote PPP in Asia. The METI report summarizes September 2004 discussions by the PPP study group of the Trade and Economic Cooperation Bureau. It examines PPP with respect to the development of infrastructures and under the assumption that Japanese companies will participate in the projects. Analysis in the JICA report ranges from infrastructure to education and healthcare sectors.

(2) From Japanese version PPP to Asian version PPP

As a preliminary step in its discussion of development assistance and PPP, METI has been working toward a Japanese version of PPP, pursuing the privatization of public services to induce new service industries that would ease financial deficits, improve the quality of public services, reduce costs and create new jobs. In Asian countries there is a high demand for improvements in infrastructure and administrative services. METI addressed the problem of how to build a system that could make infrastructure building and maintenance more efficient in Asian nations by promoting PPP across Asian countries. As the best means of dealing with these issues, METI proposes that the Japanese government and companies work on them cooperatively. Specifically, the government would convert areas where a lack of commercial interest discourages private enterprise into ones which offer acceptable commercial return thereby encouraging the establishment of private businesses searching for profit.

PPP as proposed by METI pursues efficient assistance through the entry of private enterprise. It does not entail blurring the line between the government and private companies, but it concretely specifies collaboration among four parties: the Japanese government, Asian governments, Asian private enterprise, and Japanese private enterprise. The aim is to realize efficient service through increased competitiveness resulting both from administrative efficiency reform at the government level and management efficiency reform

Table 8-5. Japan's PPP cases (designed public & managed by private)

		Main construction	O&M
Port and harbor	Laem Chahang Port (Thai land)	loan	Marubeni-Kamigumi, NYK
	Colombo Port (SriLanka)	loan	P&O
	Constanta Port (Romania)	loan	Dubai Ports Authority
Railway	Bangkok Subway	loan	Thai leading civil engineering company accepted the siemens participated in the vehicle system
Water	Manila Water (Philipeans)	loan	Ayala (Philipean local company) Mitsubishi Corporation
Airport	Beijing Capital International Airport (China)	loan Chinese enterprices	Paris Airport Authority
	Viru-Viru Airport Terminal (Bolivia)	loan	U.S. AGI

Source: METI (2005a)

at the level of the firm. There is basic recognition behind this promotion of PPP in Asia that Japan will be strongly involved in the export of Japanese brands and Japanese infrastructural services. There is no question that Japanese economic assistance, focusing on infrastructure, has a role in the activation of private production, trade, and investment.

(3) PPP cases

Generally PPP is active in such areas as ports, trains, water systems and airports, which private enterprise cannot afford to develop as public projects but where private enterprise is involved in operations and maintenance (O & M) (Table 8 -5). However, PPP also covers some administrative service information technology (IT) fields, such as electric procurement systems, wireless internet protocol (IP) phone systems, and electronic passports.

8-3-5 Issues in introducing of PPP in Japan

It is important to promote PPP in Japan expeditiously but there are three related issues: risk reduction, funding cooperation, and strategic business.

(1) Risk reduction

The biggest issue in promoting the participation of Japanese private enter-

prise in PPP is how to share the risks. It is important to keep in mind management of the risks — the way the risks can be reduced. METI proposes solutions for two types of risk: project finance risk (e.g., contracts and compensations for loss) where recovery is possible through market mechanisms; the other is the political commitment risk associated with PPP in developing countries.

① The establishment of business platform and information provision
The risk in projects currently implemented is handled by private enterprise. The concrete solution is to improve the capacity as total service provider (the ability to supply general services). Although Japanese companies are highly capable in the infrastructure area, they have lacked international competence in structuring the industry as a system and coordinating each field as a total service. Asian Public Private Partnership was founded in January 2006 to create a business platform for discussing corporate capability on PPP activities. This partnership allows private enterprise to discuss and exchange information on ways to promote Asian PPP. Asian PPP will activate a system whereby information from the government is sent to each company through the business platform. For this partnership, it is important to have access to information on business environments, such as that which is collected by the World Bank. A system is required that will translate objective data like Doing Business into Japanese so that private enterprise will have insight into international discussions and information necessary for decision making.

② Dialogue between governments
It is an absolutely necessary condition for PPP that the partner government is involved because the government and private enterprises have complementary roles. Ensuring the partner government's commitment is important. For this reason, it is important also to discuss a system for the partner government to enhance the reliability of that commitment (such as legal infrastructure development including information disclosure and penalties) rather than to engage in bilateral political dialogue. METI is promoting the establishment of a bilateral PPP working group with each Asian country to provide a platform for the partner government to discuss proposals as well as to promote discussion with the Japanese government. In March, 2005, a PPP forum was held in Bangkok followed by another one in Jakarta.

(2) Cooperation with private funds

Attention has been given to cooperation with private funds to realize PPP business. One reason for this is that the financial system vulnerability which

caused the 1997 Asian currency crisis has not been fully resolved. This vulnerability should be addressed because such crisis adversely affects the private sector in the financing of infrastructure building and maintenance

① Project finance

METI is proposing a financial package of Asian PPP combined with various project finance sources. Specifically, it is proposing a project finance revenue bond in fields where private enterprise already is involved. However, further research must be conducted as there is not yet sufficient analysis to support the plan. An alternative is to use sector loans and grant aid to implement market enhancement for the purpose of extending the fields suitable for the future entrance of private enterprises.

② Review of developmental finance including ODA

Developmental finance including ODA is also being reviewed. Some specific plans are being mentioned: introducing more flexibility into ODA, making it possible to provide ODA to sub-sovereign partner governments, providing ODA for O&M, and enhancing market mechanisms in cooperation with other international institutions. In this regard, it is important to examine institutionally the Nippon Export and Investment Insurance (NEXI) system, especially in terms of the needs of Japanese firms.

(3) Strategic infrastructure development

The third major issue is to tackle infrastructure development more strategically. It is important for both the government and private enterprise to be involved in each step of the project (plan, proposal, implementation, and evaluation). The condition of infrastructure development in developing countries already illustrates the difficulty for government to establish an optimum private investment environment that will produce a PPP investment climate. For this purpose the following should be considered: 1) form partnerships with private enterprises that are familiar with the economy of the country in which PPP is to be implemented, 2) make policy proposals for legislation related to privatization and develop the business environment through partnerships, and 3) implement specific privatization projects in developing countries as pilots where policies and environments have already been devised. It is also important to involve private enterprise in revenue bond feasibility studies.

8-4. Conclusion – Contributions to Development by private enterprise

Economic development as a recognized process is relatively recent (since the post-World War II era), and social development is even more recent. Within this short historical timeframe, FDI and trade have predominated, contributing significantly to the development of target countries. The dramatic economic growth of South-East and East Asian countries after the late 1980s offers a clear example of FDI and trade activity impact. The role played by Japanese private enterprise in this process illustrates the vital contributions that the private sector can make to sustainable development.

The growth of Asian countries, including India, and the stagnation of sub-Saharan African countries indicate that private enterprise plays an essential role in the economic growth necessary for development. Since the fall of the Soviet Union, the government-led socialistic approach to development has been refuted. Nonetheless, in some African countries where the private sector is almost non-existent, making consistent progress in poverty reduction and attainment of the Millennium Development goals (MDGs) difficult. In recent years, the major donors, including the World Bank, have reaffirmed the importance of the private sector.

Japanese private enterprise and ODA have played a major role in the development of East and South East Asia. The apparent impact of FDI and private enterprise on development has given Japan a sense of comparative advantage for a development strategy based on private enterprise. The current ongoing recovery of the Japanese economy is quite likely to create interest among Japanese companies in the problems (e.g., poverty) of developing countries. As mentioned earlier in this chapter, compared to western countries, Japanese companies have made surprisingly little contribution in this field, due perhaps to differences in culture and history, and possibly tax regimes. However, as mentioned in Chapter 1, it is unrealistic for Japanese private enterprise to remain indifferent to the issues of developing countries. The Japanese government should provide incentives to the private sector, including PPP discussed here, so that they can increase their contribution to economic development. Based on the above analyses, some of the ramifications of optimal involvement by Japanese companies are suggested, especially as related to the role of PPP.

Table 8-6. Involvements of private enterprises into development and PPP

	Profit oriented motivation	Non-profit oriented motivation
Japan's PPP (promoted by METI)	① FDI	② Donation through corporate foundation
	③ BOP business	④ Development-related activities such as poverty reduction through the establishment of CSR
definition by PPP the World Bank and USAID		

8-4-1 PPP and contributions by private enterprise to development

FDI is development financing by private enterprise which contributes to job creation and technology transfer in developing countries while pursuing profit. Firms that provide FDI, regardless of their intentions, carry indirect development effects. Supportive activities are provided through CSR for companies willing to be more directly involved in development result. The development impact of CRS is not as great as that of the companies' own business activities but its effect is more direct because CSR focuses at the project-level. Whatever the motivation, PPP functions to involve private enterprise in development. In the West, not only private enterprise but NGOs and foundations are considered to be PPP development partners, maintaining their partnership to support corporate CSR activities and BOP business. In Japan, PPP measures being addressed include sharing with the government the cost and the risk associated with corporate involvement and promoting private enterprise participation. These are issues relevant to the promotion of direct investment based on corporate profitability. The difference between the Japanese and western approaches, therefore, seems to be, as shown in Table 8-6, that in Japan PPP is viewed mainly as enhancement of partnerships that promotes FDI while in the West it has multiple purposes.

8-4-2 Implications for development by the Japanese private sector

The realization of a business based PPP in which Japanese companies can be expected to make contributions to development will require consistent effort. In the future it will be important to structure alliances so that all private sector interests are engaged as development players.

To achieve that objective, there are some issues to be clarified both in the private sector and in governments. In the West all stakeholders in private

enterprise may be involved in development. It can be assumed, therefore, that this style of PPP rests on a high CSR familiarity among companies and a wider social atmosphere for tackling developing country assistance. At the same time, as shown in section 8-3, new movements among private enterprise are visible, for example, rising interest in CSR and implementation by companies themselves directly through NGOs. To accelerate these movements in this globalized age, such companies will increase their CSR participation, implying that more research on CSR and corporate development is needed.

One area government should consider to enhance the active involvement of private firms in CSR is preferential tax treatment. Simplifying procedures for NGO development assistance will facilitate private sector involvement.

With an eye toward constructing partnerships so that more Japanese private sector interests can be incorporated in development, PPP issues should be addressed to promote private enterprise participation. The Japanese ODA system is now undergoing drastic change, making it necessary to develop new developmental strategies that involve private enterprise or other private sector interests rather than simply implementing traditional activities at the government level.

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Africa's Poverty Reduction Strategy

Yuichi Sasaoka¹

The goal of reducing poverty in Africa is attracting more attention than ever before in Japan and the international community.² Since many African countries gained their independence in the 1960s, it has repeatedly been said that development has failed in Africa. The 1970s was the era of 'big government' in which government projects and public enterprises expanded enormously. This development methodology collapsed, and with rising primary commodity prices, Africa faced inflation, budget deficits, and political instability. From 1980 through the early 1990s, the World Bank and the International Monetary Fund (IMF) implemented Structural Adjustment Programs (SAP) in over 30 African countries that included market liberalization and promoting macroeconomic growth. Until the end of the 1980s, aid competition between the East and West blocs under the cold war excessively increased the volume of Official Development Assistance (ODA) to Africa.

During the cold war, the 'quality' of democracy and political and social governance were not an issue if a new African state belonged to either East or West bloc. Serious problems seen in the Mobutu dictatorship in former Zaire, human rights abuses in Nigeria, and apartheid in South Africa were all overlooked in the early stages. In the early 1990s, Europe and the United States decreased their ODA to Africa, the continent made little progress, and governance remained weak. Among donors, a phenomenon called 'aid

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2. In this paper, Africa refers to sub-Saharan Africa (SSA). However, the African continent as a whole is also a frequent topic of discussion; it is a ground for research and the creation of organizations and movements focusing on development. The African Union (AU) and New Partnership for African Development (NEPAD) are organizations that cover the entire continent.

fatigue' set in and economic assistance shifted to regions with emerging demand such as Eastern Europe. Skepticism spread among donors, researchers, and civil society about hopes for African development.³

On the other hand, a framework for a new world order was being developed that included low-income countries marginalized under globalization. A declaration of the 1990 Houston Summit was intended to promote democracy worldwide during the 10 remaining years of the 20th century. For African states facing declining financial aid, political liberalization (democracy) was not an option, but an obligation (Young, 1991). A new era began where additional aid would be granted provided that good governance and democracy were promoted, however, aid would be cut immediately if progress seemed minimal. At the same time, a new development strategy was introduced that focused on aid to low-income countries using the World Bank's Comprehensive Development Framework (CDF) and the Poverty Reduction Strategy Paper (PRSP) as a core approach.

