Eastern and Western Ideas for African Growth

Diversity and complementarity in development aid

Edited by Kenichi Ohno and Izumi Ohno

Routledge-GRIPS Development Forum Studies

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The West and the East approach economic development differently. The Europeans and Americans stress a free and fair business climate, promoting private activities generally without picking winners, and improving governance. East Asia is interested in achieving concrete results and projects rather than formal correctness, prioritizing a few sectors for industrialization, and eventual graduation from aid. The West mostly shapes shifting strategies of the international donor community while the East has, in reality, made remarkable progress in industrial catch-up. The two approaches cannot be merged easily but they can be used in proper combination to realize growth and economic transformation.

This book proposes more dialogue and complementarity between the two in the development effort of Africa and other regions. In this collected volume, contributed by experts and practitioners from both East and West, the need to introduce Eastern ideas to the global development strategy is emphasized. Analysis of British and other Western donor policies is given while Japanese, Korean, and other Asian approaches are also explained with concrete examples. The concept of governance for growth is presented and the impact of rising China on development studies is contemplated. The practices of industrial policy dialogues and actions assisted by East Asian experts are reported from Tunisia, Zambia, Ethiopia, Rwanda, and others.

The book should be useful and inspiring for all donors, institutions, NGOs, and business enterprises engaged in development cooperation.

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Contents

Figures

Tables

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Preface

This book was born out of our desire to link two different strands of development thought, the one in the East and the other in the West, for synergetic cooperation in development assistance. Global development strategies, sponsored by international institutions and meetings and evolving fairly rapidly over the years, are mostly informed and driven by Western development ideas. Meanwhile, policy orientations of the Far East and Southeast Asia, which are less clearly articulated in words but practiced widely and often with remarkable results, approach the politics and economics of national development from a different angle. These two strands are aware of each other, but mutual understanding is not deep enough for constructive learning or creation of something new from the best of each. Sometimes there is even emotional rejection against each other which prevents further cooperation. We do not recommend or foresee the possibility of a merger of the two; they should remain separate and retain their unique features. But honest and serious dialogue and joint work in conducting development projects between the two should be promoted. With this book we would like to partially fill the knowledge gap between East and West.

In undertaking this project, we, the Japanese researchers, found ideal partners in the aid circle of the United Kingdom, where government, academia, and civil society worked together to generate policy activism. The National Graduate Institute for Policy Studies (GRIPS) in Tokyo cooperated closely with the Overseas Development Institute (ODI) in London to produce this volume. However, bilateral discussion quickly spilled over to other countries. We were delighted to also invite experts working in Korea, Malaysia, Zambia, Tunisia, Uganda, and Rwanda to share with us relevant perspectives from their development experiences.

This book was initially compiled as a non-commercial policy report in 2008, the year in which Japan hosted the G-8 Summit meeting and the Fourth Tokyo International Conference on African Development (TICAD IV), as well as the year in which the Japan International Cooperation Agency (JICA) was restructured to assume greater functions as an aid agency. This book was offered as an intellectual input to these events and circulated to the leaders, officials, and experts in charge of economic development and international cooperation, especially those from Africa.

In July 2008, we had the privilege of presenting the previous version of this book to Prime Minister Meles Zenawi of Ethiopia, at the African Task Force meeting in Addis Ababa hosted by Professor Joseph E. Stiglitz of the Initiative for Policy Dialogue and supported by JICA (see Noman et al. 2012 for discussions in this meeting). Mr Meles took great interest in our work, especially the chapter on how Japan transferred the pragmatic method of quality and productivity improvement to Tunisia (Chapter 8 of this volume). This resulted in the official request of the Ethiopian government to Japan to replicate a similar project in Ethiopia, as well as to start regular industrial policy dialogue between the two countries. As of 2013, the quality and productivity improvement project, which we call *kaizen*, and the bilateral policy dialogue conducted by GRIPS and JICA, continue into their second phases in Ethiopia.

We were also confident, however, that the book contained ideas that were useful beyond the events in 2008. Moreover, the principles advanced here should be applied to all government officials, donors, enterprises, and NGOs engaged in the task of development and should not be confined to cooperation between Japan and the United Kingdom. We have therefore decided to republish this volume, with a new title, added chapters, and revisions and updates to existing chapters, in the Routledge-GRIPS Development Forum Studies series to reach a broader audience.

Chapter 1 presents the basic ideas of this volume. Chapters 2 and 3 review the Eastern and Western ways with Japan and the UK as focal donors. Chapters 4 to 6 discuss shifting development visions and introduce *growth-enhancing governance*, a concept that may help to bridge the gap between the East and the West. Chapters 7 to 11 go into concrete details of particular countries and give examples of how the East approaches industrial policy problems. We hope that some of these chapters will interest the reader and serve as entry points for objectively evaluating and comparing the two development approaches of our time. We did not impose uniformity in style or terminology on our diverse authors, which range from renowned academicians to experienced practitioners. The reader will surely see that, collectively and ultimately, all chapters speak in one voice despite the different backgrounds from which they arise.

We thank all contributors to this volume exceedingly. We are also grateful to the JICA, the Japanese Ministry of Foreign Affairs, and the British Department for International Development for giving us opportunities to try and present our ideas and exchange views. The responsibility for content is borne by the author(s) of each chapter in their personal capacity.

Tokyo, January 2013
Editors

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1 An overview

Diversity and complementarity in development efforts

Izumi Ohno

1 Introduction

Each developing country is unique. The donor community is also a heterogeneous group. Development efforts should take advantage of these differences instead of suppressing all development strategies and aid instruments into one. Japan and the United Kingdom (UK) are very different donors and, precisely because of that, there is a great potential for productive bilateral cooperation in aid efforts between them.

Global aid trends have changed significantly over time. Even within the last two decades, dominant aid policy has shifted from macro-oriented structural adjustment to poverty reduction with concrete social sector targets, then to a search for a new source of growth. Recently, there has also been strong pressure to adopt budget support and unify aid procedures. In some developing countries, project aid has been marginalized regardless of whether it is integrated into the government's policies and systems. Expenditures on health and education increased greatly at the cost of economic infrastructure. These shifts are often global and driven by the quest for new initiatives and political leadership on the donors' side rather than by customized responses to socio-economic situations in individual developing countries.

This report argues that donor collaboration should follow the principle of diversity and complementarity so as to maximize aggregate aid effectiveness. The idea is a general one that should be extended to the entire donor community although we mainly focus on Japan–UK cooperation in this volume. This proposal is justified by the principles of comparative advantages among donors, non-fungibility of ideas, and inseparability of content and instrument, as explained below.

To be more precise, aid policy and instruments should be partly common and partly different among donors. Donors should be sufficiently common to be able to work together, share long-term goals, and simplify procedures. But they should at the same time retain their natural differences to permit a meaningful division of labor in development efforts. This is so especially because donor diversity has increased significantly in the twenty-first

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century, with a number of former developing countries graduating to the status of emerging non-Western aid givers. With a growing role of the private sector in development, the architecture for development cooperation has become more complex. Under this circumstance, it is all the more important to seek an inclusive approach for combined development effectiveness.

At present, rising interest in growth promotion in the UK and Japan's desire to make new contributions in Africa offer an excellent opportunity to strengthen the bilateral partnership. Japan can also act as a mediator in Asia–Africa cooperation by promoting knowledge sharing between East Asia's emerging donors, such as China, South Korea, Malaysia, Thailand, and African countries where the UK has accumulated rich information and experience. Through joint effort, Japan and the UK should concretize growth initiatives in developing countries struggling to take off economically, especially in Sub-Saharan Africa.

This introductory chapter will discuss the importance of strategic and instrumental diversity in development aid, the lessons of East Asian experiences, the main features of Japanese and British aid, and the significance of deepening Japan–UK partnership in the new era of development cooperation.

2 Arguments for strategic and instrumental diversity

The past decades have seen large swings in development vision. After the mostly disappointing results of macroeconomic austerity and structural adjustment programs in the 1980s, the international community began to pay more attention to human, social, and institutional aspects of development, which culminated in a concerted effort to fight poverty. Since the late 1990s, poverty reduction has become an overarching goal for all development assistance to poor countries (Figure 1.1). At the center of this approach was the Poverty Reduction Strategy Paper (PRSP) introduced by the World Bank and the International Monetary Fund (IMF) in late 1999 in connection with the Enhanced Highly Indebted Poor Countries (HIPC) Initiative. Moreover, the United Nations (UN) Group also launched a very important initiative for reducing poverty. Following the UN Millennium Summit in September 2000, the UN General Assembly adopted the UN Millennium Development Goals (MDGs) in September 2001. MDGs and PRSPs are linked as the end and the means of poverty reduction, and have exerted great influence on the development strategy formulation of low-income countries.

Aid instruments have also undergone major shifts. Initially, the lack of capital was regarded as the key resource gap that faced developing countries, and projects were the dominant form of aid delivery until the early 1980s. Subsequently, with the prevalence of structural adjustment programs in the 1980s, the share of program aid increased drastically at the World Bank and elsewhere. More recently, the 1990s saw the rise of new aid modalities—such as general budget support and sector programs—with the introduction of

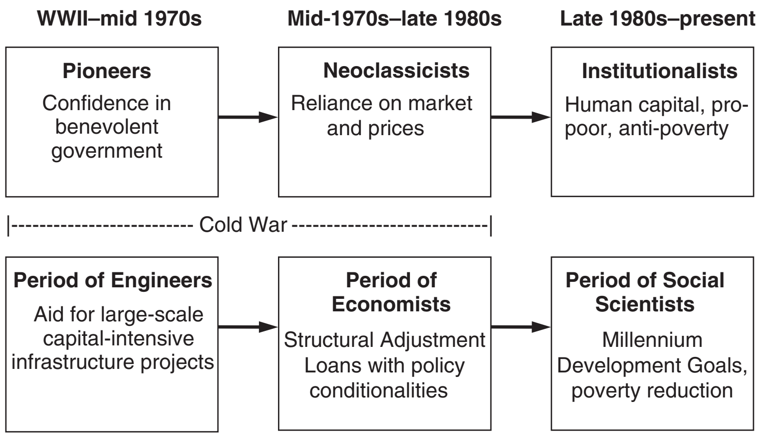

Figure 1.1 The evolution of development ideas

Source: Adapted from Akiyama et al. (2003, p.21, Figure 2).

the PRSP and associated institutional frameworks. As a result, the share of general budget support and sector program support increased from 8 percent of total ODA commitments in 2001 to 20 percent in 2004. Low-income countries received the lion's share (63 percent) of these new modalities in 2004 (IDA, 2007, p.6). This latest move can be regarded as an attempt to overcome the weaknesses of past aid modalities consisting of "stand-alone" projects and structural adjustment programs. Sub-Saharan Africa always took the major brunt of these shifts in aid vision and modality.

