Aid Review: Open for business

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Reading through the Independent Review of Aid Effectiveness it is hard not to feel something of a sense of awe: 353 pages of detail on the state of Australian aid coupled with considered advice on how to improve the aid programme. The review is scholarly and sound, and full of information, not just on Australian aid but also contemporary development thought. Many of its recommendations are excellent and most of them are at the very least defensible.

Given all this it feels somewhat churlish to focus a blog post on what I believe the review has gotten wrong. But good policy development requires debate and so, in the spirit of debate, in today's blog post I am going to take issue with one aspect of the review: its analysis and recommendations regarding AusAID engagement with the private sector (sector F in Chapter 11 - staring on page 224).

My concerns aren't so much that the section is flat out wrong but rather that it inadequately problematizes what is actually a distinctly difficult area for an aid agency to engage in.

The case made by the review for aid programme engagement with the private sector as a driver of development is a familiar one. Through fostering innovation the private sector contributes to productivity growth, which brings with it rising GDP and raised levels of welfare. Similarly, when set amongst well-functioning institutions and competitive markets private firms, thanks to the magic of invisible hand, contribute to the efficient allocation of resources. If the aid programme can help the private sector in this, it follows that it will be helping improve development outcomes.

This is all true as far as it goes, but it's only half the story. In addition to contributing to development in the ways outlined in the report, both domestic and international firms have also in many instances delayed or distorted it. From companies that have taken advantage of natural monopolies to price safe drinking water out the reach of the poor to international logging firms that bribe politicians to ignore environmental regulations, private enterprises have done considerable harm in developing countries at times. These negatives don't mean that the positives don't also exist -- the private sector really does have a lot to offer development. But harnessing this in the weak institutional environment of most developing countries is not necessarily easy, and here the report would be far more convincing if it explicitly acknowledged this.

The report also highlights the potential for corporate social responsibility and inclusive business models to maximise the positive development impacts of private firms, in doing so making the case for more aid support in these areas. Once again this isn't wrong per se. There is certainly some potential for CSR type work to help improve development outcomes. But there are also risks. In particular, corporate social responsibility can end up being little more than marketing spin designed to improve companies' images. This isn't inevitable but the risk is real enough and the report would have been better had it explicitly mentioned it.

Having covered the pros of the private sector the review then outlines AusAID's current engagement, suggesting that it is inadequate, before making recommendations on how improvements could be made. Four recommendations are made (p 229), one to do with support for corporate social responsibility, the other three all in some way to do with increased AusAID engagement with the private sector.

Development is a complicated endeavour filled with numerous different actors, and it stands to reason that increased engagement is almost always a good thing. So in recommending engagement the review isn't entirely wrong. But it also neglects the elephant in the room: throughout its history aid has been tarnished by episodes where money ostensibly devoted to helping the poor has been captured by domestic interests in donor countries and effectively used as a subsidy. It's no mystery why this occurs; the answer is simple political economy. The impacts of aid are felt far away by people who can't lobby politicians in donor countries. On the other hand the private sector in donor countries can lobby and often does. In a head to head match-up between poor people in faraway lands and powerful political lobbies in donor capital cities the poor don't often win.

Obviously, the risk posed by domestic business lobbies targeting aid doesn't mean that AusAID should never engage with Australian firms but it does make increased engagement problematic. And before I'd be comfortable recommending it I would want to hear a lot about just how engagement could be managed in a way that reduces the risk of aid capture. Yet the report doesn't cover this at all.

Instead, on page 227 the authors of the review concur with a submission from the group Businesses for Millennium Development:

> "AusAID's engagement with business and the private sector has been constrained by a risk–averse attitude within AusAID to engaging with business groups and private sector initiatives."

As I said at the beginning of this post, the review is an excellent document full of much that is useful and right. But in the case of private sector engagement, if I were advising AusAID I would stress a much more cautious approach.

If the risks are real, there is nothing wrong with being risk averse.

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