Funds of ODA from the Development Assistance Committee (DAC) dropped from \$14 billion in 1994 to \$10 billion in 2001, however, Africa again became a concern to European countries around 1999 when leaders at the Cologne Summit agreed on an enhanced Heavily Indebted Poor Countries (HIPC) initiative. Following this action was approval by an IMF-World Bank Joint Development Committee of the Poverty Reduction Strategy Paper (PRSP) in 1999, and adoption of the Millennium Development Goals (MDGs) in 2000. Following the terrorist attacks in 2001, the United States has made ambitious efforts in poverty reduction, linking it to counter terrorism measures. In the same year the New Partnership for African Development (NEPAD) was enacted, in 2002 the African Union (AU) was established, and in 2003 the Evian Summit set forth an African agenda and the Third Tokyo International Conference on African Development (TICAD III) was organized. Promoting aid to Africa has gained international momentum and is growing.

With these preceding actions, 2005 was designated as the Year of Africa and the international community has committed to support the continent's

3. Several researchers examined the causes of Africa's slow development. Fukunishi and Yamagata (2002) pointed out prime factors such as natural conditions and ethnic diversity, and also referred to policy-related factors such as premature opening of markets and low-quality education. Sachs-Warner (1995) said low rates of life expectancy and closed markets are major factors. Easterly-Levine (1997) explained that heterogeneity in society (such as ethnicity) was a factor behind government economic policies that hinder growth. According to DfID (2001), armed conflict has become one of the most important causes of poverty in Africa.

rebirth. The UN (UNDP) Millennium Project and the Commission for Africa (CfA) issued a report explaining the severity of Africa's problems such as poverty, HIV/AIDS, and conflicts; and the importance of international cooperation to solve these problems. A considerable number of African countries have successfully improved their governance and achieved sustainable development, and through AU and NEPAD, Africa is undertaking positive political action toward regional integration and good governance by its people. Alongside these international campaigns, the Gleneagles Summit in July and the United Nations World Summit (High-Level Plenary Meeting of the 60th Session of the General Assembly) in September reached significant agreements. Industrialized nations pledged to double their aid for Africa. Cooperation between industrialized countries and Africa has advanced. Although African development has not been successful, it will see a massive increase in new aid and enter a new phase (see the subsequent section by Sugano for details on Africa's current development strategies and their policy implications).

This chapter will examine some of the significant development approaches for Africa and also make suggestions for Japanese aid. The first section will review the concept of a Poverty Reduction Strategy (PRS) as a national strategy, while the second will observe the core sectors presented in the PRS — primary education, agriculture and rural development, and infrastructure. The third section will discuss aid modalities, which are also relevant to these sectors. The fourth section will examine the future course of Japan's development with specifics for implementation, and the last section will summarize the entire chapter.

9-1. PRS as a national development strategy

The PRS — which has been widely accepted in the development community with the start of this century — is not simply a framework for low-income countries such as those in Africa to accept loans from the International Development Association (IDA) and IMF. It has a major impact on the overall policymaking that determines a country's development strategy.⁴ As of June 2005, 49 countries have prepared a PRS. More than one-half are from Africa and more than one-half are HIPC's (World Bank and IMF, 2005:1). Under a partnership principle, governments in collaboration with develop-

4. For details on the political significance of the PRS, see the subsequent section by Sugano.

ment stakeholders plan, implement, and monitor the PRS, hoping that this partnership will increase the scale of operations, reduce government transaction costs, and improve accountability.

In connection with a series of institutional reforms, development activities show progress in countries that have already engaged in the PRS process. Contributing to the progress are various reform initiatives introduced within the last 10 years such as public sector reform, Sector Programs (SP), Public Financial Management (PFM), and decentralization. Institutional reforms are implemented for various reasons, for example, in Uganda a public service delivery reform was adopted in response to a Public Expenditure Tracking Survey (PETS) that made it apparent that aid was not reaching final service points (Reinikka and Svensson, 2002). However, many reform programs continue to be donor-led because they are linked to policy conditions and governments are unable to take full ownership.

The PRS needs to address the appropriate role of the government and markets to meet each individual country's development and identify which sectors should be given priority for government resources. Each African state should make this decision, however, this also becomes a difficult problem for donors when holding policy dialogues with the recipient country. If the PRS requires global integration of free competitive markets and is only an extension of the "Washington Consensus" in which structural adjustments policies are promoted, the PRS may not be able to seek a proactive role for the government (Rodick, 2001). Conversely, if the PRS is looked upon as incorporating a new social policy perspective — the attainment of MDGs — it then functions as a strategy of 'inclusive' liberalism (Craig and Porter, 2003).

In the past policy interventions to improve living conditions for the poor took contrasting approaches (Ahluwalia, 1990; Bhagwati, 1988; Dreze and Sen, 1989). On one hand was an indirect strategy, in which economic growth was emphasized and the benefits of growth would trickle down to the poor. Dreze and Sen refer to this approach as 'growth-mediated security.' On the other hand was the direct strategy, in which income would be diffused in a manner favorable to the poor, creating a more desirable state of consumption for the poor, and leading to poverty alleviation. This approach is referred to as 'support-led security.' Shigeru Ishikawa (2002), while emphasizing the role of the developing country government, contrasted these approaches as the 'broad-based growth' approach and the 'pro-poor targets' approach. The former takes growth promoting measures through building infrastructure and introducing industrial policies and aims to sustainably reduce poverty by

redistributing the benefits of growth. The latter takes measures to expand basic services such as those of the social sector and focuses on immediate action in saving the poor from harsh living conditions.

When the first round of PRSs were prepared in each country, a 'pro-poor targets' approach were emphasized. The PRS is a set of aid programs with poverty reduction as its overarching goal, along with sector programs in both the social sectors and productive sectors (such as agriculture and roads). The PRS and sector programs share factors such as inclusiveness, a results orientation, and participation and do not contradict each other theoretically, however, the final outcome of a poverty reduction approach needs to be confirmed by monitoring and an Annual Progress Review (APR). The sector program is effective at achieving development goals by sharing policies and strategies among donor partners. Moreover, it also has an objective to restructure the government's recurrent budget to meet the volume of aid, reduce the recipient country's transaction costs imposed by the various donor systems, and promote coordination on specifications (of tools and machinery) for future maintenance purposes.

When compared to other regions, Africa's low-income countries apparently improved their human development index between 1998 and 2002, indicated by measures such as primary education completion rates, measles vaccination rates, and access to safe water (World Bank and IMF, 2005:6). Nonetheless, sector programs are criticized because their basic principles appear uniform,⁵ but the similarity of African sector programs is a result of their European origins and ideology developed after the colonial period.⁶

Emphasis on the 'broad-based growth' approach is gradually growing in the PRS process of each individual country. Although budget limitations make it difficult to pursue these two approaches simultaneously or combine them to develop the most appropriate strategy, there is significance in these actions. Growth promotion was not disregarded when the PRSP was still in its planning stage in Washington (IMF-WB, 1999). At that time the social sector attracted attention due to external factors such as the HIPC's initiative and adoption of the MDGs and an internal factor, commitment to democratic elections. There was also recognition that in order to reduce poverty, it was

5. Other criticisms argue that uniform programs are forced on several countries and participation from people of all levels is not achieved (McGinn, Samoff), and that donors who are the majority actually gain more power than the recipient government, creating a hierarchy of power among donors (Klees). See also Chapter 3.

6. Policies that guarantee a minimum quality of service to be received by its people (National Minimum Standards) come from a social ideology.

essential to establish industries that generate employment.

The major donors' plan to expand aid to Africa in preparation for the 2005 Gleneagles Summit accelerated the move to integrate the two approaches/strategies (hereafter referred to as the 'mixed strategy'). Furthermore, the Sachs report and the Commission for Africa report pointed out that with increases in the amount of aid to Africa, strengthening governance and promoting infrastructure investments would be significant in addition to improving the social sector.⁷ NEPAD shares this position and the World Bank in its Africa Action Plan presented the importance of shared growth through private sector promotion, exports, and infrastructure investments (WB, 2005).

With an increase in the volume of aid, the current international tone of the PRS generally accepts the 'mixed strategy'. In Tanzania, it appears that overemphasis on a certain sector will not only raise political opposition, but will also diminish incentives if it becomes part of the structure. Hence in 2005 a second round of PRS was prepared that is more flexible but also more complex compared to the first. With the exception of post-conflict countries, the time has come to specifically develop a strategy that integrates the social sector and productive sector. Concrete methodology of PRS in each country has not yet provided a clear outline of sector planning especially in the productive sector and is expected to make significant progress.

In recent years African nations have come to focus on their weak governance.⁸ The Commission for Africa has stated the importance of promoting democracy and improving governance because these institutions are necessary for poverty reduction (CfA, 2005). Weak governance allows ethnic conflicts to emerge and patron-client relationships to exist. Progress is necessary in governance and democracy, but the European and American model cannot simply be applied. African states face challenges posed by the contemporary world and many are still in the process of becoming modern states. The development mechanism that is supported by a system of people sharing benefits with the community is generally weak.

7. Killick's (2005) view is that increases in investment should be performed cautiously and should not be made in haste.

8. In NEPAD's framework document (October 2001), one of the factors for Africa's stagnant economic growth is attributed to "poor leadership, corruption and bad governance in many countries" (Article No. 22).

9-2. Core sectors and their future direction

This section will discuss three core sectors presented in the PRS — primary education, agriculture and rural development, and infrastructure. Priority setting of these sectors differs depending on the individual country and timing, however, these sectors help to understand the significance of an ‘mixed strategy’. Every sector has the characteristics to apply itself to the mixed strategy, for example, in the field of water resources, water used for drinking purposes will fall under the social sector, however, water used for agricultural purposes will fall under the productive sector. Resource allocation is not only an issue that affects the combination of different sectors, but is also an issue within each sector.

9-2-1 Primary education

In the PRS, the social sector generally includes primary education, healthcare, HIV/AIDS, and infrastructure (such as providing water and developing roads in rural areas). With the influence of MDGs, these pro-poor public expenditures are increasing in countries implementing their PRS. According to the 2005 IMF/World Bank review, among the countries that qualified for assistance as HIPC, annual expenditures by 27 countries on poverty reduction as a share of GDP increased from 5.5 percent in 1999 to 7.8 in 2004 (the entire developing country rate was 6.4 percent in 1999 and 8.3 percent in 2004). Educational spending, along with healthcare expenditures, dominate a major proportion of the pro-poor expenditure, however, the proportion of public expenditures on education in Africa is not particularly high. Educational spending as a percentage of GNP in developing countries was 4.0 percent in 1998 and 4.2 percent in 2001, whereas in Africa, it was 3.8 percent in 1998 and 3.4 percent in 2001 (UNESCO, 2005:368).⁹ Considering Africa’s exceptionally high fertility rate, educational spending per child would be even lower.

Until the 1980s, developing countries had a positive view about the relationship among educational spending, education indicators, and economic growth. However, cross-country analysis conducted during the 1990s found no correlation between educational spending and school enrollment. Likewise, no correlation was found between public spending on healthcare and the mortality rate of children below five years old. Pritchett (2001) point-

9. The major cause for the increase and decrease observed in each group is considered to be the result of a list of the countries which were surveyed in time.

ed out that the effects of investments in education were diminishing due to problems in educational systems and governance. In rural areas, systems that deliver public services to the least privileged are extremely weak and the quality of public services is exceptionally low. The effects of public spending on the social sector in low-income countries were ambiguous according to the 2000 World Development Report (WB, 2000a). Although there was evidence that improved education and healthcare contribute to accelerating economic growth, for a number reasons, the report remains skeptical about the effects of public expenditures in low-income countries.

Sector programs that center on education and healthcare are associated with a number of policy reforms. The Universal Primary Education (UPE) policy exempts primary education school fees in an effort to provide every child with an opportunity to attend school. Uganda's primary education is an excellent example of quantitative expansion — school enrollment increased from 2.8 million in 1996 to 7.6 million in 2004. This increased the opportunities for girls from poor households to enroll in school (Deininger, 2003; Nishimura, Yamano and Sasaoka, 2006). In 2003, Kenya implemented a similar policy and school enrollment increased from 5.9 million to 7.7 million. However, a sudden increase in school enrollment has lowered the quality of education and made the problem of efficiency such as increase of the absolute number of dropouts and repeaters.

Following institutional reforms and economic growth during the latter half of the 1990s, statistical surveys conducted by individual countries revealed the positive effects of investments in education. A survey in Tanzania showed that households with a parent with some secondary education or higher had over four times more income than that of a household with a parent with no education (TNBS, 2002). For an accurate assessment of this association, it would be necessary to know the income level of the household in which each parent was raised, yet the survey serves to promote enthusiasm for education in Africa.¹⁰ Reasons why Africa has not been able to demonstrate the positive assessment of education, in addition to Pritchett's remarks on governance, can be attributed to the low quality of statistical data and the biased distribution of resources (which are concentrated in urban areas).

Per capita educational spending and gross enrollment rate both reached

10. Educational spending is not the main determinant of educational outcome. Household characteristics, particularly income, parents' educational background, and literacy are considered to be more significant (ODI, 2003).

their lowest levels in 1990, however, in recent years they showed moderate improvements, thus forming a U-shaped curve. The decline stemmed from lack of funds due to growing external debt and the collection of school fees conducted under structural adjustment policies (the introduction of cost-sharing) (WDR, 2000:57). Per capita educational spending and gross enrollment rate showed a positive correlation from 1980 to 1985, but despite increased per capita educational spending, enrollment did not increase because enrollment of girls reached a plateau. The UPE policy of each individual country under the current PRS is making the trend of increasing school enrollment of girls more apparent.