What has been common throughout these changes was the tendency for one idea or approach to dominate and marginalize all others. We believe that jumping from one extreme to another jeopardizes continuity and balance. Global convergence to a single idea or approach is neither desirable nor realistic for developing countries or aid donors. While procedural problems caused by excessive aid fragmentation need to be addressed (OECD, 2005), this should not propel us to ignore inherent diversity among developing countries or the heterogeneity of donors. A pragmatic approach should be sought to realize complementarity among different donors to fulfill different development needs.

The principle of diversity and complementarity in donor collaboration can be justified by three overlapping perspectives: (i) comparative advantages of donors; (ii) non-fungibility of ideas; and (iii) inseparability of content and instruments.

2.1 Comparative advantages of donors

Each donor has different strengths and weaknesses relative to others. Comparative advantages in aid can be found in various dimensions such as special technical skills and knowledge, alternative approaches in problem-solving, and visions and philosophy fostered through the historical experiences of individual donors. To take full advantage of this diversity, each donor should mainly work on its comparative advantage and share its expertise with other donors. This conclusion comes from the most basic theory in international economics, which normally explains the benefits of international trade but can also be extended to development aid. If all donor assistance is targeted at one or a few sectors or activities, the policy space for developing countries will become severely limited. The situation where all donors do the same thing regardless of what they can do best should be avoided. But that is exactly the trend that has been observed in the recent past.

Under the strong drive for reducing poverty and the scaling-up of social sector spending in the 1990s, resources allocated to physical infrastructure were sharply reduced (Figure 1.2). The share of social sector spending in total sector-allocable Official Development Assistance (ODA) to low-income countries jumped from 29 percent in the early 1990s to 52 percent in 2000–2004. The shift was most dramatic in Sub-Saharan Africa where the share of infrastructure in sector-allocable ODA fell from 29 percent in the first half of the 1990s to 19 percent in the period of 2000–2004. As most donors have turned away from building roads, irrigation, power and the like, three-quarters of ODA for physical infrastructure for International Development Association (IDA)-eligible countries is now provided by two bilateral donors (Japan and the United States [US], 42 percent) and two multilateral donors (IDA and European Commission [EC], 32 percent) alone.

Lately, there has been a renewed interest in generating growth on the part of the World Bank and European donors. The view that attainment of the MDGs requires further acceleration of overall economic growth is now widely accepted. For example, a World Bank report, *Challenges of African Growth* (2007), points to the serious consequences of long neglected infrastructure investments in many African countries and proposes a big-push solution.

> Two decades of neglect currently manifests itself in the form of huge infrastructure gaps relative to needs in the region and compared with other developing regions. It is estimated that Sub-Saharan African countries need $18 billion a year in infrastructure financing in order to achieve the much higher 7 percent economic growth target needed to halve extreme poverty in the region by 2015.
>
> (Ndulu et al., 2007, p. 143)

While Japan traditionally focused on infrastructure development, its spending on infrastructure in Africa also sharply declined from around 2000. This was due to the Japanese government's decision to suspend new ODA loans, which were the main source of financing large-scale infrastructure, to those countries which applied for the Enhanced HIPC Initiative and

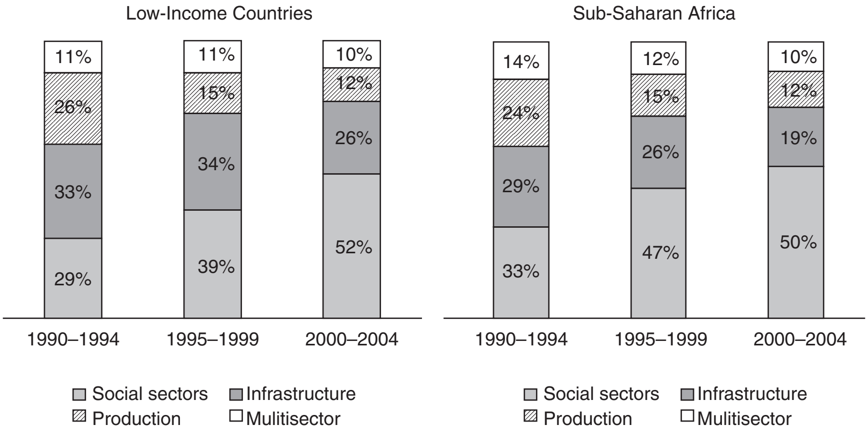

Figure 1.2 Distribution of sector allocable ODA to low-income countries and Sub-Saharan Africa (commitments, period average, %, 1990–2004)

Source: IDA (2007, p.11, Chart 7).

thereby implicitly "defaulted" on previous ODA loans.[1] The proposal report for the Fourth Tokyo International Conference for African Development (TICAD IV) by the African Diplomatic Corps in Tokyo (ADC, 2007, p.7) regretted that Japan's assistance to Africa now had a stronger focus on social development compared to other developing regions. It requested that the "new JICA"[2] devote more attention and resources to the promotion of economic development in Africa. Convergence of Japanese aid policy to the international norm was not necessarily welcomed by recipient countries.

2.2 Non-fungibility of ideas

Policy ideas are often non-fungible even under harmonized procedures. In comparison with money, ideas are more clearly distinguishable even when they are put together. Even if the desirability of a certain policy goal is widely agreed upon, be it industrial competitiveness, systemic transition, or rural poverty reduction, there are many paths and options to reach that goal. Developing countries are diverse in development stage, institutional capacity, and socio-economic structure. Donors can also offer different approaches to the same goal. Developing countries and donors should be open to various possibilities and explore ways most suitable for each case, rather than imposing cookie-cutter molds.

In this regard, systemic transition strategies deserve special attention. In the early 1990s, there was a broad consensus on the desirability of transforming former socialist countries from state-controlled centralized systems to decentralized systems based on price-driven resource allocation.

But opinions were sharply divided on the proper pace and sequencing of policy reforms. The choice between the so-called big-bang approach and gradualism emerged, and heated debates involving donor agencies and prominent economists ensued. The former approach was adopted by Russia, Mongolia, and a number of Eastern European and Central Asian countries with the support of international financial institutions and Western economic advisors. Meanwhile, China and Vietnam, which had initiated transition without external help in the 1980s, opted for incremental reforms. The point here is that superiority of either approach cannot be determined without reference to the inherited political, social, and economic situations of each country. Another important point is that, given each situation, it is necessary to ask whether the country in question adopted the right speed and manner of transition.

A similar situation occurred at the time of the Asian financial crisis in 1997–1998. It was clear that the regional currency run had to be stopped, but there was no initial consensus as to how that was to be realized. The IMF insisted that the crisis countries adopt macroeconomic austerity, raise short-term interest rates, and close bad financial institutions immediately. Others, including the then chief economist of the World Bank, strongly criticized this prescription as totally misguided. Subsequently, the IMF had to admit that its policy package might have been partly responsible for the worsening of the crisis. After the crisis subsided, East Asian countries began to build up international reserves, develop bond markets, and establish a cooperation scheme among regional central banks in order to reduce reliance on the IMF. This event illustrated the importance of availability of second (and more) opinions from which affected countries can choose.

In formulating development strategies, some East Asian countries took advantage of the non-fungibility of policy ideas by listening to a variety of competing advice from different donors before arriving at the final decision. For example, Thailand's experience in implementing the Eastern Seaboard Development Plan (ESDP) illustrates how the country used divergent ideas of Japan and the World Bank to its own advantage.[3]

The ESDP was Thailand's flagship regional development plan aimed at export-oriented industrialization, receiving a high priority in the Fifth (1982–1986) and the Sixth (1987–1991) development plans. It had an unprecedented scale and was composed of a multitude of projects in infrastructure development, industrial estates, urban development, water resources, and environmental management. Nevertheless, the ESDP provoked much controversy at its early phase of implementation. The Thai economy at the time suffered from macroeconomic imbalances caused by oil shocks, global stagflation, and a slump in primary commodity prices. While building modern infrastructure was urgently necessary to strengthen export capacity, the government also needed to adopt stringent measures to cope with macroeconomic crises. The opinions of the two major donors were also divided, with Japan arguing for the timely execution of the ESDP and the World Bank arguing against it. The Thai government assumed full responsibility for steering this process by conducting its own analysis and revising the ESDP. The Thai leadership reached a set of workable solutions and successfully negotiated with the two dominant donors. The fact that Thailand pursued its own way in spite of uneasy relations with the major donors deserves special attention.

2.3 Inseparability of content and instruments

In development aid, content and instruments are hardly separable. Generally, the project approach can address specific problems, seek policy innovation, and implement pilot activities by collectively mobilizing funds, material inputs, technology, and knowledge for well-defined objectives. On the other hand, budget support can provide large resource transfers, including recurrent expenditures, and generate multiple policy and institutional reforms in a synergic manner. For this reason, it is important to match aid modalities with development priorities of each country (Ohno and Niiya, 2004). On the donor side, too, content and instruments are closely integrated. Donors that excel in policy dialogue and administrative reform may find budget support useful. Donors that emphasize field-based process support may prefer project aid as an entry point. Adopting diverse aid instruments to meet different development objectives may at times go against the need for instrumental harmonization. Practical balance should be maintained in reconciling both requirements.