Besides economic development, another hypothetical effect of educational investment is progress in the area of population control. Past arguments about the relationship between educational spending and population growth took place within each country, and insufficient data have raised contrasting views. Ainsworth et al. (1996) conducted research on years of girls' schooling and fertility rates in 14 countries and found that when girls received primary schooling for more than three years, the fertility rate dropped in one-half of the countries. Moreover, if they moved on to secondary school, the fertility rate dropped in all the countries surveyed. This research calls for further examination on the assumption that basic education has a positive effect on controlling population growth. On the other hand, opposing views were presented by Garenne and Joseph (2002). After an analysis of more than 20 countries, they said that urbanization, decrease in mortality rate, and wider acceptance of contraceptive uses were the determinants for decline in fertility rates, and that the effect of girls' education was uncertain. In an attempt to fill in the gender gap, however, there is no opposition from stakeholders against public policies that prioritize education for girls.

If the enrollment of more girls in school can have positive effects on future demographic stabilization in Africa, it would be advantageous to increase investments in primary education, provided that girls' reproductive health rights are respected. Educating girls can have other effects such as delaying marriage and childbearing, improving the mother's knowledge of hygiene, enhancing the mother's ability to plan rationally and her environmental management skills. Education may also enhance confidence, and thus mothers may gain a greater voice within the household. Africa's high fertility rate is related to factors such as high mortality rates, slow development of the monetary economy, children being valued as a source of labor, and risk management for women with weak property rights. Looking at fertility

changes between 1980 and 2000, there is a noticeable fact. The fertility rate in Africa was not that much higher than that of other regions in 1980 (Africa was 6.8 and the average of developing countries was 6.1). In the following 20 years, however, other regions have almost cut their fertility rates in half, whereas Africa's reduction remains at 16 percent (UN, 2002). Apparently further measures are necessary to control Africa's population growth.

In addition to these arguments and assessments, some believe that post primary education is important to determine the requirements for future economic growth. The same applies to higher education and advanced science and technology education as well as R&D. However, it would be impossible to make immediate increases in resources for all sub-sectors. Emphasis on primary education can be justified for several reasons. One is the international goals like MDGs and Education for All (EFA). The second is the argument that a policy should be given time to reveal its outcome. The third is the prerequisite for the next level of education. With these arguments in mind, it is important to assess educational spending in a medium- to long-term time frame using an 'mixed strategy' perspective, which should also be developed to exploit the synergy from investments in education and other sectors.

9-2-2 Agriculture and rural development

Land productivity in African countries compared to other developing countries has shown little increase since 1961. According to the Food and Agriculture Organization of the United Nations (FAO), it took Africa 40 years to increase yields from 700 kilograms to 1 metric ton per hectare, while Asia and Latin America increased yields from more than 1 metric ton to more than 3 metric tons per hectare (FAOSTAT). With the exception of Africa, other regions experienced the Green Revolution with the introduction of high-yielding varieties and fertilizers.¹¹ Africa has about twice the quantity of arable land per farmer compared to Asia, however, the continent generally has a huge disadvantage. It receives little rainfall, and many soils lack fertility. There are Oxisolos soil strata which are too old and weathered.

11. In East Asia, progress in human development and the development of a relatively stable agricultural production system were the base for economic growth. Countries such as South Korea, Singapore, China, and Taiwan had achieved UPE by 1965, and then moved on to experience high economic growth through export-oriented industrialization. On the other hand, Africa's political framework was unstable after independence, its public services were limited, and its people were only able to receive public education for about three years under severe living conditions. Africa lacks the "abundant high quality labor force" on which East Asian development was based. For this reason, within the PRS, agriculture and rural development, together with the social sector, can be looked upon as the remaining options for development.

Cultivation depletes the soils in only a few years, which must then remain fallow for more years to regain some fertility.¹² Cereal grains and root crops are the major sources of calories, however, the calorie intake level in Africa is far lower than that of other regions. Currently, there are 23 countries in Africa that are requesting food aid from the international community (FAO Liaison Office in Japan, 2003:1).

Africa's high fertility rate leads to a decrease in per capita agricultural acreage. Past increases in agricultural productivity were a result of growth in agricultural acreage, but as farm acreage decreases over generations, yield increases per unit area become extremely important. With the exception of South Africa, 70 percent of Africans are farmers. Although farmers need to increase land productivity, they lack capital for investments and technological improvements. Moreover, because cash cropping is vulnerable to price fluctuations, farmers are at risk when an abundant harvest leads to lower prices. There is need to diversify cash crops and produce value-added products by developing agro-industries.

In the agriculture sector, the PRS does not support 'big government,' but emphasizes a market economy. If the obstacles to producing agricultural products were removed, farmers would gain from free competition in the market, improving incomes and reducing poverty. However, introducing a market economy will not enable all farmers to make a stable profit. Small-scale farmers who do not possess the resources, skills, technology, and information to survive in an increasingly competitive market economy may become impoverished. It is necessary, therefore, to include safeguards for small-scale farmers in the PRS and agriculture sector programs.

The agriculture sector also needs a 'mixed strategy' that is aiming at 'poor' and productivity (or profitability).¹³ Small-scale farmers in general lack knowledge and information, and their main concern is subsistence farming. In this regard, agriculture sector needs to be promoted through food-security policy. In order to lessen the risk for each individual farmer, agricultural cooperatives or informal organizations that promote collective activities should be established. Moreover, it is necessary to develop a solid foundation of agriculture that does not depend on food aid and monitor agricultural production forecasts. Contrastingly, it is important to develop commercial

12. Sachs (2005) also focused on soil depletion as a waste of capital and this was one of the bases for proposing his 'big push' theory.

13. When focusing on production, attention should also be paid to the Public Private Partnership (PPP) discussed in Chapter 8.

agriculture and high value-added agriculture. Programs should be developed that encourage voluntary investments from wealthy farmers, entrepreneurs, and cooperatives for commercial crops that will satisfy the growing demand from urban areas and domestic markets. Expanding exports and import substitution also need attention.

Aid programs are not only required to focus on production, but also to develop processing, storage, transportation, and distribution to help small-scale farmers overcome barriers to entering the market economy. Irrigation is effective at improving agricultural productivity, but because the PRS no longer promotes large irrigation facilities, the focus has shifted to community-based, small-scale irrigation facilities. Improvements in production technology should be introduced in line with development of local skills. It is essential to encourage small-scale farmers to sell their surplus, provide them with market information, and improve their access to markets. There is also a need to organize farmers to support a complete flow of goods from production through distribution.

The government's responsibility in supporting access to inputs is unclear. In the past government-affiliated officials would visit farms to provide guidance on farming. Although this method was promoted, it ended in the 1980s with the introduction of structural adjustment policies and a shortage of government funds. In some areas, donors and NGOs have employed facilitators to provide technical guidance directly to farmers, however targeted areas were limited. Recent aid programs have tried to reduce unit costs and widen the range of targeted areas. Moreover, in Uganda and Tanzania where the agriculture sector program and decentralization are in progress, agricultural support services have been privatized. Farmer organizations develop plans through a participatory process and submit them to the local government to receive grants. If approved, they can request farming guidance from extension workers and research institutions on a contract basis, which is an attempt to provide technical assistance using a market supply approach. The success of these methods will depend on the degree of market development and progress of human development in rural areas.

In rural areas there are many small-scale farmers and the majority are poor. An agricultural revolution is important, however, for human security, and production and labor opportunities need to be diversified. In this context, the Rural Development Strategy (RDS) is significant because the strategy applies beyond the agriculture sector.¹⁴ An RDS encourages farmers to engage in non-farm activities and stabilize their cash income through region-

ally-specific businesses. Tanzania's RDS (2001) included approaches to balance and make progress in productivity, human development, and governance. Past PRS and sector programs in other countries, however, did not explore the extent to which agriculture and rural development and the social sector could mutually promote each other. A region with high productivity potential may achieve positive effects for development through support from only an agriculture project. However, in a region with low productivity, it is necessary to extend support beyond the agriculture sector and develop closer links with non-farm activities, the social sector, and the informal sector.

In addition, it is essential to have a prospering provincial/district city that can be the core of the agricultural community. Professor Amani, who prepared the RDS for Tanzania, also emphasizes this point. A site where urban residents could purchase rural products would boost trade and reduce poverty in the agricultural community by creating jobs and commercial activity. In a provincial/district city, it is important to effectively integrate the productive sector, social sector, and governance. If the PRS, which is central to the government, employs an 'mixed strategy,' the RDS is the regional version that embodies it.

9-2-3 Developing infrastructure

East Asia's experience demonstrates that developing infrastructure has contributed to economic growth and export promotion. It could be said that this was primarily due to its strong links with growth strategy. When considering the 'mixed strategy' for Africa, infrastructure development has multiple functions in addition to its connection to economic growth — different scales and types of infrastructure are expected to meet a wide variety of needs for social development. They will also contribute to promoting social justice, distributing resources, and reducing vulnerability of the poor, in addition to economic growth. In the Sachs report (2005), infrastructure development is encouraged to overcome Africa's problems, however, before preparing a plan, it is important to accurately assess demand because Africa is sparsely populated. The purpose of infrastructure development lies more in supporting local economies and social activities than in leading economic growth.

(1) Building roads

As a basis for rural development, rural roads are necessary. These roads are

14. The World Bank's RDS is structured as follows: (i) promoting widely shared growth, (ii) increasing opportunities and access to services, (iii) reducing risks and vulnerabilities, and (iv) good governance.

essential not only for production and distribution of agricultural goods, but also for transporting patients and receiving disaster relief. For food security, rural roads need to be developed to deliver food and relief supplies to areas of food shortages during the rainy season, and to transport disaster victims to safe locations. Planning and development of road networks must be decided using a transparent process, however, it is also necessary to examine and make decisions from a perspective that understands the multiple effects on poverty reduction. Moreover, a road maintenance system should be established locally and donors should support capital formation through a plan developed to make the government — the central or local government, or agency, whichever is more appropriate — financially and technically autonomous. Partnerships among donors are important, as is support that focuses on how rural roads are maintained within the government's recurrent budget and the necessary revenue structure.

(2) Transportation infrastructure

Large-scale infrastructure facilities for transportation-related activities are important for maintaining relationships not only with coastal countries (that already possess basic facilities), but also with neighboring landlocked countries. Landlocked countries and the inland regions of large countries that are difficult to access tend to have a gloomy picture of their development. Transportation cost is expensive, and industrial products (processed goods for export made from imported raw materials) are not internationally competitive. Imported inputs for agriculture and imported basic necessities are expensive, yet in order to lower the costs, it is necessary to develop ports, storage facilities, and trunk roads in coastal countries.¹⁵ The Kenyan port of Mombasa is the main port of entry for imported goods transported to landlocked countries such as Uganda, Rwanda, and potentially, Ethiopia. There are expectations that developing a distribution system from Mombasa to Ethiopia will contribute to conflict prevention by mitigating the confrontation between Ethiopia and its neighboring countries. As for air transportation, despite the substantial role it displays in the export of flowers, frozen vegetables, and fish, its role for imports is limited.

(3) Small-scale infrastructure

Small-scale infrastructure needs to be developed for provincial/district cities

15. One study reported that the price of urea at \$90 dollars per ton in Europe rose to \$120 when it reached Kenya's port, and soared to \$500 in Uganda and \$770 in Malawi (FAO Liaison Office in Japan).

to prosper, as explained in 9-2-2. Besides road networks, providing market information and developing a wide range of facilities that store and process agricultural products will create an environment where intermediary agents (middlemen/brokers) will be forced to compete for a price to producers. The government, however, should not intervene in areas where the private sector can manage on its own and should respect the approaches set forth in the RDS and the agriculture sector program. Additionally, infrastructure to support provincial/district city residents is needed and tasks remain in areas such as water supplies and electrification. In particular, waste has become a more serious problem within the past few years.

9-3. Aid modalities

Aid modalities and the challenges to an 'mixed strategy' are discussed in this section. Following changes in the international environment and the mainstreaming of poverty reduction, recent issues of aid modality need to consider the following four points.

9-3-1 Sector programs

The sector program was developed in a number of sectors from the 'pro-poor targets' approach that values fair distribution and equality, and is usually financed by the government and with budget support from donors. Aid funds are required to increase predictability and to be on-budget.¹⁶ Questions arise about whether projects comply with a sector program. Donors that promote projects should take active measures to make a harmonious and efficient link with the program-based approach. In Tanzania where aid coordination has made significant progress, there are sectors where donors will find it difficult to implement a stand-alone project of their own. Various types of budget support and a pooled fund for technical cooperation are responsible for sector planning. Even if projects are implemented, prior notification of budget plans and conditions to enhance aid effectiveness such as aligning with government systems of disbursement and procurement may be required.