Pritchett and Woolcock (2002) classify public-sector activities according to the levels of "discretion" and "transaction intensiveness." Discretion means the extent to which an activity requires extensive professional or context-specific knowledge, and transaction intensiveness refers to the number of transactions needed to undertake an activity. Noting that services that are both discretionary and transaction-intensive are extremely difficult to deliver, they conclude that a programmed approach is appropriate in areas involving the scaling-up of standardized services, but less so where heterogeneous services are involved. Building on their work, Fukuyama (2004) classifies public services by the degree of specificity and transaction volume, and stresses the importance of taking different approaches in response to the specific nature of targeted public-sector activities.

This idea can be extended to the broader issue of aid modality in general by incorporating different degrees of resource and institutional constraints in developing countries. The Joint Evaluation of General Budget Support (IDD et al., 2006, p.S16) emphasizes the complementarity of aid instruments, noting that:

> [t]here is a serious danger of overloading one instrument, and of expecting it to achieve too many things and too quickly. The appropriate scope and focus of the PGBS [Partnership General Budget Support] instrument can only be decided in country context.

In sum, the right mix of strategic content and aid instruments should be selected to reflect the diversity of development stage, institutional capacity, and socio-economic needs of individual developing countries as well as the comparative advantages of the donors.

More recently, donor diversity has greatly intensified as an increasing number of emerging donors, regional and global programs, and private philanthropic funds are joining traditional donors in offering aid to the developing world.[4] As Menocal and Denney (2011) state, "[t]he donor marketplace is getting considerably crowded," with the emergence of new players that have different aid philosophy and modalities from those of traditional donors. This makes it all the more crucial to make full use of comparative advantages of each player to maximize collective development efforts. Pragmatic eclecticism, rather than dogmatic convergence, is called for.

This point is emphasized in the World Bank report (IDA, 2007), the Paris Declaration for Aid Effectiveness (OECD, 2005), and the latest Busan Partnership for Effective Development Cooperation (OECD, 2011). These documents recognize the challenges associated with the growing complexity of global aid architecture and stress the importance of achieving donor complementarity across national, regional, and global development priorities and programs. Especially, the Busan Partnership for Effective Development Co-operation—the outcome document of the Fourth High Level Forum on Aid Effectiveness, held in late 2011—is notable because it appreciates the diversity of stakeholders involved in development cooperation. As shown below, the document recognizes the differences of the nature, modalities, and responsibilities that apply to South–South cooperation and that to North–South cooperation (OECD, 2011, p.2):

> We also have a more complex architecture for development co-operation, characterized by a greater number of state and non-state actors, as well as co-operation among countries at different stages in development, many of them middle-income countries. South-South and triangular co-operation, new forms of public-private partnership, and other modalities and vehicles for development have become more prominent, complementing North-South forms of co-operation.

Therefore, it is essential for development actors to identify their comparative advantages, and then cooperate with each other to build synergies and maximize combined development effectiveness.

3 The East Asian lessons[5]

The fact that East Asian countries on average grew much faster than countries in other developing regions, including Sub-Saharan Africa, is undeniable, and we naturally look for lessons from these brilliant performers. Japan, as the leading industrial country in that region and itself the first successful non-Western latecomer, is expected to play a catalytic role in transferring East Asian developmental know-how to countries with the willingness to learn. The Japanese government promotes such intellectual exchange directly as well as by encouraging other East Asian high performers to engage in such assistance (the "South–South" cooperation).

However, East Asian experiences mean different things to different people, and some of the "lessons" are not transferable and could even be harmful if applied without care. Let us first enumerate what should not be the East Asian lessons.

First, promoting policy measures adopted by a certain East Asian country in the past to another soil, without regard to historical context or country differences, is hardly desirable, be it Japan's main bank system, Korea's heavy industry drive, or Green Revolution in the Philippines. Doing so would make the same basic mistake as the much-criticized uniform policy conditionalities of international financial institutions. This is not to entirely deny the possibility of replicating some of the East Asian policies in Africa, for example, after careful study and necessary modification to fit the local conditions. But without such preparation, the global marketing of a policy measure that seems to have worked in one country is not advisable.

Second, a strong government dictating private sector activities has not been a universal prescription for success in East Asia. There is a myth among some Western scholars that Japan's high growth from the mid-1950s to the early 1970s was realized through the selective industrial policy of the Ministry of International Trade and Industry (MITI). This myth is easily rebuffed by Japanese business people and officials who actually lived through that era. The common understanding among these people is that private sector dynamism was primary while public policy sometimes played an important but supplementary role. What was surprising about MITI was the effectiveness with which it worked with private firms, learned their needs, and delivered desirable policies. With the possible exception of Park Chung Hee's South Korea, the general lesson from East Asia is that policy tended to fail when it had the upper hand over the private sector. In identifying dynamic comparative advantage, the private sector was the leader and the government was the follower.

Third, the view that an authoritarian state is a prerequisite for economic take-off is too simplistic. True, the majority of East Asian high performers have adopted one form or another of authoritarian developmentalism as a temporary regime to lift the economy from a low base to an upper-middle income level. But again, the mindless copying of this type of regime is very dangerous. For one thing, success hinged on the developmental orientation of the regime rather than its authoritarian ways, which were merely the means to advance development. The dynamics of such a regime, which generally lasts for only a few decades to be replaced by a more democratic regime if development proves successful, should also be recognized. Moreover, it is much harder to install such a regime today in comparison with the 1960s and

1970s when the Cold War was on. Today's developing countries should avoid unnecessary authoritarian elements that are unrelated to growth promotion while selectively importing individual factors that contribute to development. The political lesson from East Asia is a subtle one that requires a more sophisticated assessment than a simple good-or-bad verdict.[6]

If these are misinterpretations, what are the genuine lessons from East Asia that should be communicated to the rest of the world? At the general level, we propose the following three.

3.1 Field-based, concrete thinking

When confronted with any developmental challenge, East Asian officials and aid experts typically start by gathering concrete facts on the ground, absorbing local opinion and knowledge, combining it with the best international expertise, and proposing as concrete actions as possible. In agriculture, for instance, a Japanese consultant may want to stay in one locality to study compatibility among local soil, climate, and crop types as well as the existing structure of the village community and the availability of market access for targeted products rather than drafting a sector development plan for the entire country. In industry, an East Asian advisor may visit a small number of factories repeatedly for six months to talk with general managers, implement 5S,[7] improve machinery operation and maintenance, introduce the just-in-time system, and propose a new factory layout for efficiency (Chapter 7). Such a hands-on approach with profound interest in physical concreteness is in sharp contrast to the framework approach of typical Western donors who are good at promoting procedural efficiency, legal preparation, organizational reform, accounting standards, and the like. Yanagihara (1998) calls the Japanese (or East Asian) way of working on development the "ingredients approach" in contrast to the "framework approach" of the West. The two approaches are different and highly complementary. When the general framework is supported by concrete growth actions, development efforts are likely to bear fruits.

3.2 Development as a holistic social process

For East Asian countries, development is not just a collection of individual problems such as mobilizing savings or improving healthcare. It is an interlinked dynamic process involving all the aspects of the society. Since the economy is embedded in the social structure and political regime, which usually change slowly, every development policy must be designed and executed in full consideration of the social and political constraints of the country in question. From this perspective, a number of attitudes and expectations naturally emerge such as the rejection of naïve free market ideology or standardized policy conditionalities, the crucial role of top leaders in breaking the initial poverty trap, the importance of constructing an "imagined community" for national unity, adopting pragmatic gradualism in political development, and re-interpretation of imported systems in a particular social context. These holistic ideas can be very useful in placing into proper context mechanical views emanating from the West regarding macroeconomic stabilization, administrative reform, or anti-corruption drive, for example, and avoiding socio-economic disasters brought on by ill-informed social engineers.

3.3 Balance between growth policy and social policy

For developing countries that have already initiated an economic take-off, another lesson from East Asia becomes relevant. This lesson concerns the need to maintain a policy mix to accelerate growth on the one hand and solve social problems generated by growth on the other (Chapter 2). Fast growth is often associated with international integration, industrialization, and urbanization. These changes bring new problems such as income gaps, pollution, congestion, and crimes, as well as new attitudes, demands, and mobility on the part of people. Unless these problems and situations are handled skillfully by policy makers, society will explode and all development efforts may stall. In East Asia, countries that managed these growth-caused problems reasonably well achieved high income while others were stuck in the "middle-income trap." For example, Japan in its high growth era narrowed the urban-rural gap through internal migration of labor, fiscal transfers, and agricultural price supports. Malaysia adopted an ethnic affirmative action policy in 1971 to elevate native Malays, who had been economically less active than Chinese or Indian Malays, and preserve national unity. Vietnam has implemented many measures to assist ethnic minorities living in mountainous and remote areas. It should be added that these policies must be regarded as temporary and should be dismantled at a proper time as social transformation proceeds under economic prosperity. In contrast to these examples of success, Indonesia and the Philippines seem to be struggling with stubborn political and ethnic problems even though they have reached middle income levels. Thailand also faces a serious problem in bridging the gap between thriving Bangkok and rural areas which are left behind.

3.4 Begin with comprehensive policy dialogue

We recognize that the views mentioned above are by no means the monopoly of East Asian development officials. Nor do we claim that every Japanese advisor practices them. However, it can be said that, as a tendency, these views permeate more strongly in the East than in the West, which currently sets the global development agenda. The difference between the two perspectives, in their ideal forms, is a fundamental one rooted in methodology and philosophy. Moreover, the two are complements rather than substitutes. The best results will be obtained when the functional framework approach of the West is combined with the Eastern approach that emphasizes broad social context and the uniqueness of individual experiences. Abstract thinking should be supported by pragmatic action.

All this is fine as general ideas, but developing countries also need specific advice. How should the East Asian lessons be transplanted to a particular sector of any Sub-Saharan African country? Since the East Asian approach emphasizes social context and denies common answers, it cannot deliver a predetermined solution applicable to all countries. What it can suggest is the way a solution can be reached. A country should collect a large amount of information and conduct intensive policy discussion before key issues are identified, strategies are agreed, action plans are drawn up, and institutional preparations are made. This time-consuming process is unavoidable if the country is to find a solution suitable for its unique case, build trust among stakeholders, and improve local policy capability. A good Japanese expert would live in the field for years, speak the local language, become immersed in local customs, and share frustration and hardship with local counterparts before drafting a proposal. Such an expert would not give general advice upon the first visit to the country. This type of comprehensive intellectual engagement is lacking in countries where government officials are too busy attending workshops and symposiums offered by temporary visitors.