The social and agriculture sectors of low-income countries have a tenden-

16. 'Through-budget' refers to donor funds deposited in the government's national treasury as revenue, such as funds provided to a program-based approach (similar to the budget support explained in Chapter 5). 'On-budget' has a broader meaning, and even if funds are not deposited in the national treasury, donors are required to provide information to the government (such as details about budgeted funds and the amount of disbursed funds).

cy to seek uniformity as government programs. In these sectors it is difficult to legitimize interventions that only target a specific area for pilot implementation. An intervention, including projects, should therefore target a broad range of poor people rather than focusing on a specific site. If Japan implements a major project through its own development assistance, other donors that support the government's programs through financial contributions to the recurrent budget may look upon Japan as a free rider.

The degree of difficulty in implementing projects differs from country to country, and thus, it would be wrong to say that complete program-based approach is the single aid instrument promoted in Africa. Countries with the possibility for this kind of support include Tanzania, Uganda, Ethiopia, Mozambique, Zambia, Malawi, and Ghana. In these countries, donors that promote projects will be required — from a partnership framework — to participate in budget support and conduct only a limited number of wide-ranging target projects that are on-budget. Even in other countries, when implementing a project donor countries will need to align their support with the government's overarching policy framework and programs and share information on planning, funds, procurement, and assessment with all partners (government, donors and civil society, etc).

9-3-2 Specific targets

Projects that target a specific site can be legitimized from a broad-based growth approach because the output and outcome will have spillover effects to the broader public. A prime example would be projects dealing with infrastructure and the industrial sector. When implementing these projects, it is vital that they comply with the government's overarching policies and strategies and that a clear scenario is presented that explains the contribution of the targeted area's development to poverty reduction. Before implementing a small target project, it would be better for donors to establish a program of their own through technical assistance, hold discussions to confirm which government policies and programs the established program aligns with, and publicize it. To make the connection between economic growth and poverty alleviation, it is necessary to demonstrate the simultaneous decrease of both income poverty and social sector poverty. When designing a growth-promoting project, it is necessary to make projections about economic growth with attention to employment, new demands, and the income redistribution system. The plan should be well-balanced and flexible, because the poor is vulnerable to any kind of shocks. Resilience to shocks is necessary from the

standpoint of human security.

9-3-3 Rural development strategy

Rural projects that cross sectors sometimes cannot easily comply with the PRS-SP. In such cases, the RDS settles the project under the government's policy system and within the society. The RDS focuses on 'rural' — a spatial theme — and attempts to display a wide range of activities such as primary education, healthcare, infrastructure, governance, non-farm activities and so forth by replacing the traditional concept of agricultural development. The RDS will become an important option when the 'mixed strategy' takes form in rural areas. In line with this framework, the World Bank is emphasizing the Community-Driven Development (CDD) approach (World Bank, 2000b). CDD is a set of projects, and does not simply apply to projects taking place in rural areas, but also includes an approach that aims to enhance community empowerment through a participatory process. The basic methodology originated from "Area-based approach" initiated in the 1980s by the Nordic countries. Additional elements in this methodology include private sector involvement to improve the investment climate and distribute the benefits of economic growth.

The RDS, due to its comprehensive nature, has close links with various development strategies. For example, the environment conservation and natural resource management field overlaps with the Sustainable Livelihoods (SL) approach (DFID, 1998), a kind of RDS versions. When more than one sector is involved, coordination among administration and finance is important with SP. Coordination with local governments and service-provider organizations is necessary, where decentralization process devolves the power and responsibility from central bureaucracy. The main donors that emphasize the RDS are the World Bank, International Fund for Agriculture Development (IFAD), and Germany's GTZ. In the past, the Nordic countries promoted the RDS, however, with a focus on fair distribution and respect for the government ownership, they have shifted to more program-based approach and budget support.

On the other hand, the RDSs carried out by African governments are still evolving. Strong conflicts among ministries and poor coordination have made it difficult to make use of these plans. The plans are not so convincingly systematic and in case they just provide some voices to modify neo-liberal points of views in the agricultural SP. Beginning in 2000, several countries have made tremendous efforts to develop and implement the PRS and agriculture

sector program, thus the RDS has been overshadowed between them. The RDS, however, is an essential strategic framework for donors that promote projects because the 'mixed strategy' can be carried out in rural areas, and because experience can be accumulated through a steady, practical learning process.

9-3-4 Decentralization

With a goal of democratizing rural communities and strengthening delivery of public services that help reduce poverty, decentralization has attracted increasing attention. In countries where decentralization has progressed, funds for grants to local governments are pooled by the central government, and sector grants are allocated to the local government within the PRS-SP framework with the aim to reach the poorest of the poor. Nordic countries, the United Kingdom, and the World Bank are trying to strengthen this framework through budget support and coordinated program aid. The poorest of the poor have a voice as citizens and are in a position to exercise their client power as service recipients to service-providing institutions (World Bank, 2004). In order to establish their rights politically, public services need to be provided through local grant-based projects.

With the exception of technical assistance, donor-promoted projects are not actively implemented in rural areas.¹⁷ In promoting decentralization, budget support schemes have advantages over projects because projects have difficulty supporting grants to local governments (Sasaoka, 2005). Current decentralization plans are criticized because the discretionary powers granted to local governments are limited and there are several constraints to empowerment. Past projects carried out by the central government and donors were only able to provide support to a specific area, however, they were able to devolve more power to the local government and organizations through trial and error. Although plans are implemented fairly in regions where decentralization has progressed, it is important to direct attention to the risks of pursuing uniformity and mechanical equality.¹⁸

17. In cases where RDS support to local governments is provided on a project basis, grants from the central government are reduced in accordance with the 'off-set scheme,' which has been adopted in Uganda and Ethiopia.

18. Interviews conducted in Kenya in 2006 revealed that in decentralized cities, municipalities, towns and counties, political pressure to construct identical hospitals increased in each election district, making it more complicated to develop referral systems among hospitals and to supply personnel for service delivery.

9-3-5 Summary

Following the evolution of diverse aid modalities, Japanese aid, with its main aid modality of a project approach, now must comply with the government's overarching plans and strategies. Four issues face this aid modality: (i) budget support to PRS-SP, (ii) harmonization of sector programs and projects, (iii) harmonization of RDS and projects, and (iv) harmonization of RDS, sector programs, and projects. Overall, Japanese aid should not be implemented under an isolated, sporadic scheme. Japan's aid system should be a packaged program, embedded explicitly in the government's policy program. Exceptions would only apply to emergency humanitarian assistance and small-scale support to NGOs.

For (iii), harmonization of the RDS and projects, Japan initiated the "grant aid for community empowerment" under a village initiative beginning in 2006 and is planning to implement an untied, small-scale infrastructure project in a rural area. If these projects were randomly implemented without any alignment to higher-level policies and strategies, it would only replicate the limitations of project aid argued by the sector program approach (Harrold, 1995; Foster, 2000). On the other hand, if projects were to cross a broad range of sectors, it would be difficult to incorporate them under the sector program. For the project scheme to receive support from the government's RDS and the rural community's participatory planning and implementation framework, Japan will need to execute a well-planned communication strategy from an early stage.

To promote development that responds to distinct regional issues and enhances governance in a local community, and for the community to be involved in agriculture development, local infrastructure, and environmental protection, it is important to employ projects with various institution-building measures. Government-based development activities will shift toward programs, however, and non-government development activities need to be promoted through projects. There is a need for higher-level planning and strategies such as the RDS to flexibly coordinate the entire process, instead of SP with a high degree of standardization. In general, the RDS is very significant for governments of low-income countries and for donors like Japan. In countries where the RDS is slow to progress, Japan should be at the forefront of efforts to promote it.

For (iv), harmonizing the RDS, sector programs, and projects, the RDS has a function — in the context of a macro development strategy — to balance the sector program (which focuses on the social sector) and project aid

(which includes the productive sectors, governance, and environment conservation). The RDS can balance projects managed locally and projects directed by the central government with grants under standardized conditions. It can also promote financial coordination between the development budget and the recurrent budget, and between local grants and locally-generated revenues and funds. It has a role to entrench the overall impact of the PRS in the local community. This formulating process may seem roundabout to those working in the field, however, the RDS is necessary because it systematically introduces knowledge that is locally-based and concrete to the centrally-based policy framework of PRS-SP, and because it coordinates overall activities belonging to both government and non-government institutions.

9-4. Japan's strategy and specifics for implementation

Based on the discussions presented in the previous sections, this section will examine the desirable future course of Japanese aid for Africa. The PRS has the potential to have great impact through interactions with various public policies and governance reforms. In some sectors, however, strategies will have qualitative differences and the slow development of markets and governance can hamper the planning and implementation process. Japan is presented with a challenge to coordinate sectors, reforms, and local communities through the RDS as it aligns with the government's overarching policy framework represented by the PRS-SP. Japanese aid needs to change substantially as aid to Africa draws greater attention.

Within this context and with a focus on strengthening the recipient government's governance, this section will focus on three factors — participation, monitoring, and financial strategy.

9-4-1 Participation

Participation is regarded an important principle for planning and implementation over a wide field from PRS-SP to rural development projects. This does not necessarily mean that using participatory tools will automatically promote participation or improve it. Participation includes the development process, including the decision-making process within the community, and in the long term it means strengthening governance. Development schemes that only function when donors provide resources are not true forms of participation. Even if there is a little improvement, it is necessary to create lasting changes in the community development process after donors have withdrawn their

aid. Participation tools should be used with full understanding of this requirement.

The critical issue is that it is almost impossible not to step into the political realm of the government and society.

- To investigate the actual situation of participation, it is important to acknowledge how much participation is achieved by the poor through the planning, implementation, and evaluation process, and to clarify if the poor are being empowered through participation. If clients of services, including the poor, gain a political voice, the government will have clear accountability for the quality and quantity of services it provides.
- If government projects/programs and aid are delivered fairly through a participatory method, then beneficiaries will support a particular system. This is one of the intentions of the PRS. By becoming service recipients, people will be able to have faith in governance and democracy, which will strengthen cooperative activities among people and encourage development of institutions in general.
- The governance of the PRS will be affected by the incentives that support institutions and by sociocultural factors. When dealing with incentives, it is important to focus not only on the citizens (clients of services), but also on government staff and to improve salaries and payment schedules.¹⁹ In each country preconditions for supporting the PRS included receiving stable financing for the recurrent budget which helped develop institutions. Moreover, government staff need to be educated and trained so they are accountable for the services they provide, including to the poor.

9-4-2 Monitoring

As a donor, it is necessary to actively monitor the PRS. The PRS process is a joint action promoted through a ownership with the recipient country and a partnership among various stakeholders. Poverty monitoring and production of the APR are final confirmation of this effort. By sharing poverty data and its analyses, partners can construct more effective and interdependent strategies. The critical issue is the relationship between development activities and an evaluation of outcomes and macro-impacts.

19. In Uganda's education sector program, aid will cover not only other charges (OCs), but also personnel emolument (PE) for teachers including its arrears, under the condition that teachers participate in retraining programs and ghost teachers are removed from the payroll.

- Making progress toward objectives set by development strategies through a results-oriented approach and monitoring on a partnership basis will reduce the transaction costs for African governments and improve their accountability. Participating in such an aid coordination helps understand the relationships of partial contributions from individual donors and the entire development achievements. This cannot be achieved by individual donors alone.
- By monitoring the PRS process, the progress of each policy, strategy, and reform process can be confirmed. This will help capture the problems and challenges of the entire development strategy. However, the PRS and MDGs face challenges in harmonizing monitoring mechanisms (indicators and data collection systems) and in developing local monitoring systems. The actual implementation of these mechanisms and systems is not easy.
- Identifying the final destination of government expenditures through public expenditure management, information disclosure, and the public expenditure tracking survey (PETS) will improve the accountability of African governments.²⁰ Verifying government spending with the monitoring outputs and outcomes at each level will allow for a more precise understanding of the present situation.

9-4-3 Financial strategy

African governments need to strengthen their financial strategies. The social sector, including primary education, has a huge share of the recurrent budget. Salaries for service providers and administrative and maintenance costs are so large.²¹ Supporting the recurrent budget with foreign aid, however, raises the problem of aid dependency. An increase in the volume of aid in an effort to meet the MDGs is making this problem more serious. There may be voices that suggest pursuing pro-poor growth, but the problem is not that simple if government spending is necessary to carry out this strategy. Hence, the proposition here would be to build revenue institutions with a minimal increase in the government budget. The government will need to increase its own revenue.

- A foundation for revenue with a focus on efficiency is necessary, which

20. A Public Expenditure Tracking Survey (PETS) in Tanzania, unlike in Uganda, revealed no significant improvements observed in the implementation system with the exception of a few districts.

21. To the question of whether poor countries can afford to implement social sector programs, Sen (2002) replied that labor costs are relatively low in poor countries as a supportive evidence.

in other words is an increase in tax revenue. A tax system that will not hamper economic growth is needed. The desired system is one that would have an automatic increase in tax revenue as a result of expanded economic activities through import duty reduction under trade liberalization. The central and local governments should decide the key areas of taxation and strengthen the tax collection system to work efficiently and fairly.