If Japan wishes to initiate a new growth assistance initiative in any Sub-Saharan country, where its knowledge and experience have so far been sparse, we suggest that it start with the same type of policy dialogue that it routinely conducts in East Asia. In countries such as Vietnam, Indonesia, and Laos, the Japanese government has mobilized a large number of Japanese academics, businesses, and aid consultants to identify key issues, study them, and offer policy advice.[8] Size and procedures may differ from one country to another. Popular agendas include improving the FDI environment, drafting master plans, and enhancing industrial capability. The process involves both the commitment of top-level leaders and deep involvement of middle-level officials. Each dialogue typically lasts for a few years with a possibility of extension into multiple phases. In some instances, the research has been followed up by additional aid programs or bilateral joint efforts to implement and monitor proposed action plans.

While East Asia and Sub-Saharan Africa are different, and issues and solutions may differ considerably between the two regions, the method of organizing policy dialogue as discussed above should be valid for both. Admittedly, Japan has much less money and human resources to mobilize in Sub-Saharan Africa in comparison with East Asia, where its economic ties and aid efforts are concentrated. For this reason, Japan's new growth assistance initiative in Sub-Saharan Africa, if it is to be done, should start with a manageable size and target only one or two countries initially. In the chosen country, Japan should become a lead donor in growth policy and work closely with other stakeholders such as domestic and foreign businesses, academics, NGOs, and bilateral and multilateral donors.

4 Japanese aid

In development aid, Japan and the UK are dissimilar donors. The two have different ideas, approaches, and instruments, as explained in this and the next sections. At the same time, both are strongly committed to development and remain substantial providers of development assistance. In 2010, Japan and the UK together contributed over US$24 billion in aid (net disbursement base), equivalent to nearly 20 percent of the total ODA by Development Assistance Committee (DAC) member countries. Without conscious effort to understand and work with each other, they are likely to conduct their aid efforts more or less independently and the chance for fruitful partnership will be lost. Table 1.1 and Figure 1.3 give summaries of ODA in the two countries and the trends of aid volume.

Table 1.1 Comparison of British and Japanese ODA

	UK	*Japan*
Volume (ODA/GNI) [2010][1]	$13,053 mn (0.57%)	$11,054 mn (0.20%)
Bilateral share [2010][2]	61.4%	66.3%
Grant share [2009–2010][3]	95.1%	52.3%
Regional distribution [2009–2010][4]	1. Sub-Saharan Africa (53.6%) 2. South & Central Asia (31.7%)	1. East Asia & Oceania (43.6%) 2. South & Central Asia (25.3%)
Sector distribution [2009–2010][5]	1. Social & administrative infrastructure (44.5%) 2. Economic infrastructure (10.6%)	1. Economic infrastructure (41.3%) 2. Social & administrative infrastructure (25.8%)
Budget support[6]	13 countries	7 countries

Source: OECD Creditor Reporting System online database.

Notes:
1 Net disbursements.
2 Percent of total net disbursements.
3 Percent of total ODA commitment.
4 Percent of total gross disbursements.
5 Percent of total bilateral commitment.
6 UK data are based on 2011/2012 (DFID, 2012). This represents approximately 15 percent of the DFID total bilateral program. Japan has so far provided budget support to Tanzania (2001–), Vietnam (2004–), Indonesia (2005–2010), Laos (2006–2007), Cambodia (2007), Philippines (2007–2008), and Ghana (2008–), based on the information available from MOFA ODA project lists.

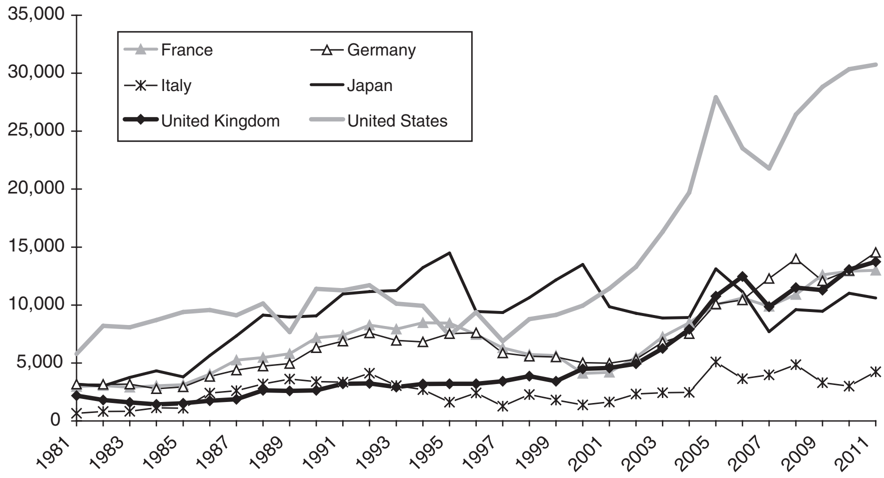

Figure 1.3 ODA trends of G7 countries (net disbursements in US$ million)
Source: OECD/DAC CRS online database.

4.1 Trends of Japanese aid

Japan's postwar decision to renounce use of military force implied that ODA had to compensate for the absence of Japan's military contribution to conflict areas in the world. In fact, ODA has been Japan's principal means to participate in globally shared efforts and to address Japan's specific external goals in each period, such as war reparation payment in the 1950s, trade promotion in the 1960s, securing imported energy and raw materials in the 1970s, and the "recycling" of the trade surplus in the 1980s. By the early 1980s, Japan emerged as the largest donor in terms of aid volume.

Subsequently, however, under fiscal austerity Japan's ODA budget, once regarded as a *sacred* budget item, has declined over the past 15 years with a cumulative reduction of 48 percent in FY2012 from the peak level in FY1997. As a result, the US replaced Japan as top donor in 2001 for the first time since 1991, and the UK, also overtaking Japan, became the second largest donor in 2006. The UK continues to enjoy top-three ranking, meanwhile Japan dropped to the fifth rank from 2007 on. In Japan, domestic constituency for development assistance is weak, and the Japanese public is experiencing aid fatigue.[9] The public feels that the budget should be spent on services that benefit them more directly such as medical care, social infrastructure, and the pension system.

Geographically, East Asia continues to be the primary destination of Japan's bilateral aid. Until the early 2000s, Japan's aid to Sub-Saharan Africa accounted for only about 10 percent, but its share of the total ODA has steadily increased under the leadership of Mme. Sadako Ogata, who assumed the presidency of JICA in October 2003 (until March 2012). At the TICAD IV held in May 2008, the Japanese government pledged to double aid to Africa by 2012, including grants, technical cooperation, and loans, and to utilize other official flows to encourage foreign investment to Africa. So far, good progress has been made toward fulfilling this promise. Sectorally, economic infrastructure receives the largest allocation, followed by social and administrative infrastructure. Japan has a broad aid menu, including concessional loans, grants, and technical cooperation. Japan is unique in having loans compose a relatively large share of its bilateral aid. The high priority placed on economic infrastructure reflects Japan's ability to mobilize sizable financial resources for development projects through the active use of concessional loans.

4.2 Development and aid visions

Japan's development and aid visions strongly reflect its dual experience as a latecomer and a donor. First, Japan is the only non-Western country with an early history of successful industrialization. Ever since Japan opened its doors to the world in the second half of the nineteenth century, the desire to catch up with the advanced nations in the West has been a strong driving force leading to its economic achievements today. Second, the generation of Japanese who lived through it vividly remember the destruction and poverty the nation sustained following its defeat in World War II. This situation was gradually overcome by very hard work, a fact in which that generation still takes considerable pride. Japan's success in strengthening its manufacturing base in turn contributed to trade- and investment-driven development and resultant poverty reduction in East Asia. Thus, the East Asian experience and aspiration for industrial catch-up are the heart of Japan's ODA vision. Being a late industrializer, Japan possesses a unique dual identity as a member of developing Asia as well as a member of the developed West.

These historic factors have heavily influenced the shaping of development visions and relationships Japan wished to foster with developing countries through aid. While Western donor countries—except for the UK—were also latecomers in the nineteenth and the early twentieth centuries, their development and aid visions do not reflect latecomer perspectives as strongly as Japan's. Joseph Stiglitz also notes that "Japan understands development because it went through the development process so recently."[10] Motoki Takahashi (2005, p.18), specialist in African development at Kobe University, states:

> [W]hat Japan learned from its own development experience and from its experience supporting East Asia was that development cannot be realized without self-reliant endeavors by recipient societies. This is very simple, but is the truth which donors tend to have difficulty respecting.

In particular, the following latecomer perspectives which Japan often preaches are unlikely to emerge from the West (Ohno, 2007).

- *Growth aspiration and graduation from aid*—aid is not charity or moral obligation to people in misery. Aid should support the self-help efforts of developing countries in building self-reliant economies and achieving eventual graduation from aid. Aid must be administered in a way that contributes to the national pride of developing countries.
- *Real-sector concern*—in the early stages of development, the government should play an active role in promoting and even creating a market economy. Greater attention should be paid to the dynamic structure of the real economy.
- *Long-term perspective*—development is a long-term and path-dependent undertaking. In its execution, it is necessary to give due consideration to the history, society, and culture of each country.
- *Pragmatism in aid delivery*—while observing general principles in international aid practice, developing countries should be given room to interpret and adapt approaches to the local context. Diversity in aid types should be accommodated.

These are complementary to the approach taken by Western countries and international organizations, which feature far-sighted frameworks, convergence toward a single system, and emphasis on macroeconomic financial issues and governance.