- The viability of development strategies would improve by developing a scenario where increases in government revenue in the long term will allow governments to liquidate their budgets instead of relying on foreign aid. For low-income countries to establish a foundation for revenue by 2015, the MDG target year, is generally considered difficult. However, each government is required to maintain or increase the level of revenue in line with the MDGs at its earliest possible time after 2015 and lower its degree of aid dependency. Each donor needs to initiate discussions that set international objectives beyond 2015 with a focus on increasing government revenue, though achieving MDGs targets is considered very difficult in the African region.
- Cooperative activities mentioned earlier include tax payments and user fees as part of a financial strategy. It is necessary to provide information and education that can foster social capital and create a culture that understands the necessity to pay taxes in return for receiving public services. It is necessary to expand people-to-people cooperation and extend it to the local government. Moreover, the government should be required to ensure transparency of revenue flows.

9-5. Conclusion

The PRS is a national framework that includes medium-term sector planning, local (government) development planning, and the national budget process, all with the goal of alleviating poverty by revamping policies and programs. In general, Africa is a poor continent on various indicators and has a high population growth rate. Initial conditions for development were not favorable, and it faces various problems of governance. Theoretically, it is possible to create a plan in which the government, with cooperation from partners such as civil society organizations, prepares and implements a PRS and works on institutional reforms and gains public support through delivery of public services. Further advancement of outcomes and institutional reforms are mutu-

ally facilitating, according to the plan.

However, the capability of African governments, social institutions, and organizations are strictly limited. Even when projects are implemented, the outputs and outcomes do not extend to other regions and there is no guarantee about the budget support that the flow of funds will be managed properly and monitored smoothly. There are a number of limitations to the project modality, whereas budget support involves some risks, including recipients becoming aid dependent. Under these circumstances, Japan is expected to have an aid system where different instruments can be applied jointly and freely as an aid modality. The development 'menu' will need to be prepared in a specific context to meet a country's development tasks and progress in its sectors, however, it is essential to have the necessary tools to be able to respond to many different situations.

As explained earlier, the three significant factors of Japan's development strategy are participation, monitoring, and financial (revenue) strategy. Despite their significance, my perception is that in the past, Japanese aid did not make enough efforts in these areas. Through more work in these areas, there is a need for Japanese aid to connect with African governments and societies at a more profound level. Japan should become a more committed donor to help bring prosperity and justice to Africa. The 'mixed strategy' applied to the core sectors is not simply an eclectic mix. Africa is faced with severe conditions, its market forces and governance are weak, and thus a balanced strategy with an emphasis on stability is desirable. This strategy applies to the balance between sectors with a 'pro-poor targets' approach and the 'broad-based growth' approach, and to the balance of resource allocation by central and local governments. Even if economic growth is emphasized, the development scenario is incomplete if sufficient revenue cannot be generated to support future social sector activities. It is important to tackle poverty through the RDS and decentralization, both of which are attempts to restructure the central government with an emphasis on local needs and characteristics.

It is not easy for the Japanese community to have an accurate view of the present state of Africa and African poverty. Japan does not receive many immigrants from Africa and does not have a clear image of what the society is like. Media coverage of Africa may have increased recently with the White Band movement²². The Japanese are known for their long life expectancy, however, its population started decreasing last year. It is projected that the population will drop to 70 million in 100 years if it continues to decrease at

the same pace. Africa has a population of 700 million, with many people dying from HIV/AIDS and malaria and the average life expectancy dropping. Japan and Africa, as an industrialized country and a developing country, stand in sharp contrast to each other in many ways. For development aid to be effective in Africa, donors will need to have field experiences and a plenty of imagination.

22. The Global Call to Action against Poverty is a world-wide alliance committed to suggesting world leaders to come up to their promises, and to make a breakthrough on poverty in 2005. [<http://www.whiteband.org>, <http://www.pia.co.jp/whiteband>, <http://www.hottokenai.jp>]

Complementary Discussions to Chapter

Perspectives on African Development Strategies and their Policy Implications

Yukio Sugano¹

9-1. Introduction

The year 2005 marked a new horizon on African development. Renewed financial commitments by donors at the G8 Summit at Gleneagles and the UN World Summit on Millennium Development Goals (MDGs) focused the international development agenda throughout 2005. In the climate of mounting interest in African development, research projects and other initiatives yielded a considerable number of official reports and research papers. This chapter will review strategic perspectives and trends from these reports, examine their policy implications for African development, and explore future prospects.

The report of the UN Millennium Project Task Force, an independent advisory body to the Secretary-General, offers a diagnosis of why progress toward the MDGs is so mixed across regions and goals, and presents recommendations to be implemented at the country level and those to guide international agencies at the country level. Sub-Saharan Africa, the only region where most countries are far from achieving most or all of the goals, is the major focus of the report. Similarly significant is a report from the Commission for Africa, organized under the initiative of U.K. government, which analyzes the development challenges facing African countries, scrutinizes strategies, and offers recommendations. Both reports advocate the urgency of African development to the international community and call for

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immediate actions.

Poverty Reduction Strategies (PRSs) have been in place for six years, providing a basic framework to organize international endeavors for African development,² and second-generation PRSs have been prepared by several countries. In 2005, the World Bank and other institutions submitted evaluation reports on the progress and results of the PRS process in low-income countries. The reports show how PRSs have unfolded at the country level over the last five years, and offer policy implications.

The evaluation reports also articulate the gravity of, among others, two aspects of the PRS process. First, the capacity of the public sector is increasingly recognized as critical to enable development. Recent World Bank reports on capacity development in African countries underscore that capacity development is the centerpiece of development challenges. Second, recent studies highlight the intrinsically political context of the PRS process and how the political economy determines how the PRS process unfolds.

With a significant financial commitment attained at the G8 Summit and UN World Summit, strategies for scaling-up endeavors for African development with expanded resources have gained attention. Donor initiatives will facilitate international responses to the call for expanded assistance for Africa. Among them, the World Bank group has compiled an Africa Action Plan to support policy and public actions by African countries to achieve well-defined goals such as the MDGs. Other reports deal with various issues relating to scaling-up development efforts.

9-2. Development challenges and recommendations for Africa

9-2-1 Two reports

Two important reports that were made public during 2005 described urgent development challenges facing Africa. The report of the UN Millennium Project led by Jeffrey Sachs (Sachs Report) outlines ways how to achieve the MDGs. It covers all low-income countries with a major focus on African countries, while the Africa Commission Report deals with development strategies specifically for African development.

Both reports have much in common, particularly in these areas:

2. While Japan is considered to have a comparative advantage in building infrastructure, Japan's 2003 ODA Charter is aligned to the mainstream discourse on development by adopting poverty alleviation and good governance among its principles.

- Raise awareness among the international community to augment assistance to support African countries.
- The drafting process uses multiple resources, including researchers, practitioners, and official documents.
- Advocate the urgency of African development and attainment of the MDGs, drawing attention to the tremendous costs that will be incurred if prompt actions are not taken.
- Identify good governance to be placed at the heart of African resurgence.
- Call for, among others, a rapid increase of ODA for Africa.
- Identify a 'big push' of basic investments in public administration, human capital, and basic infrastructure as the key to escape the poverty trap, upon which rapid expansion of ODA is based.
- Underline the belief that successful growth will be led by a strong private sector, and that policies and governance should be focused on creating the conditions where growth can flourish.
- Reconfirm the essential role of infrastructure.

'Big push'

The two reports, however, present somewhat different explanations on how a 'big push' of basic investment is required for Africa. The Sachs Report explains it in the context of a poverty trap in low-income countries, where capital stock is too low, the economy is unproductive, and households are impoverished. In addition, Sub-Saharan Africa is further burdened by adverse conditions, including:

- Transport (for example, landlocked economies, inland populations far from coast and navigable rivers, and very low population density).
- Agriculture (low and highly variable rainfall, lack of suitable conditions for irrigation, nutrient-poor or nutrient-depleted soils, and vulnerability to pests).
- Health — malaria and other tropical diseases, high HIV/AIDS prevalence, and others.

These conditions reinforce and amplify poverty, and the situation continues to degenerate. The report goes on to say that a big push is required to raise the economy's capital stock to the point where the downward spiral ends and self-sustaining economic growth takes over.

The report of the Commission for Africa says that a big push is required because of the interlocking nature of problems. Countries confront many

development challenges such as building an effective state, peace and security, human development including education and health, and a strong private sector. These areas are interrelated, and success or failure in one area may reinforce or constrain the others. The legacy of Africa's difficult history and its current circumstances mean that Africa will have to break out of a set of vicious cycles that reinforce each other and shackle the continent. If the problems facing Africa are interlocking, so are the recommendations and actions to overcome them. The report concludes that the big push approach is the only one that can address Africa's challenges with the required urgency and effectiveness.

Country-level processes for development

Both reports try to convince us that a big push approach, which means a prompt expansion of ODA, is indispensable to reverse the interlocking problems of African countries and help them maintain a sound development track. Conversely, it is an open question whether a rapid increase of ODA would effectively help these countries achieve sustainable development. Vast resources were deployed to Sub-Saharan Africa until the 1990s, far larger than those to Asia on per capita basis, resources that have not left any meaningful agricultural or industrial assets. It cannot be ruled out that another massive investment would once again be wasted.

While advocating a big push as the key requirement, both reports address important aspects of development. The Sachs Report presents country-level processes for development, including an action plan for countries and the international system. Likewise, the Africa Commission Report proposes an action plan.

The significant financial commitment by donors in 2005 has left an agenda in the next stage — how to advance African development with expanded resources. It will be addressed in the latter part of this chapter.

9-2-2 The 'effect of aid' issue

In June 2006, the two research papers by two IMF economists on the effects of aid on economic growth attracted the attention of the public (Rajan and Subramanian, 2005a). Their comprehensive econometric analysis considered preceding studies. In the cross-section analysis, the coefficient representing the effect of aid was very small, which means that aid contributions to growth are minimal, while the panel data analysis shows that the effect of aid is very fragile or obscure. Given the policy implications of this research, the study

drew considerable international attention.

9-2-3 The aftermath

The campaign that advocates expanded assistance for Africa helped add to the momentum for increased focus on the continent. The 2005 G8 Summit at Gleneagles and UN World Summit have renewed the commitment of the international community to support African development beyond the 2002 Monterrey pledges for additional development assistance and debt relief.

Among the moves to strengthen assistance to Africa, the initiatives by the U.K. government to launch an international campaign stood out. The government in recent years consistently advocated the urgency of expanded support to Africa. In 2005, Prime Minister Blair organized the Commission for Africa that compiled a voluminous report. The government designated the African development issue as one of the major agenda items of the G8 Summit at Gleneagles, where Chairman Blair declared that an agreement had been reached on doubling ODA to Africa.

Likewise, the French government demonstrated a positive stance toward Africa. On the occasion of a G8 Finance Ministers Meeting, the government floated a plan of 'front loading' aid to Africa, with the establishment of an international financing institution which would procure a critical mass of money by issuing bonds.

During the G8 Summit, Japan pledged to double its ODA to Africa over the next three years. Japan will strive to realize a strategic expansion of ODA, intending to increase its ODA volume by US\$ 10 billion in aggregate over the next five years.³

9-3. Progress of poverty reduction strategies at the country level

9-3-1 Review of poverty reduction strategies

In 2005, World Bank, IMF, and the World Bank Operations Evaluation Department reports reviewed the Poverty Reduction Strategy process after its five years of implementation in low-income countries. During the previous year the Overseas Development Institute also compiled a monitoring report on PRSs. While the PRS process in every country is unique, we observed overall trends through the reports, how the process has unfolded over time,

3. The UNDP *Human Development Report* (2005) criticized Japan for "no meaningful commitment on overall aid to GNI levels".

what has worked, what has not worked, and priorities for the future.

(1) Internal review of PRSs by World Bank and IMF

An official internal full-scale evaluation conducted by the World Bank and IMF after 2002 (2005 Review) delivers basic facts on implementation of PRSs at the country level, including:

- While countries have been encouraged to start setting concrete targets connected to policy goals, 16 percent of them put the target largely in place, 65 percent are taking action, and 22 percent have not begun any action.
- For a country to achieve its development goals, a medium-term development program needs to be linked to those goals. The report says, however, that “Overall progress on this front is mixed, and many PRSs would benefit from a more explicit link between goals and targets and the policies needed to achieve them.” In linking goals and targets to clear public actions, countries need to ascertain causal links, decide on the degree of specificity in their PRSPs, and make important choices about prioritization and sequencing. The report concludes that such work is a very challenging task, particularly in countries facing severe technical and institutional constraints.
- Policies and public actions are often inadequately prioritized.
- In line with increased attention to production sectors, countries are increasingly making growth a central element of their Poverty Reduction Strategies. However, there has been considerable variation in the quality of PRS growth strategies. Much of the discussion related to growth pillars has remained qualitative, with less specificity on policy and institutional reforms.
- Medium-term expenditure framework (MTEF) was introduced in 28 countries, but they require political commitment and deep institutional reforms and are constrained by weak institutional and technical capacity.
- An effective national monitoring system requires statistical capacity for which substantial improvements are needed in most IDA countries. Most countries continue to have difficulties tracking and measuring the effectiveness of pro-poor spending.
- Overall progress on improving aid through alignment, harmonization, and better coordination has been mixed. While donors often cite problems with the PRS or weaknesses of country systems as constraints,

they are making progress in focusing their support on priority areas specified by countries, starting to use simplified procedures and practices, and collaborating in joint analytic work and sector-wide approaches.

(2) ODI report

Drawing upon a range of formal and informal information on the PRS process, including selected interviews with DFID staff and others, ODI conducted a survey to review progress to date, identify key challenges, and draw practical implications for those engaged in PRSs at the country level, particularly donors. Gains achieved to date are described below.

What has been achieved to date

- Poverty plans are more comprehensive than ever before.
- ‘Poverty-oriented’ expenditures and inputs have increased.
- Prospects for linking poverty planning and budgeting have improved.
- Interest in poverty monitoring has increased.
- New opportunities for poverty policy debates, including some permanent ones, have been created.
- Civil society has been mobilized on an unprecedented scale.
- The principle of donor alignment and harmonization has been established internationally. There have been initial moves among donors toward alignment and harmonization by, among others, moving to sector and general budget support.

What is still missing

- Line ministries and sub-national levels of government have not been actively engaged in many PRS processes.
- Operational links between the PRS and budget and outcomes, especially at the sector level, remain extremely weak in many countries.
- Most PRSs have yet to deliver a fully integrated strategy in which the quality of production sector plans match those of social sectors.
- Existing institutions for government accountability such as parliament, audit offices, and media have been largely bypassed in the PRS process in favor of introducing new mechanisms for participation such as focus groups, consultative workshops, and PPAs.
- Poor people and organizations representing their interests have not been adequately represented in most PRS processes to date.
- Donors continue to spread their assistance across too many sectors and deliver aid through fragmented projects and programs that carry

heavy transaction costs for governments.

- Large amounts of aid continue to flow into poor countries almost entirely outside of national PRSs and budget processes.

9-3-2 Progress in implementation of the PRS process

The 2005 Review and the ODI monitoring report convey significant information about several aspects of the PRS process — what has worked and what had not, and how the process unfolded over time. While it is a little too early for a conclusive evaluation after only five years of implementation, it may be worthwhile at this stage to examine to what extent the basic procedures are being implemented and basic goals met, and to explore prospects for its future development.

(1) Overall results of PRS implementation

Only a few people may disagree with the observation that overall implementation of the PRS process to date shows that it has not delivered what was initially expected. As the review conducted by the World Bank and IMF in 2002 has already suggested, it was increasingly clear in the 2005 Review that the PRS process is generally a major challenge for low-income countries.

The 2005 Review suggests that inadequate capacity for analysis and organization, which is the crucial element for the PRS process, prevails in these countries. The process requires assembling integrated medium-term goals and monitoring the PRS, complete with short- and long-term goals and monitoring systems — “a set of tasks that few industrial countries could systematically do well.” In fact, low-income countries are obliged to create them with limited technical and institutional capacity, and simultaneously reinforce national institutions, processes, and governance systems. Given the situation in low-income countries, and appreciating the magnitude of endeavors by some governments, we must be realistic and recognize that progress will be gradual, and therefore there is less possibility that this vital prerequisite will be fulfilled in the medium term. Recent evaluations thus reveal one of the root causes of problems and underline the gravity of capacity building for the public sector in the PRS process.

The policy implications of evaluations are enormous. Now that the PRS approach has become widespread, particularly in African countries, and has become the basic framework of country ownership and donor alignment, the proper implementation of the PRS approach is crucial for African development. Although the PRS approach will proceed in medium- to long-term per-

spectives with only gradual improvement, enough time is not left for African countries. Scaling-up development efforts with expanded resources will soon start. Improved functioning of the PRS process, including establishing effective growth strategies and production sector strategies, is urgently required.

(2) The most unsatisfactory aspect of implementation — country ownership

The foremost core principle of the PRS approach is that it must be country-driven and owned as a broad-based participatory process. Country ownership is important in terms of evidence-based decision making. Deficient in many countries, however, is a focus on the need to frame clear development goals and targets, link these to budgets and effect public financial management, and monitor implementation to facilitate adjustment of policies and programs.

On the other hand, donor alignment and harmonization have progressed considerably, catalyzed by the PRS approach, although it is still below the level of what it should be. It is common that new or more closely coordinated donor groups have been created, and donors are moving away from project and programs toward more upstream modalities such as sector and general budget support.

Unsatisfactory implementation is diverse. First, when PRSs lack operational details and fail to reach prioritization and specificity for such reasons as a lack of analysis and capacity, unwillingness to make tough policy choices across competing demands, or an inadequate medium-term plan, the notion of donor alignment becomes illusory. Second, the lack of specificity in PRSs gives rise to ‘derivative products’ such as a performance assessment framework (PAF), which is designed to help facilitate PRS operations and donor alignment. Third, interventions by external stakeholders to fill analytical gaps often outweigh country ownership of that analysis or capacity, and tend to diminish country ownership in the PRS process.

(3) Missing key function of a PRS — to promote changes

The 2005 Review touched upon the important characteristics of a PRS. The approach comprises a set of principles and actions that affect the environment in which policy is formulated, and promotes changes in many areas rather than constituting a clearly defined set of activities.

To promote change in many areas may, in our view, be the key function of the PRS approach. As Booth (2005) is cited in the latter part of this chap-

ter, proper functioning of the PRS to allocate resources and to provide incentives to government is facilitated by an enabling environment with a reformed trustworthy budget process, presence of sector working groups, incentives in the public service, and other measures. The other side of the coin, is that when the PRS begins in a low-income country where such an environment is largely not in place, it stimulates changes toward fostering such an environment.

In this respect, the 2005 Review also confirms various connections between processes that constitute the PRS. More precisely, countries that have close links between their PRS cycles and their budget process make faster progress in prioritization. Linking the PRS to the budget and mid-term expenditure framework (MTEF) has been more successful where planning processes already existed and budget reforms were underway. Further, MTEFs and sector strategies can be mutually reinforcing.

One key question is to what extent relevant reforms that promote change have been successful in countries where a PRS is underway. While the question is closely related to the political economy in each country, the answer is generally not positive.

(4) Limited success in involving an entire government in the PRS process

Earlier reports from the World Bank and IMF (2003) describe a not unusual story that a PRS unit was isolated from other government departments and operating as an enclave. As noted in the ODI report, it is widely held that in many countries line ministries and local governments have not been actively engaged in the PRS process. In typical cases, limited departments of the government such as the PRS unit and Ministry of Finance, along with some line ministries such as the Ministry of Health and Ministry of Education mainly deal with the PRS.

Some involvement of the entire government, however, is clearly essential for successful implementation as well as improving the PRS quality. Without cooperation of line ministries, analytical and organizational work required for the process cannot be pursued adequately. For example, it is difficult to set goals and targets, link goals and targets to clear public actions, and formulate growth strategies and productive sector strategies.

The causes of the failure referred to above appear to be structural. ODI reports that incentives for line ministry engagement in the PRS process are often negative, because both officials and ministers fear loss of control over

sector priorities, targets, and indicators, as well as a reduced share of donor funding if they move project and programs to the national budget. Moreover, donors themselves reinforce these disincentives to national ownership by maintaining large sections of their portfolios off the national budget.

The prevailing practice in donor coordination suggests that many donors may find advantages in participating in a sector-wide approach only in limited sectors such as education, health, local roads, and in some cases, agriculture. In other sectors they may wish to continue traditional type of cooperation. In other words, many of the host governments and donors may take it for granted that the PRS process focuses on social sectors rather than rural issues or infrastructure, not to mention production sectors.

If host governments and donors maintain their mindset, the PRS approach will continue with substantive organizational weakness.

(5) Prevailing incompetence in growth strategies and production sector strategies

Results of the review indicate that growth strategies and production sector strategies are extremely weak in PRSs. The ODI Report attributed relative neglect of the production sectors to a number of factors — important analytical gaps remain in defining how development interventions can best contribute to pro-poor growth, and underlying policy processes in the production sectors are often particularly weak. The 2005 Review also states that while many PRSs were intended to incorporate production sectors, most have found it challenging to do so, and treatment has tended to be less detailed than for social sectors.

Strategies for pro-poor growth, along with social development, are two pillars of PRSs. Against this background, particularly at an early stage, not so much attention was paid to growth strategies as to social sectors. According to the 2005 Review, it is only in recent years that countries are increasingly making growth a central element of their PRS. However, the quality of PRS growth strategies varies considerably from country to country, and much of the discussion related to growth pillars has remained qualitative, with less specificity about policy and institutional reforms. The 2005 Review concluded that improved growth analytics are needed at the country level.

Incompetent growth strategies and production sector strategies are among the typical weaknesses observable in the PRS approach.

9-4. PRS approach and politics

Development strategies are fundamentally a political agenda. Core principles of the PRS, such as ownership, medium- to long-term perspective, comprehensiveness and partnership orientation are closely linked to state effectiveness. Recent international development trends have recognized the importance of political systems as a key factor in the success or failure of poverty reduction.

9-4-1 PRS is accepted locally: An example

Because of its link to the HIPC initiative and IDA concessional lending, many countries perceived the PRS approach as an externally imposed requirement. Its origin also tends to be viewed as largely technocratic. Under this circumstance, it was totally unclear whether political leaders and constituents would be interested in supporting it. The 2005 Review refers to Zambia, where the PRS process that was initially viewed as externally imposed gained domestic currency, with wide participation by civil society and the general public. Understanding the political economy that determines how the PRS process unfolds is important, according to the 2005 Review.

9-4-2 Politics and the PRS approach

The Overseas Development Institute, London (ODI) and Department for International Development (DFID) are jointly undertaking an in-depth study about the PRS and political processes. How well the PRS functions to allocate resources and provide incentives within government is influenced by several factors (Booth, 2005). These include presence of sector working groups that set priorities and guidelines; a reformed budget process that is trustworthy, based on policy objectives, and linked to the PRS by definite criteria and procedures; and appropriate incentives in the public service and local government that enable capacity to develop in a positive way. Booth also said that any improvements in these areas help a PRS to give new direction to country efforts, and existence of a PRS, in turn, motivates better sectoral policy thinking and reform of public financial management. However, lack of political buy-in affects all of these processes negatively, and the reforms needed to give real life to the PRS may suffer.

9-4-3 Case studies on politics and PRS approach

ODI also conducted four country case studies on politics and the PRS

approach (Piron, 2004). As background to the research, she cites two contrasting visions behind the PRS approach. One perspective is that the PRS is viewed as offering a potentially transformative agenda of pro-poor reform, and providing opportunities for national governments to become more committed to pro-poor policies and for donors to work more in line with country-owned priorities and processes. In the alternative perspective, the very fact that the PRS approach is being led by donors is seen as predisposing it to have a negative effect on national political development.

The two visions are not so opposite and many would agree that incremental progress is possible through the PRS approach but at the same time are aware of the challenges involved in the consistent implementation of pro-poor policies (Piron, 2004).

Case studies in four countries (including Uganda) suggest that pro-poor change is possible but that change is largely incremental. Examples of incremental progress include improved policy making through more intra-governmental coordination, and a gradual opening of the policy making process in each of the country. Piron concludes by emphasizing the overwhelming importance of context, and that historical considerations play an important role in shaping the possible reach of the PRS process and determining what can reasonably be expected. It is essential to understand both the 'political momentum' and the medium- to long-term 'drivers of change'.

It is worth noting that the case study finds pro-poor changes are largely incremental. This may represent a potentially negative aspect of the political context in which the PRS process operates.

9-4-4 'Drivers of change' approach

Endeavors of DFID and ODI to explore the PRS and its political context have led to research defined as the 'drivers of change' approach.

If donors are serious about working to support poverty reduction, they must increase their understanding of the political context in countries where they work. The drivers of change (DoC) approach is intended to be an innovative attempt to address this challenge. The starting point of the DoC approach is that donors know what is necessary to realize MDGs and widespread poverty reduction, but they don't know 'how' to bring about the necessary changes. The DoC approach therefore advocates close examination and analysis of country context with a specific focus on how change is occurring within the country, in other words, what is driving change.

The DoC approach has been developed over the past few years, and more

than 20 offices of DFID and ODI have carried out DoC work. Although the effects of this work on poverty reduction are yet to be ascertained, engagement with a political economy approach is bringing insights for programming and internal work methods in DFID.

It is interesting to note that the DoC approach is interpreted by ODI as a part of recent trends in development assistance in seeking the reason for failure in development assistance in historical context. Aid donors have been moving ‘upstream’ in their approach to aid and poverty reduction. In the 1990s the predominant form of aid was projects, which has now progressively changed to programs, policies, institutions, and most recently, to a focus on politics.

At this stage, the DoC approach has just started. We will continue to see how it will develop.