4.3 Challenges and the latest ODA reforms

Japan is yet to project its ODA vision effectively to the world. The country often takes the back seat in global development debates where major directions are determined by other players. Japan is often seen as operating very much at the micro level—engaged in specific projects at sub-national levels—and being of limited interest to a wider development audience, who are more interested in methods of scaling up results (Wild and Denney, 2011). As a result, Japan continues to be tormented by a gap between the mainstream development thinking and the East Asian development experience, which is widely regarded as a “success story” to which Japan made a significant contribution through investment, trade, and aid.

Several factors are accountable for Japan’s insufficient communication with external stakeholders. First, historically Japan has taken a reactive stance in aid relations, especially in imposing policy conditionality. Japan’s ODA originated from official and semi-official war reparations to the East Asian neighbors, and its approach naturally carried the sense of atonement and moral debt to them. However, a reserved attitude is not necessarily a negative quality in an aid donor. By being less assertive, Japan can conduct interactive policy dialogues with developing countries in a way that bolsters their national pride and strengthens mutual trust (Ishikawa, 2005; Takahashi, 2005).

Second, Japan's fragmented ODA decision-making inhibits coherent policy formulation and implementation. While the ODA Charter (2003) explicitly gives the Ministry of Foreign Affairs (MOFA) the authority to centrally coordinate ODA policy and implementation, the institutional configuration of Japan's ODA remains complex (OECD, 2010). Traditionally, the planning and implementation of ODA policy and budget were scattered across many organizations, including the Ministry of Finance (MOF), the Ministry of Economy, Trade and Industry (METI), the Japan International Cooperation Agency (JICA), and the Japan Bank for International Cooperation (JBIC). The latter two were charged exclusively with ODA implementation. Furthermore, implementation systems were separated by scheme. Bilateral aid is divided among MOFA (grant aid), JICA (technical cooperation), and JBIC (concessional loans). Contributions to international organizations are conducted between MOFA (UN-related organizations) and MOF (international financial institutions). Moreover, more than a dozen "domestic" ministries also partake in providing ODA with limited scope and budget, and their activities are not necessarily reported to MOFA or integrated with the rest of ODA.[11]

Since 2006, there have been major efforts to streamline Japan's ODA system. At the policy level, MOFA undertook internal reorganization in August 2006 by merging the bilateral and multilateral aid sections into one bureau, i.e., the International Cooperation Bureau. The bureau was further restructured in 2009, by transforming its scheme-based divisions (i.e., loans, grants and technical cooperation) into region-based ones. At the implementation level, the new JICA was established in October 2008, integrating parts of the former JBIC into JICA, and JICA has been transformed from an agency focused on implementing technical cooperation to one which now coordinates all three schemes. With annual gross disbursements estimated at around US$8.5–9 billion, JICA has become a unique aid agency providing technical cooperation, grant aid, and ODA loans in an integrated manner. If properly managed, a unified ODA executing agency should create stronger linkages among various aid instruments and enhance the efforts already underway to reinforce country-based approaches with greater field delegation.

Third, Japan currently lacks political will for promoting ODA policy. Unlike the UK, the recent prime ministers of Japan have had no personal interest in projecting the ODA agenda domestically or internationally. The Diet plays a limited role in policy debates and decision-making on aid. Japan does not have a basic law on aid, and until recently there was little regular oversight of foreign aid on the part of the Diet.[12] Much of the real decision-making in Japan takes place within the bureaucracy with no directives from the top. The highest policy document is the ODA Charter, approved by the Cabinet, which clarifies the philosophies and principles of Japan's ODA. The 2003 ODA Charter, which replaced the 1992 version, states that the ultimate objectives of ODA are "to contribute to the peace and development of the international community, and thereby to help ensure Japan's own security and prosperity" (MOFA, 2003).

Weak political commitment to ODA persists in Japan—even after a historic change in the government in September 2009 when the Democratic Party of Japan (DPJ) assumed power, ending the long-term rule by the Liberal Democratic Party (LDP). Instructed by then new minister, Katsuya Okada, MOFA undertook an internal ODA review, and the final report proposed a number of measures to promote public understanding and support to ODA and to improve its strategic value and effectiveness in a changing global environment (MOFA, 2010). Nevertheless, there was no follow-up action on a recommendation for the revision of the ODA Charter and the existing Medium-Term ODA Policy to properly reflect the new philosophy and basic policy.[13] This is so even after the Great East Japan Earthquake hit the country, and Japan has come to face challenges to refocus its national priority and reaffirm its global commitment under the difficult domestic situation. National debates tend to narrowly focus on administrative and domestic affairs rather than Japan's future vision in an increasingly connected world. A typical example is the budget screening and transparency campaign (*Jigyou Shiwake*) launched in November 2009, under which the ODA budget was put under severe public scrutiny.

5 British aid

5.1 Trends of British aid

The UK's development assistance has been transformed significantly since 1997 when the Labour government returned to power (see Chapter 3). In 1997, the government made global poverty reduction a national priority and created the Department for International Development (DFID) as a cabinet-level ministry with responsibility for foreign aid and international development. This ensured DFID's strong representation in the government in comparison with its predecessor, the Overseas Development Administration (ODA) under the Conservative Thatcher government. Previously, the ODA was no more than one unit within the Foreign and Commonwealth Office (FCO). Having a status equal to the FCO and the then Department of Trade and Industry (DTI),[14] DFID has become a ministry with ability to speak up on UK foreign and economic policy from the developmental perspective.

DFID offers an excellent model for galvanizing development cooperation. With a clear legislative mandate, the UK has taken a coherent and organized approach to aid policy-making and implementation. DFID is responsible for almost all ODA with direct control over 89 percent of total disbursements during 2011–2012 (DFID, 2011). The UK is widely seen as a bilateral donor who is effectively leading global development debates.

Domestically it enjoys strong political and public support and is rapidly increasing its ODA budget in an effort to reach the internationally agreed target of 0.7 percent of GNI (gross national income) by 2013. In 2006, the UK became the second largest donor in volume, surpassing Japan, and continues to be a top three donor. This is in sharp contrast to the situation in Japan, given the fact that the UK also faces fiscal austerity and that the government is drastically cutting the other budgets. The UK government thoroughly prepared for the G8 Gleneagles Summit in 2005 and successfully argued the importance of scaling up aid to Africa. Lately, the UK is actively engaged in shaping the post-MDG framework on development. Prime Minister David Cameron was asked by the UN Secretary-General to be one of the three co-chairs of the High-Level Panel on post-MDGs, charged with identifying a new international framework for development when the current MDGs expire in 2015.[15] DFID Secretary Andrew Mitchell was also appointed as one of the three co-chairs of new "Global Partnership for Effective Development Cooperation" (OECD, 2011),[16] representing traditional aid donors. The other two chairs of this new partnership will be represented respectively, by the developing world and emerging economies. In this regard, there are many things that Japan can learn from the UK.

Geographically, DFID concentrates resources on the poorest countries, particularly in Sub-Saharan Africa and South Asia, and is increasing assistance to fragile and under-aided states. Sectorally, social and administrative infrastructure receives the largest allocation. About one-third of UK aid is disbursed through multilateral organizations. Under the Coalition government that took power in May 2010, DFID has decided to further concentrate its aid, based on the results of the Bilateral and Multilateral Aid Reviews. Now, DFID focuses its bilateral program on 27 priority countries and shifts resources of its multilateral program on strong-performing organizations from those that were judged to have serious weaknesses (DFID, 2011).

5.2 Development and aid visions

The overarching framework for DFID is to contribute to the achievement of the MDGs and the elimination of world poverty. As clearly stipulated in the 2002 International Development Act, all of DFID's activities are explicitly linked to the stated goals. For example, DFID's Public Service Agreement (PSA) is closely aligned with the MDGs.[17] The desire to achieve these goals also explains DFID's engagement with other donors and multilateral organizations as an integral part of its work because DFID acknowledges that the MDGs cannot be achieved by British efforts alone. As a significant amount of UK aid goes through multilateral organizations, DFID actively promotes reforms in these organizations and tries to influence their policies.

Strong political alliance among the Prime Minister, the Secretary of State, and the Chancellor of the Exchequer ensures consistency of vision and resources required to address complex tasks of international development, and gives DFID the capability to impose policy coherence within the government. In particular, Clare Short, the first Secretary of State for International Development, invigorated the newly created DFID with strong political leadership and vision. Under her leadership, DFID ended the pursuit of commercial profit through aid. In 1997, DFID abolished the Aid and Trade Provision (tied grant aid incentives under a mixed-credit scheme) initiated by the Thatcher government. DFID strongly promotes the poverty reduction agenda and counter-balances commercial interests represented by the then DTI (currently, BIS) and foreign policy concerns of the FCO.

Historically, in the UK, aid administrations have altered with change in governments, signaling the relative importance to developmental and foreign policy objectives (Chapter 3). Aid administration has been run as a single department of government under Labour, while subordinated to the FCO under the Conservatives. However, this time, the Coalition government (the Conservatives and the Liberal Democrats) endorsed the continuation of DFID as a single department, supporting its developmental considerations. The Prime Minister David Cameron and Deputy Prime Minister Nick Clegg state in the DFID document that outlined the future of UK aid: "When this Coalition was formed, we made a commitment that even in these difficult economic times we would keep our promises and increase aid to help the world's poorest people. We are proud to stand by that commitment" (DFID, 2011, p.2). This suggests continued strong interest in and commitment to international development by the top leader. At the same time, the Coalition government has introduced changes in DFID's approach, placing new emphasis on results, transparency, and value for money.

The UK excels in the design of policy frameworks and international aid architecture. In recent years, DFID and the research community in the UK have been innovators in international development, pioneering poverty reduction strategies, new aid modalities, and aid harmonization which constitute the core of today's development strategies and aid instruments. Aspiration for aid effectiveness in the early 1990s generated the PRSP initiative in 1999 and the creation of new aid modalities to support it. For instance, DFID pushed the idea of connecting debt relief to a program of poverty reduction, which became an important building block of the PRSP initiative. The need for greater donor harmonization and alignment was also a key driving force behind the PRSP process. It is noteworthy that most (if not all) of the initial inputs to these new ideas originated from British researchers and practitioners. They played the role of catalyst in initiating global changes in development and aid policies. Now, they are actively engaged in shaping the post-MDG framework on global development.

5.3 Challenges

As a bilateral donor, DFID is a highly "policy-rich" organization with a powerful presence in the global development scene, especially in Africa

(Warrener, 2004). This is partly because the UK has a large development research community, and DFID has succeeded in establishing close networks with researchers in universities, think tanks, consultancy organizations, and NGOs' policy research units. Another reason for DFID's policy-richness is its organizational challenge to manage the scaling-up of programs while its staff is being reduced. The UK is not only committed to increasing its ODA to meet the target of 0.7 percent of GNI by 2013, but also to maintaining this level of spending beyond 2013. The Coalition government is working to enshrine this commitment in law. As a result, the budget allocated to DFID has increased rapidly, although the Department is subjected to continuous pressure to reduce staff as part of the UK government's overall administrative reform.[18] Under such circumstances, DFID is inclined to use policy-oriented quick-disbursing aid instruments such as budget support, as well as channeling the budget to the programs of international organizations and other donors (for example, through delegated cooperation) under jointly agreed policy frameworks. This is understandable, but proliferation of such aid forms with indirect disbursements may make it difficult for DFID staff, both in London and in the field, to keep track of what is really happening on the ground. The abundance of money and the lack of staff also encourage outsourced research. Greater research funding is welcome in principle, but the associated problems of overburdening the research community, diminishing marginal returns, and imbalance between popular and unpopular topics should be taken into account.

Moreover, as DFID takes leadership in global aid reform, it runs the risks of being perceived as pushing its own model against the models proposed by other donors. On this point, the OECD/DAC peer review of UK aid in 2006 warns as follows:

> British strategic interest in promoting more effective approaches to aid includes a role to motivate bilateral and multilateral donors to act similarly. However, DFID enthusiasm for certain initiatives is not always shared by other partners and British advocacy can be perceived as promoting DFID's own model rather than leading and encouraging complementary donor action … Broader donor receptivity and collaboration could be possible in a more inclusive and empirical environment for partnership.
>
> (OECD, 2006, p.11)

Another issue arises from the fiction that global poverty reduction critically depends on DFID's actions. Obviously, poverty reduction in any developing country is influenced by a multitude of political, social, and economic factors, both internal and external. Aid is merely one of these many factors, and the UK is only one donor among many. Requiring DFID to achieve MDGs and assessing its performance only by that criterion is not only arrogant but also absurd. As the year 2015 approaches, should DFID claim victory for all successes or apologize for all failures? No organization should be made responsible for something it can hardly control. It is advisable to make the PSA for DFID more realistic, for example, by introducing medium-term targets that contribute significantly to the attainment of MDGs.

More fundamentally, the feasibility of UK approaches should be questioned. For example, based on the East Asian experiences, Shigeru Ishikawa, Emeritus Professor of Hitotsubashi University and Japan's leading development economist, seriously doubts that the problems of poverty and political structure (neo-patrimonial states) in Africa can be effectively addressed before domestic productive capacity is raised and employment opportunities are expanded to certain critical levels.

> We have been strongly impressed that the aid policy of the British Labo[u]r government forms a doctrine supported by a grand design and idealism; however, we cannot help but perceive problems of feasibility when the equality of opportunity and the need to overcome social exclusion – the ethical norms of Prime Minister's *Third Way* (the domestic version of the doctrine) – are simply applied to developing countries. This is because the central problem for social exclusion in the *Third Way* is the structurally unemployed and persons outside the labor force in a mature economic society which results from high growth. By contrast, the central problem for social exclusion in developing countries, especially those in Africa, is the problem of the poor which originates in low levels of productivity and development.
>
> (Ishikawa, 2005, p.30)

The relationship between governance and growth is another point of contention. In the latest resurgence of interest in growth, the UK wholeheartedly agrees with Japan on the vital importance of economic growth in reducing poverty. *Making Governance Work for the Poor*, the DFID White Paper on International Development in 2006, argues that growth is the "exit strategy" for aid and that to reduce poverty quickly, international partners need to put growth at the heart of their relationships with developing countries (DFID, 2006, p.46). To this end, the 2006 White Paper places governance at the center of growth promotion. It notes that governance delivers or prevents economic growth in two ways: (i) through state capabilities that develop markets, support investment, encourage productivity and technological innovation, and implement regulations and policies; and (ii) through accountable and responsive institutions, policies, and political processes that make economic growth politically and socially feasible.[19]

However, asking low-income countries to abide by a broad range of governance indicators may be unproductive. Currently, a number of research programs initiated by DFID and involving think tanks and universities are underway to deepen the understanding of the governance-growth nexus. The key concepts in these studies are "good-enough" governance and growth-enhancing governance.[20] The authors try to identify governance criteria, which are narrower than the World Bank's Worldwide Governance Indicators (WGI), that define minimum conditions conducive to growth promotion (see Chapters 5 and 6). This way of looking at governance may lead to the dynamic analysis of political development in low-income countries. On this point, Ishikawa (2005) notes that the modernization of political structure was the result of the modernization of economic structure in East Asia (also see Chapter 2):

> Based on our knowledge mainly from Asia, we know that changes in old social structure and even, in some cases, political structure can occur in two ways: one through reform of the institutional system or the structure itself; and the other as a by-product of economic development including industrialization … [W]hen development takes precedence there is a strong likelihood that even if vestiges of the old system remain, the political system will be able to overcome this barrier and move forward provided government and private sector development is sound … Such evidence can be seen in many successful examples of the East Asian model.
>
> (Ishikawa, 2005, pp.30–1)

The latest research on governance in the UK may shed important light on academic and policy debates on the sequence of political and economic reforms. In particular, it may help explain the dynamics behind East Asia's authoritarian developmentalism and the possibility of introducing democratic developmentalism (these topics are discussed in the following chapter).

6 Concluding remarks

Over the past decade, a number of emerging economies have become important providers of South–South cooperation, and the private sector has been increasingly engaged in inclusive business activity that has high development impact. The second decade of the twenty-first century will be even more critical in establishing "Global Partnership for Effective Development Co-operation" and shaping the post-MDG framework for development, in an inclusive manner with the broader development actors.

Japan is one of the oldest members of the DAC. At the same time, it has a different perspective of development cooperation from the West, based on its dual experience of aid recipient and donor. In this sense, Japan is well positioned to act as a bridge between the more traditional DAC donors and emerging or new donors, in the new global context. As Menocal and Denney (2011, p.34) state, "the fact that Japan does not always do things in the same way as other DAC donors is positive in that it helps to highlight that there is no single 'right' way to approach development and as such it offers a wider set of options from which developing countries can choose."

Japan has been at the forefront of South–South and triangular cooperation, which today attracts strong attention among development actors. Back in 1999, the first Medium-Term ODA Policy already regarded South–South cooperation as a distinctive feature of Japan's ODA, stating that "[it] can be particularly effective in facilitating the transfer of technologies between countries at similar stages of development or that have common backgrounds, such as language and culture" (MOFA 1999). Close linkages among aid, trade, and FDI are another feature of Japan's ODA, and recently it has received interest as the "development investment" approach compared to the "development assistance" approach of traditional DAC donors (Saidi and Wolf, 2011).

There are good opportunities for Japan to add value to the new architecture for development cooperation, where it can play to its distinctive strengths. But, largely due to its weak policy engagement, such strengths have been unrecognized at both the national and the international level. To realize this potential, Japan needs to communicate its model and engage in international policy debates more proactively, for example, by working with policy-rich and influential donors like the UK. Time is ripe to deepen the Japan–UK partnership at the dawn of the new era of development cooperation. In 2013, the UK will host the G8 Summit and is ready to take an initiative in shaping the post-Busan and the post-MDG framework, and Japan will host the TICAD V to discuss African development, together with international organizations, emerging economies, and the private sector. Japan should make an important contribution to international development, in a way that reflects Japan's dual experience as latecomer and donor. Japan's efforts will be more effective if it works with the UK for a common goal of African development.

In summary, let us reiterate the four reasons for advancing a Japan–UK partnership.

First, Japan and the UK are important players in the donor community and bring substantial resources in terms of ODA volume. Although prolonged fiscal austerity has forced Japan to cut the overall ODA budget in the past 15 years, Japan has honored its commitment made at the TICAD IV (held in May 2008) to double aid to Africa over five years (2008–2012) and is prepared to further strengthen its commitment to African development, for example, by encouraging the engagement of the Japanese private sector in inclusive business.

Second, Japan and the UK are very different donors with great potential for productive cooperation. Although working among different donors is harder than within like-minded donor groups, the synergy impact is much greater. Aid partnership based on the principle of diversity and complementarity will surely enrich global development strategies and their delivery on the ground. Japan has much experience in growth support that reflects its own catch-up history and development assistance to East Asia. Its approach is often bottom-up with strong field-based real-sector orientation. The UK has deep knowledge and experience in Africa. It is a leading donor in poverty reduction. With effective communication skills, it is also good at designing policy frameworks, conducting policy dialogue, and organizing stakeholder engagement.

Third, the UK's rising interest in concretizing growth initiatives and Japan's desire to make a new contribution in Africa offer an excellent opportunity for bilateral partnership. The British framework approach to growth, such as the recent research on the governance-growth nexus, is highly complementary to the Japanese ingredients approach to growth which pays great attention to concrete elements such as infrastructure, human resources, technology, and small- and medium-sized enterprises, in the context of each developing country.

Fourth, Japan and the UK should encourage emerging donors to support African development. A number of "East Asian Miracle" economies have graduated (or are graduating) from ODA and are willing to become new donors. Together with South Korea, Japan took initiative in establishing the Asian Development Forum in 2010, which annually convenes officials from Asian countries, including China and India, to discuss Asia's role in the global development community and ways to use ODA effectively to tackle development issues in and outside the region.[21] The Forum is inclusive of other regions, international organizations, and the 2011 Tokyo meeting benefited from the participation from senior officials from DFID, the World Bank, and an African think tank. Countries such as South Korea, China, Malaysia, and Thailand can not only bring additional resources but, most of all, share with latecomers their recent experiences as aid recipients and fast industrializers under the strong pressure of globalization. The two old donors should set up a mechanism to promote Asia–Africa cooperation. Additionally, they can also contribute ideas to today's latecomers from the sideline.