9-5. Capacity development of the public sector in African countries

Earlier in this chapter we discussed the inadequate capacity for analysis and organization that prevails in low-income countries and is a constraint to advance the PRS process effectively, and to scale up development efforts by expanding assistance. The underlying reality is that “capacity is a critical element in addressing Africa’s problems” (World Bank, 2005b). This recognition may stimulate our interest in two respects — how capacity development of the public sector is proceeding in African countries, and how capacity is developed effectively. Directly relevant to these questions are two reports from World Bank that were made public in 2005.

9-5-1 A report on assistance for capacity development in Africa

A World Bank document has reported on capacity building interventions in Africa (World Bank, 2005c). Between 1995 and 2004, the Bank provided \$10 billion, mainly loans to support a wide range of capacity building interventions in Africa. Most of the loans were directed to public sector capacity building. In 2005 the Bank’s Operations and Evaluation Department (OED) independently assessed the relevance and effectiveness of Bank support for public sector capacity building in Africa during this period. The major findings include:

- The international development community, including the World Bank, has traditionally treated public sector capacity building as a collateral

objective — a by-product or instrumental measure to advance near-term project outcomes rather than as a core goal.

- The Bank has not yet established a knowledge base and guidance for capacity development.
- Most support for capacity building in country programs remains fragmented and is designed and managed project by project.
- Where technical assistance formerly filled gaps in skills needed to manage Bank-funded projects, it has had little impact on strengthening capacity.
- The Bank's success in enhancing the performance of the public sector varies across sectors as well as countries. Support for capacity building in the roads sector has been most successful. The health and education sectors face greater challenges because they are labor intensive and decentralized, and rely on numerous dispersed frontline service providers.
- While strengthening public financial management has been a centerpiece of national economic reform agendas throughout Africa, the Bank's support for capacity building in this area has encountered considerable difficulty.

These conclusions underscore the importance of approaching capacity building in Africa as a core objective ensuring that support is country-owned, result-oriented, and evidence-based. The challenges in improving public sector performance in Africa necessitate a priority focus and processes that encourage long-term, systemic efforts.

Recommendations

The report recommends that the World Bank, among others, strengthen its knowledge base and amplify its framework for public sector capacity building to help countries better:

- prioritize capacity-building activities and donor support;
- link institutional, organizational, and human capacity development together; and
- transform traditional capacity-building tools to improve results.

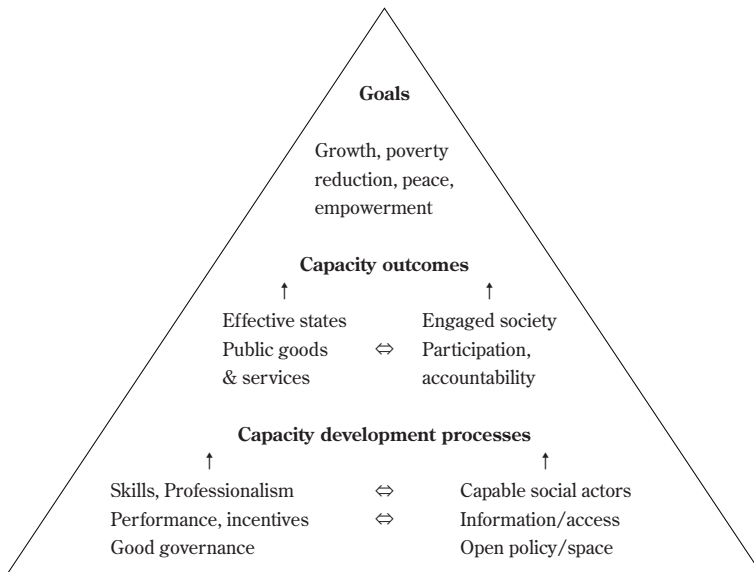
The review suggests that capacity development, particularly in complex areas, should produce better outcomes. Especially astonishing is unsatisfactory interventions in public financial management because it is accorded the highest priority in national economic reform agendas throughout Africa.

9-5-2 World Bank task force report on capacity development in Africa

The World Bank Task Force on Capacity Development in Africa, after comprehensive review of more than four decades of evidence, submitted a detailed report on this subject (World Bank, 2005b).

The major thrust of the report is a new model for capacity development for Africa (Fig. 9.1). The new model emphasizes the dual objectives of building effective states and forging engaged societies. Capacity development is a long process of country-centered action that builds on strong leadership with clear visions and strategies. African ownership, commitment, and strong leadership are seen in this model as essential to develop sustainable capacity. Capacity takes root and develops where incentives are favorable, and dwindles when conditions are adverse. The policy environment is fundamental to capacity development, and successful development moves with causal links from processes to outcomes and finally to goals. The processes entail interventions to address weaknesses in human skills, organizational and institutional performance, and overall governance.

Figure 9-1. Capacity development goals, outcomes and processes



Source: World Bank (2005b)

Shared vision of effective capacity development

The report calls for establishment of a “shared vision of effective capacity development.” The shared vision provides a conceptual and operational underpinning for a common implementation platform for development stakeholders. Key lessons toward a shared vision for capacity development include:

- Governance matters for successful and sustained capacity development.
- Capacity development requires an effective state and an engaged society.
- Africans must lead in capacity development and aid management.
- Capacity development should be a core area of country-led development strategies.
- Unleashing, nurturing, and retaining existing capacity is paramount, as is better use of local resource and the diaspora.
- Priority must be placed on country ability to build capacity.
- External stakeholders must avoid capacity-depleting practices such as project implementation units and excessive use of external consultants.

Country development strategies and capacity development

The report reaffirms that capacity development should be a core of country development strategies, however, quite astonishingly, prevailing practice runs counter to this imperative. The 2005 Review on implementation says that the PRS approach has the potential to help countries to better prioritize capacity-building activities and guide support from donors, but this dimension deserves considerably more attention. Some PRSs discuss the adverse impact of capacity constraints on implementation, but PRSs of the vast majority of countries have thus far failed to address this issue in a comprehensive manner.

While capacity is the centerpiece of challenges for Africa, the reality is that it is not properly addressed in country development strategies.

9-6. Strategies to scale-up African development with expanded assistance

With significant financial commitment by donors at the G8 Summit and UN World Summit, donors are taking initiatives to play a role in facilitating an international response to the call for expanded assistance for Africa. Among

them, the World Bank Group has compiled an Africa Action Plan to support policy and public actions led by African countries to achieve well-defined goals such as the MDGs.

Commitments to rapidly scale-up aid also call for its effective use. The 2005 Review deals with a variety of issues relating to scaling-up aid. Some countries in Africa are already heavily dependent on aid, so the issues of absorptive capacity and macroeconomic implications of aid have likewise raised renewed interest among academics and practitioners, and are covered by research papers and reports.

9-6-1 Africa Action Plan

The Africa Action Plan (AAP) intends to provide a result-oriented framework to support African countries in several ways, including building honest and capable states through governance reforms, raising the rate of growth, and enabling the poor and women to participate in and benefit from growth. In addressing Africa's needs in these areas, prerequisites are partnerships at the country, regional, and global levels; greater country and sector selectivity in the design and targeting of interventions; better harmonization and alignment of development partner actions to support country-led strategies; and the establishment of sound monitoring and evaluation systems.

In AAP, the World Bank Group has broadly grouped African countries into four categories, using three criteria: (a) economic performance measured by GDP growth and CPIA governance indicators, (b) progress toward meeting the MDGs, and (c) prospects for effective harmonization of development partners:

- Group A — “countries capable of using more aid quickly across a wide range of interventions” includes Burkina Faso, Ghana, and Tanzania. Outcome orientation is high, donors are well aligned, and more resources can be used effectively and immediately.
- Group B — “countries where selective scaling-up is possible” includes Ethiopia, Mali, and Nigeria. Outcome orientation is moderate. Partners are partly aligned, and additional resources can be used selectively to scale-up programs.
- Group C — “fragile states, where additional aid is likely to be focused on targeted programs” includes Burundi, Chad, and DRC. Challenges include strengthening state capacity, fostering ownership, etc. Scaling-up will be limited to specific targeted programs such as malaria, education, HIV/AIDS, and some infrastructure.

- Group D — “states affected by recent conflict” like Liberia. The focus is on stopping and preventing conflict, and recreating the rudiment of a state.

The selection of countries considered effective use of aid and also reflects the need for donors to respond to constituents who call for effective use of aid or the combination of increased aid and its more effective use. While only a limited number of donors, including the USA and the Netherlands, are explicitly selective, many donors implicitly apply similar policies.

9-6-2 Scaling-up aid

The AAP says that in the face of increasing resources, one major task for countries is to strengthen the analytical foundation for scaling-up results. The PRS process has drawn attention to the strong links between policies and programs and poverty-related outcomes, including growth. It has underscored the need for more country-specific analysis of these issues, including poverty analysis and growth diagnostics that put more emphasis on production sectors. The AAP also recommends that development partners should continue to help countries to address analytical gaps, but recognizing that priorities vary from country to country.

The 2005 Review considers several factors to be considered when scaling-up with expanded assistance using findings from the PRS process. It suggests that the PRS approach can be used effectively as a framework for scaling-up aid because there is tension to be resolved between the PRS that provides a realistic framework for day-to-day policy implementation and one that maps out efforts and financing required to achieve more ambitious longer-term goals like the MDGs.⁴

9-6-3 Absorptive capacity

Among issues relating to scaling-up aid, absorptive capacity has been considered by the 2005 Review, an ODI report, and other research papers. A high proportion of aid is already noticeable in the GDP of many African countries. Scaling-up aid and increasing its concentration on a limited number of recipients will necessarily accelerate this trend. The effects of aid on macroeconomics was considered by IMF economists Rajan and Subramanian (2005b), who conclude that inflow of aid may bring negative effects on the competitiveness of a country through appreciation of its currency exchange rate.

4. The Sachs Report states that PRSs should be revised so that they are ambitious enough to achieve MDGs.

This was also considered in the 2005 Review and the ODI report.

In summary, scaling-up endeavors for African development with expanded resources involves multiple issues — most central is how to strengthen the analytical foundation for scaling-up results. Strong links between policies and programs and poverty-related outcomes including growth are important processes that should be pursued through effective implementation of the PRS process.

9-7. Summary

9-7-1 New stage of African development

International development for Africa has entered into a new phase, and as aid levels to Sub-Saharan Africa increase substantially, countries are going to increase efforts to scale-up results.

The Sachs Report and African Commission Report advocated that a ‘big push’ was required to achieve self-sustaining economic growth in African countries and called for expansion of aid. The international community responded positively to this recommendation by making a commitment to double ODA. The prerequisite of financial resources is going to be largely fulfilled.

While there will be more external resources available than ever before for development over the medium term, the benefits will not be distributed evenly to all countries. There will be explicit and implicit selectivity to be applied more rigorously, and possible implications for aid dependency in countries that receive more aid. On the other hand, development partners are called on to ensure that pledged resources materialize in ways that are flexible and predictable.

At this new stage of African development, several considerations reflect view in the preceding part of this chapter:

- Countries and their development partners are required to increasingly focus on defining, measuring, and managing development to maximize effectiveness.
- With more resources available, the PRS should provide a framework to scale-up country-level efforts to reach the MDGs.
- Development partners will support critical national policies and public actions to achieve well-defined goals such as the MDGs. The principal means to achieve these goals include governance reform and raising the rate of growth with greater emphasis on production sectors.

Growth strategies, production sector strategies, and infrastructure development need to be more intensively pursued while striking an appropriate balance with social development.

- The PRS needs to address capacity constraints, help countries to better prioritize capacity development, and guide in receiving support from donors.

9-7-2 Roles of the PRS and its limit

This chapter has discussed the role of the PRS in African development and how it has been implemented at the country level. The PRS is also closely related to the political context of a country and its ability to build capacity.

Success of the PRS approach is limited. It has not delivered what was initially expected. Reviews show that country ownership, the core principle of the PRS, proved to be most deficient in the process, a concern that was also heard from Driscoll and Booth. Driscoll (2004) said that “The risk of disillusionment is real, as the (PRS) approach uncovers but cannot immediately transform the enormous legacy of failed aid and poverty reduction efforts over the past half a century.” Booth (2005) said that “To sum up there are sound reasons for wanting more country ownership of poverty-reduction policies. The PRSP experiment has been the ‘only show in town’ trying to address this need for the last five years. It cannot yet to be said that the experiment has failed, if only because no better idea has yet been articulated by anyone. On the other hand, it is clear that PRSPs have not delivered what was hoped for.”

The fundamental cause of the limited success, in our view, is that the PRS approach apparently has grown into a system that is too large and too sophisticated for low-income countries to manage effectively.

Too large

The PRS approach comprehensively covers the broad area of almost all government activities. It includes numerous complicated procedures, many of which require a massive amount of work. Procedures function as a set, and because they are linked, any delay, failure, or absence of one procedure may affect others. For example, when poverty monitoring is not set in operation, there is no feedback to planning and policy formation. Most of its procedures, including PRSP, progress reports, PER, MTEF, and poverty monitoring are in addition to the existing system and practice. It is not a one time heavy workload, but a daily routine that continues perpetually. It is very chal-

lenging for low-income countries to deal with the whole range of such procedures using a limited workforce. Even countries such as Burkina Faso, Ghana, and Tanzania that are making best efforts to advance the PRS process in good faith cannot adequately deal with many of the procedures.