Notes

1 The Japanese government resumed ODA loans to a limited number of African countries which have demonstrated good track records in macroeconomic management and debt sustainability following the application of debt relief (Enhanced HIPC Initiative). At the Gleneagles G8 Summit in 2005, the Japanese government announced the introduction of the Enhanced Private Sector Assistance for Africa (EPSA), a joint initiative with the African Development Bank (AfDB) to promote private sector development. EPSA consists of three components: (i) trust fund; (ii) co-financing by the then Japan Bank for International Cooperation (JBIC, now JICA) and AfDB to sovereign borrowers; and (iii) JBIC loans through AfDB to private businesses as end-users.

2 In October 2008, the "new JICA" was created by integrating parts of the former JBIC, which managed ODA loans, into the JICA, which was traditionally charged with the execution of technical cooperation. The "new JICA" is also responsible for some grants previously managed by the Ministry of Foreign Affairs.

3 See more details for Shimomura (2005) and Ohno and Shimamura (2007).
4 ODA almost quadrupled from US$37.8 billion in 1980 to US$148.4 billion in 2010, but decreased as a proportion of total financial inflows into developing countries which include remittances, commercial loans, and equity investment. While ODA constituted around 50 percent of total financial inflows in 1980, it now accounts for less than 30 percent (Source: OECD International Development Statistics online database).
5 For more discussion on East Asian experiences, see Chapter 2 of this volume.
6 Chapter 2 contains further discussion on authoritarian developmentalism and democratic developmentalism.
7 The 5S (a Japanese management approach) is the most elementary way to improve production efficiency by keeping the factory tidy and well organized. Its elements are *seiri*, *seiton*, *seiso*, *seiketsu*, and *shitsuke*, which roughly mean remove unnecessary things, arrange tools and parts for easy view, keep the work place clean, maintain personal hygiene, and behave with discipline.
8 In Vietnam, JICA organized a three-phase bilateral joint research project on economic development and transition toward a market-oriented economy headed by Prof. Shigeru Ishikawa (1995–2001). In Laos, a similar JICA project headed by Prof. Yonosuke Hara was carried out in two phases (2000–2005). In Indonesia, JICA supported a team of Japanese experts headed by Prof. Takashi Shiraishi (during 2002–2004), which conducted intensive policy dialogues with Indonesian policy makers on scenarios of economic recovery from the Asian financial crisis. In addition, there are numerous Japanese programs of various duration and content for industrial policy advice as well as long- and short-term training and expert dispatches in virtually all East Asian developing countries.
9 According to the opinion polls by the Cabinet Secretariat, the public support of Japan's engagement in foreign aid has declined sharply in the past decade. In 2011, the percentage of people who responded that Japan should increase the ODA budget was 27 percent, falling from around 40 percent in the early 1990s. The public support of Japan's foreign aid was the lowest in 2004—when those actively supporting ODA dropped to less than 19 percent of the total respondents, and those who felt that Japan should decrease or eliminate ODA rose to around 29 percent.
10 Presentation by Prof. Joseph E. Stiglitz of Columbia University, "Globalization and Development," at a special seminar on Making Globalization Work for Developing Countries organized by the Institute for International Cooperation, JICA, on July 31, 2007, Tokyo.
11 In addition to JICA, 13 different ministries are involved in technical cooperation (so JICA undertakes about half of the technical cooperation).
12 In this regard, the creation of a special committee for ODA in the House of Councilors (the upper house) in early 2006 deserves special attention.
13 The first Medium-Term ODA Policy was formulated in August 1999, and then revised in February 2005 to reflect the vision stipulated in the 2003 ODA Charter. After seven years have passed, the policy framework is due to be updated. But, no initiative has been taken by the DPJ government on this matter, despite significant changes in the domestic and external environment surrounding Japan's ODA since then.
14 In June 2007, DTI was divided into: Department for Business, Enterprise and Regulatory Reform (DBERR) and Department for Innovation, Universities and Skills (DIUS). In June 2009, the Department for Business, Innovation and Skills (BIS) was created by merging the two departments.
15 The other two co-chairs are President Johnson-Sirleaf of Liberia and President Yudhoyono of Indonesia.

16 "Global Partnership for Effective Development Co-operation" is a new partnership framework, agreed at the Busan High Level Forum on Aid Effectiveness, held in November 2011 in South Korea.

17 The PSA was introduced in 1998 as part of the overall results-oriented approach of the New Labor government. A set of time-bound and results-oriented performance targets are agreed between each Department and the Treasury and recorded in a triennial PSA.

18 The number of staff in post decreased from 1,907 (2004) to 1,600 (2009), and further down to 1,562 (2012), according to the data from DFID Annual Reports and Accounts, 2008–2009 and 2011–2012. These are the number of full-time equivalent civil service staff employed by DFID (as of March in respective years) in the UK and overseas, including those working overseas on aid projects.

19 Based on the presentation "Governance: Japan and UK Views" by Peter Owen, Senior Governance Adviser at DFID's Policy and Research Division, in February, 2007.

20 Professor Mushtaq H. Khan of the School of Oriental and African Studies, University of London, has written extensively on "growth-enhancing governance" capabilities (see Khan, 2006, for example). The ODI's Poverty and Public Policy Group (PPPG) is undertaking a five-year DFID-funded study on power, politics, and the state to explore the possibility of hybrid formal-informal power structures that may be able to provide "good-enough" governance. Separately, DFID and ODI researchers are conducting the World Governance Assessment (WGA) project to identify a set of core indicators closely related to good governance.

21 The first meeting took place in Seoul in November 2010, right after the G20 Seoul Summit, and the second meeting was held in Tokyo in June 2011. The third meeting was held in 2012 in Thailand.

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2 The East Asian growth regime and political development

*Kenichi Ohno**

1 Introduction

Many low-income developing countries are caught in a trap. The private sector is small and weak, and lacks skills, technology, funds, trust, and management capability. Local producers can hardly compete with global giants in open markets. Under these circumstances, the government is expected to lift the country out of poverty, but the government itself also faces a multitude of problems such as inefficiency, corruption, lack of talent and information, bureaucratic formalism, and political pressure. Bad policy, stagnant economy, and social instability exacerbate one another. Countries must break away from this vicious circle before they can initiate an economic take-off. The question is how to do this, and East Asian experiences in the last several decades may provide some clues for latecomer countries which are not yet on a path of robust growth.

East Asia's success pattern was very different from the current popular thinking in the ODA donor community. Countries in East Asia did not start the "breaking away" process by drafting a poverty reduction strategy paper or minding governance, transparency, and grass-roots participation. As a matter of highest priority, they had to cope with the life-or-death problem posed by external military threat or internal social fragmentation. To maintain national unity and military readiness, economic growth was considered imperative. A political regime that could handle this situation, which we call authoritarian developmentalism, was established in a number of countries. This regime pursued economic growth at any cost and thus broke the poverty trap. New problems generated by fast growth, such as income and wealth gaps, urbanization, internal migration, environmental damage, and congestion were also recognized and dealt with.

However, it must also be admitted that such regimes and policies, which may have suited the reality of the Cold War era, are a little too harsh and insensitive for developing countries today. Historical lessons must be learned in full recognition of circumstantial differences. This chapter proposes to learn from the East Asian experiences selectively and with modifications, instead of accepting or rejecting them totally and unconditionally.

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2 Good but uneven performance

East Asia's economic development has been quite remarkable, but high performance was not uniform across countries or over time. It is also difficult to argue that East Asia owes its success to good initial political and economic conditions alone. It is necessary at the outset to dispel these myths and emphasize the role of policy in achieving economic success. East Asian growth was generated mainly through competent execution of appropriate policies, as explained below, rather than spontaneous emergence of some inherent characteristics of the region such as diligence or Confucianism. Countries that did not implement needed policies or those that implemented them insufficiently have failed to participate in regional economic dynamism. Figure 2.1 shows a wide range of achievements in governance and economic development in East Asia with a strong positive correlation between the two measures (0.90).[1]

While the precise geographical definition of East Asia is somewhat debatable, it is safe to say that only a subset of economies belonging to this region have achieved or are achieving sustained economic miracles. Japan, Singapore, and Hong Kong have already reached high income and life style comparable to the richest countries in the West. Taiwan and South Korea are very near that level. Malaysia, Thailand, China, and Vietnam, although in different development stages, are moving up rapidly.[2] These nine economies are full participants in the East Asian production network. The growth record of Indonesia has not been as strong as those of others though its economic performance has improved considerably in recent years. On the other hand, the Philippines has been integrated in regional dynamism for a long time but its performance and future prospects remain more precarious.

Additionally, a number of economies lie outside the East Asian Factory for various reasons. After a long period of internal instability and economic difficulties, Cambodia finally seems to be attracting foreign manufacturing firms in a very early stage of industrialization. Myanmar, with ongoing political liberalization, also began to greatly attract attention of foreign investors. Meanwhile, Laos, Papua New Guinea, and East Timor are struggling for political stability or economic take-off, or both. At this point, North Korea is a political outcast dependent on Chinese trade and aid for which no meaningful growth strategy can be discussed. Finally, Brunei, a small oil-rich country, is an entirely different type that does not belong to East Asian production linkage.