Too sophisticated

Implementing the PRS process requires a high level of analysis and organization. The 2005 Review admits that requirements of the process such as putting together integrated medium- term goals and monitoring a PRS, complete with short- and long-term goals and monitoring systems are “a set of tasks that few industrial countries could systematically do well.” It is therefore very natural for countries to make only slow progress in the PRS process.

Real challenge begins at the planning stage. The 2005 Review suggests examples of sub-standard PRSs that don't support evidence-based decision making. Many of the countries apparently face challenges at the threshold of the PRS process in terms of setting concrete targets to policy goals, linking development programs to these goals, prioritizing policies and public actions, etc. A higher level of procedures such as effective national monitoring evidently looks out of reach for most of the countries.

In an overwhelming majority of countries, ownership of the PRS process — the first and foremost principle — is fragile, and the concept of donor alignment is illusory.

Capacity and a development agenda are dilemmas facing developing countries. Normally countries must address both issues simultaneously because they don't have time to wait for their capacity to improve in the face of outstanding development challenges. The PRS process, however, exposes the vulnerability of countries.

9-7-3 Future prospects for the PRS approach

If the present situation continues, it will take a long time for low-income countries to develop the capacity to effectively advance the PRS process. Studies on capacity development show that only consistent and long-term endeavors will improve chances for success, but they also show that capacity development is not yet properly addressed in country development strategies.

The situation is grim because the PRS approach is designed to provide a basic framework of country ownership and donor alignment for low-income

countries in Africa. The situation is all the more embarrassing at a time when scaling-up development efforts with increased resources is going to begin.

What will be the fate of the PRS approach? Virtually no effective alternative has been floated in international development discussion. Accordingly, at least for the time being, one possibility is that efforts will be made to compensate for what has not been working in the PRS process. One example is the creation of derivative products such as performance assessment framework (PAF) to complement lack of specificity in the PRS process. Another example is donor intervention, for example, to fill analytical gaps such as drawing sector strategies, monitoring, etc. Such intervention, however, can be a risky venture. Unless carefully designed and supervised by the host government, it may undermine country ownership.

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Final Chapter

Transition to Strategic Aid

Takamasa Akiyama, Yuichi Sasaoka

As Akiyama discussed in detail in Chapter 1, in recent years there have been significant structural changes in the global political economy and in international aid trends. Amidst these changes, Japan as a major donor country is standing at an important crossroads. At the time of this writing, the Japanese government is about to embark on an ODA reform based on a February 2006 report submitted by the Overseas Economic Cooperation Study Group¹. According to the plan advocated, planning will be handled by a newly created Overseas Economic Cooperation Council (tentative name) which will report directly to the Prime Minister. The Ministry of Foreign Affairs has the main responsibility for general policies and all implementing agencies will be consolidated into the Japan International Cooperation Agency (JICA). The authors of the present analysis welcome the opportunity to consider directions for ODA policies and strategies and to discuss priorities at the perfect time, as ODA reform is being considered.

The authors of this book met in November 2005 to discuss editorial policies. In recognizing the movement toward ODA reform, they agreed that it would be appropriate to make bold and strongly reform-oriented recommendations. They decided that each of them, in his/her specific chapter, would insist that Japan continue to play a leading role in the new aid trends, and that Japan should implement bold reform while taking advantage of and reinforcing its traditional strengths and addressing its weaknesses. These issues are connected to a series of changes including clarification of the main objectives in overall strategy, moving away from aid based on modalities (and organizations) and reconsideration of relationships between policies and implementing agencies. A critical look at past Japanese ODA reveals that its implementation tended to be inward-looking, emphasizing accountability to

1. Mainichi Shimbun (Newspaper) March 2, 2006 morning edition.

the Japanese people along with acquisition and maintenance of budgetary resources. Evaluations tended to center on monitoring processes and minimizing criticism. If these conditions are retained, Japan may be unable to obtain strategic advantage in the field of international development aid which poses increasingly complex challenges. All the authors share this impression and regard this reform crossroads as an occasion to take a fresh look at ODA policies.

A simple perusal might prompt some readers to think that this book is structured to provide discussion of different aid modalities. Admittedly, the structure is based on the current aid system. However, a careful reading will reveal that each chapter proposes a perspective extending beyond modalities. Poverty reduction strategies in Africa (Chapter 9), the private sector (Chapter 8) and human security (Chapter 7) are discussed as important topics. Among these, the central role is currently played by poverty reduction strategy (PRS). The private sector role emphasized is as an axis for higher income regions, for lower income regions human security is emphasized². Aid modalities and topics are related to each other, and they are supported by the basic principles at the core of PRS such as ownership, partnership (Chapter 3), participatory development and results orientation.

What are the common threads that run through the book? Six are articulated. First, each author proposes to reform modality-based schemes and implement aid unfettered by them. Miyoshi (Chapter 6) states that JICA's Regional Departments and theme-oriented organization offers a foundation for building a cross-scheme system. If yen loans and grant aid are incorporated into JICA, this will entail huge organizational changes but it will also provide a perfect opportunity to give substance to program assistance, turn schemes into means, and promote local initiatives, partnerships and aid coordination. Moreover, with regard to aid modalities, as Sasaoka and Nishimura (Chapter 3) and Ohno (Chapter 5) suggest, restrictions on the donor side should be reduced and a system built that can provide more demand-driven aid.

On this point, the authors would emphasize the importance of future regional or country-based budgeting and the promotion of country-specific and thematic approaches based on that budgeting. Traditionally, operational budgets are first divided into the three modalities of yen loans, grant aid and technical cooperation; then regional and country distribution is determined

2. Of course, these areas overlap with and complement each other.

within each modality. The total amount of aid for a country is determined by aggregating the amounts of aid per modality. In the future, after some trial and error, the system should be modified so that regional and country planning comes first and selection of aid modalities and modality-based distribution take place within that framework. This will clarify the policy system of development aid and bring a totally different process to the government and implementing agencies.

The second common thread is the importance of having a clear development strategy scenario for both the whole of ODA and the development scenarios of recipient countries. Traditionally, regional and/or country aid policies are formulated first, followed by the selection of sectors, programs and projects. In the future, there must be well thought-out development strategies at the regional or country level which will be followed up by priority sectors and program selection. In order to analyze these development strategy scenarios, research functions within the government and implementing agencies should be strengthened and collaboration with universities, think tanks, research institutes and consultants should be enhanced. With regard to development assistance activities in recipient countries, the program approach must be an essential feature and comprehensive capacity building for existing organizations and technologies must be emphasized (Chapters 5, 6 and 9).

In their attempt to implement the PRS as the central objective of today's ODA, the economic growth school emphasizes the private sector while the BHN (basic human needs) school emphasizes human security. With regard to bi-directionality between these two views, Sasaoka and Sugano (Chapter 9) talk about the significance of a "mixed strategy" that combines broad-based growth and pro-poor targets. Of course, the actual mix would vary depending on the country and sector. What to emphasize in the best mix would be decided on a case-by-case basis. For this reason, each donor should work with the recipient government and civil society to create a country assistance plan based on policy dialogue and penetrating analysis of current conditions. For its part, Japan needs a system for examining its comparative advantage and demand and supply conditions to determine aid amount, sectoral distribution and governance guidelines, etc.

Ohno's "argument for bisecting ODA" (Chapter 5) charts future direction of ODA from a regional/global perspective. This argument is not about creating two aid systems that act as fundamental pillars as is the case in the US, rather it presupposes two concepts as criteria for clarifying the thinking and

as a reference framework. Of course, the categories of middle income and low income countries are not simply congruent with Asia and Africa, respectively, and needs-based categorization is not simple. However, it would be important for Japan to have a regional criterion for regional contribution to East Asia, and a global criterion for support of the poorest countries wherever they are. The authors suspect that sorting out the problems of developing countries based on their growth stages and important issues will help clarify the strategies as well as the roles of infrastructure (Chapter 4) and the private sector (Chapter 8).

The third common thread is the demarcation (sorting out of corresponding relations) between policy ministries and implementing agencies. As the outlook for cross-scheme aid has become brighter, there is now a possibility that implementing agencies can fully handle the planning and implementation of program-based aid activities. While not discussed directly in this book, this has something in common with Shimomura's (Chapter 2) perspective of local initiatives and respect for those in the field as well as Sasaoka and Nishimura's (Chapter 3) perspective on Organization Theory. Under a cross-scheme policy environment, implementing agencies and people in the field will be able to make more suggestions about the progress of program assistance and how to improve aid modalities. Local ODA task forces will be given larger roles to play and become more active. For their part, policy ministries would focus on genuine policy areas and on establishing objective evaluation and monitoring systems. They would also discuss among themselves how to address the issue of policy coherence which is required of DAC member countries as part of a broader development policy that extends beyond aid.

To sort out the relationship between policy and implementation, objectives and missions must be clarified. Instead of having multiple and parallel objectives, once an overarching objective has been established within a consolidated organization, lesser or subordinate objectives should be aligned with it and stressed within the evaluation system and organizational communication structure. If links among different objectives are not stressed sufficiently, a subordinate objective may interpret itself as the overarching objective or as an independent objective and begin to function independently. This is discussed by Miyoshi (Chapter 6) from a policy systems perspective and by Ojima (Chapter 4) from an aid effectiveness perspective.

The fourth thread is the importance of active participation in the aid coordination regime built around the PRS, and of having simultaneously a self-

identity. This is related to the contrast in the manner of discussion between Shimomura (Chapter 2) and Sasaoka and Nishimura (Chapter 3). Based on understanding among the authors, consideration of the “dark side” of the PRS regime in Chapter 2 and promotion of partnerships in Chapter 3 intentionally illuminate the same subject from opposite directions. The dark side aims to reconstruct an aid stance unique to Japan; the promotion of partnerships aims to expand the existing aid philosophy. By integrating these, the authors are establishing a rationale for an aid stance on the basis of which Japan would actively participate in the PRS regime and partnerships while cognizant of its dark side.

The fifth thread is the formation of donors’ viewpoints on aid strategies and programs. Makino (Chapter 7) and Ojima (Chapter 4) are trying to reconstruct them from the perspectives of human security and infrastructure, respectively. The former recognizes that as the aid emphasis shifts to PRS and human security, the perspective from the bottom gains importance, and it attempts to formulate a solution for the poor in three time-based stages. The latter offers a scenario wherein private funds, loans and grant aid are phased in and out depending on the growth stage of each country and where programs and modality-based activities at any given time are changing. A perspective that positions projects within the program regime of the recipient country is of course important to a shift to a program approach. This is related to the development scenario mentioned above in discussion of the second common thread.

The sixth thread is working with private resources discussed by Kuga, Aoyagi and Akiyama in Chapter 8. This is especially relevant for the infrastructure building discussed in Chapter 4, and is also related to regional contributions mentioned in Chapter 5. The experience of East Asia suggests that development by ODA has clear limitations and that success depends largely on how well the private sector is engaged. This is true also for regions other than East Asia, including Africa. However, current conditions in Africa and some other regions are not conducive to private sector activities. Thought will have to be given to the building of an environment in which donors and the private sector of the recipient country can cooperate.

The essence of the strategic stance to be inferred from this book, and which takes into consideration the comparative advantages of Japanese aid, is to provide aid that contributes to long-term self-help efforts of developing countries. This is a stance that Japan has long emphasized and it means that developing countries promote poverty reduction through true ownership and

achieve long-term economic growth. Ultimately, Japan's contributions may be limited to supporting a few least developed countries over the long term so that they will be able to sustain themselves economically. In such cases, it will be necessary to analyze institutional issues including political systems and factors of poverty reduction and economic growth in these countries, and to work with governments to construct long-term development strategies under an "all-Japan" system that includes the private sector. This, it must be understood, will take years, and decades.

Under the new system to be formulated, comprehensive aid with policy coherence may become possible. In general, a new development strategy presented to the world must be backed-up with world-class theories and analyses. Also it will be desirable to engage actively in discussions with other donors. Japan has never been in complete accord with international aid trends, but has acceded to them in principle because the theoretical and analytical grounds for its counterarguments have been weak. Under the new aid system, it will be important to strengthen the theoretical base and to participate seriously in debate over international development strategies. The authors would be highly gratified if their book could contribute to this process.

Finally, it is important that a secretariat charged with strategizing ODA report directly to the Prime Minister. As Akiyama stated in Chapter 1 and according to lessons learned during the Cold War era, it is unwise to allow aid to become subservient to other objectives and to lose sight of its true objectives. ODA should not be considered in the context of a "clash of civilizations" but in the context of a global development strategy. Its overarching objective must be clearly expressed in the mission statements of governments and aid agencies. Japanese ODA, along with other policy tools, should be used effectively in line with the Japanese government's diplomacy to ensure peace and prosperity in the world. This belief is shared by all the authors of this book.