The paths traveled by East Asian economies have been far from smooth. When Gunnar Myrdal wrote *Asian Drama* in 1968, Southeast Asia was considered to be a region trapped in dire poverty. He argued that the only way to get out of it was through population control, more equitable land distribution, and investment in health care and education (FDI-led growth was not mentioned). According to historical statistics compiled by Maddison (2001, 2012), shown in Figure 2.2, Africa had a higher average income than Asia in the

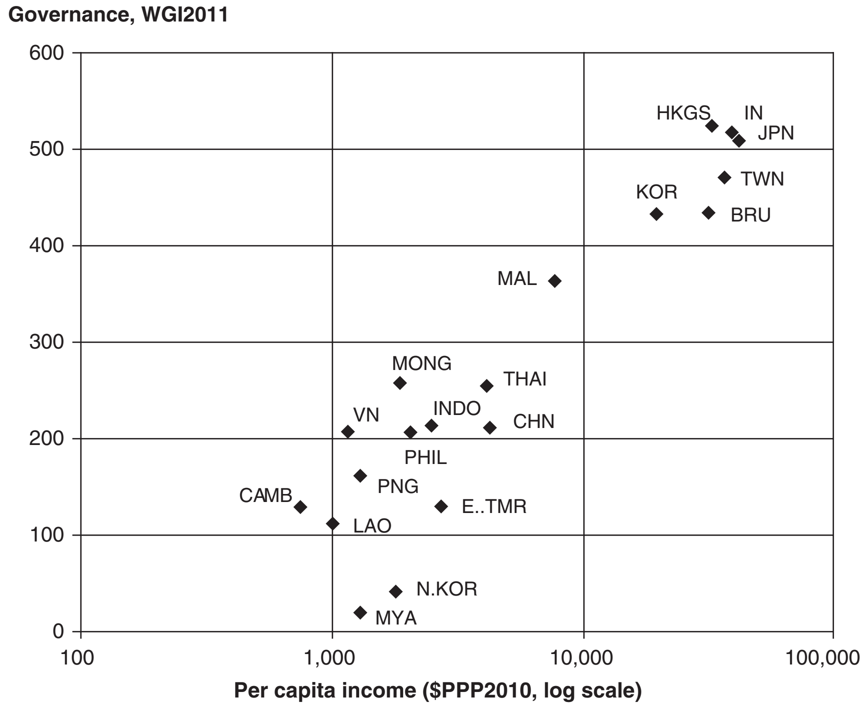

Figure 2.1 East Asia: governance and income

Sources: Compiled from World Bank, *Worldwide Governance Indicators* (2010); and World Bank, *World Development Indicators* (2011). CIA, *The World Factbook* (2011) was used for income data of North Korea, Myanmar, and Taiwan. Brunei's income data is for 2009.

Notes: Worldwide Governance Indicators consist of six dimensions (voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, control of corruption) with each carrying 0 to 100 points. The vertical value in this diagram simply adds these points for each country or area.

1950s. China, now the mighty factory of the world, was mired in political and economic confusion in much of the 1950s, 1960s, and 1970s. The Cold War turned hot in the Korean Peninsula and Indochina, and tension continued across the Taiwan Strait, all of which severely affected the political economy of the entire region. In the late 1950s, South Korea was considered a basket case under an incompetent leader with rampant corruption (see Section 6).

More recently, growth was interrupted by various events such as the oil shocks in the 1970s, the ASEAN recession in the early 1980s, Japan's economic stagnation since the 1990s, the Asian financial crisis in 1997–98, the global IT recession in the early 2000s, the Lehman shock in 2008, and the Euro crisis in 2011. It is therefore difficult to argue that East Asia grew fast because the region enjoyed peace and stability or because it had inherited

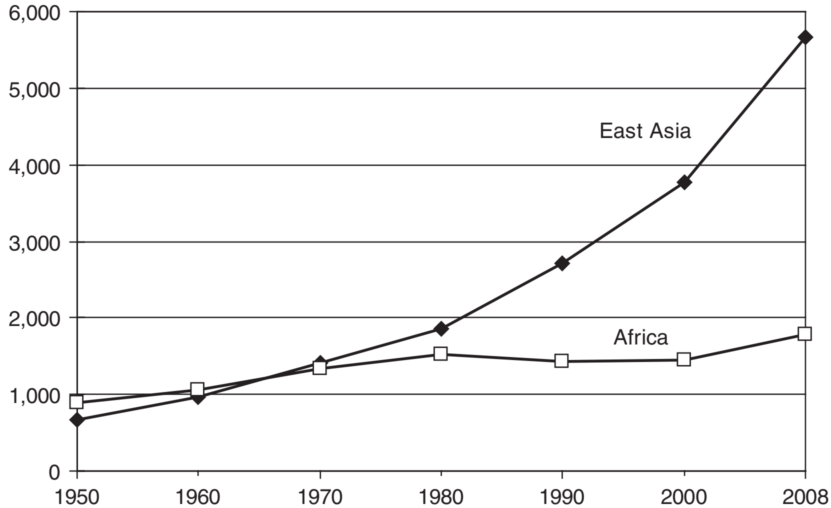

Figure 2.2 Per capita GDP (measured in 1990 international Geary-Khamis dollars)
Source: Maddison (2012).

better initial economic conditions than Sub-Saharan Africa. Policy, not external circumstances, made the critical difference.

3 Growth policies and social policies

The development strategy of the global development community shifts every several years. The current strategy focuses on the Millennium Development Goals (MDGs) proposed by the United Nations in 2000, which feature poverty reduction and attainment of seven other social goals in the period between 1990 and 2015. Moreover, good governance is also targeted as a main pillar of development effort. However, it is now widely recognized that meaningful poverty reduction cannot be achieved only by shifting existing resources around or improving education and health care. Economic growth is absolutely necessary for sustained poverty reduction and avoidance of permanent aid dependency. Despite broad consensus on this matter, however, the global development community seems at a loss as to what concrete measures are required to generate long-term growth, especially in Sub-Saharan Africa.

These questions were alien to East Asian development thinking, where growth has always been the central objective for which policies and resources were mobilized. For East Asian countries, poverty reduction was one of the many natural fruits of competent economic management rather than an overarching goal toward which every development effort must be exerted.

In fact, reducing poverty was a goal too small for them; East Asian states invariably pursued a more ambitious goal of greatly improving technology, competitiveness, and living standards so as to join the ranks of advanced countries and establish a respected stature in the world economy.

Despite differences among countries, there was a general policy orientation followed by all successful economies in East Asia. This policy orientation had two main components: growth policies and social policies. Growth policies include standard measures that ignite and sustain private-sector dynamism such as provision of indicative visions, plans, and strategies; human resource development; technology; infrastructure; SME promotion; FDI attraction; finance; and subsidies.[3] Social policies are a set of measures that cope with problems generated by rapid growth, such as inequality, pollution, urbanization, congestion, labor migration, asset bubbles, corruption, illegal drugs, materialism, and decline of traditional values and customs. Growth policies are primary and social policies are secondary, in the sense that the latter ameliorate new problems generated by the successful execution of the former.

Yasusuke Murakami (1992, 1994) stresses the importance of simultaneous execution of growth policies and social policies (which he calls "supplementary policies") in order to avert the negative aspects of developmentalism. As he puts it,

> When targeted key industries begin to grow rapidly, people in these and related industries will experience a shift in life style and even in attitude toward life … [E]specially in latecomer countries, social structure, including the national psychology, will be impacted strongly by the force of "modernization," sowing the seeds of social tension. Such tension typically arises from a widening gap in income and life style between urban and rural populations. Equally notable is the formation of mega-cities and surrounding slums which are often seen in Latin America and Asia. Failure to alleviate social tension under these circumstances can lead to political conflict, which ultimately stymies developmentalism itself.
>
> (Murakami, 1994, p. 192, English translation)

Once rapid growth begins, social transformation is inevitable. It permeates all aspects of social life, including psychology, attitude, work, entertainment, family, urbanization, village community, human mobility, transport, environment, culture, and nationalism. Development cannot be sustained unless both growth policies and social policies are conducted in proper balance. The required details of these policies differ from one country to another, and they must be designed and implemented carefully to suit local needs. In East Asia, only those countries that managed to do this more or less competently have achieved economic miracles. Some economies such as Japan, Taiwan, and Korea succeeded in raising everyone's income

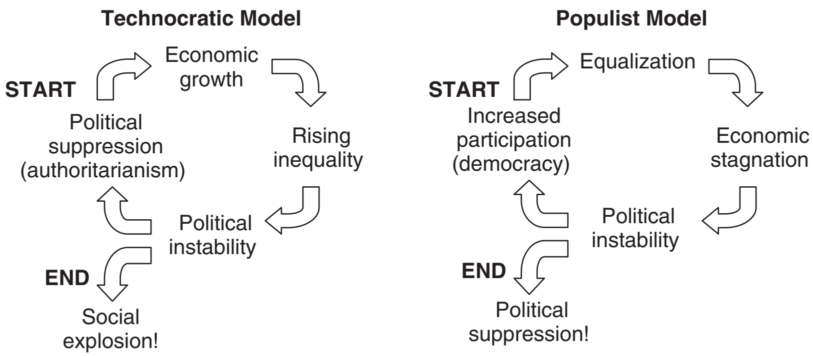

Figure 2.3 No easy choice?
Source: Compiled from Huntington and Nelson (1976).

during the high growth era. But other countries such as China, Thailand, and the Philippines were unable to narrow huge income and wealth gaps as they grew.

Observing the dismal situation in Latin America in the 1960s and 1970s, where ruthless dictators and incompetent populism alternated, Huntington and Nelson (1976) concluded that chaos would be the inevitable end result no matter how the country started the development process (Figure 2.3). In their technocratic model, an authoritarian state with suppressive policies initiates growth, which breeds inequality and raises social tension. To cope with this situation, the regime introduces even more suppressive policies. After a few rounds of this, discontent mounts to a critical level, people take to the streets, and society explodes. Alternatively, in their populist model, a democratic state which permits broad participation is installed initially. The government distributes available economic benefits among supporters but does not succeed in mobilizing resources selectively and decisively to increase GDP. Economic stagnation leads to dissatisfaction and the regime is eventually thrown out by a military coup. The conclusion follows that there is no easy way to generate economic growth while maintaining political stability.

Using this framework, what East Asia's successful economies did can be portrayed as a revised technocratic model where rising inequality and other growth-generated problems were ameliorated through social policies (Figure 2.4). With this policy mix, crisis is averted and the virtuous circle of economic growth and political stability is maintained for a few decades until the society changes from within (see Section 5 below). This was the East Asian answer to the Latin American puzzle presented by Huntington and Nelson. The policy pattern was clear, but the question was how adeptly a country could execute it.

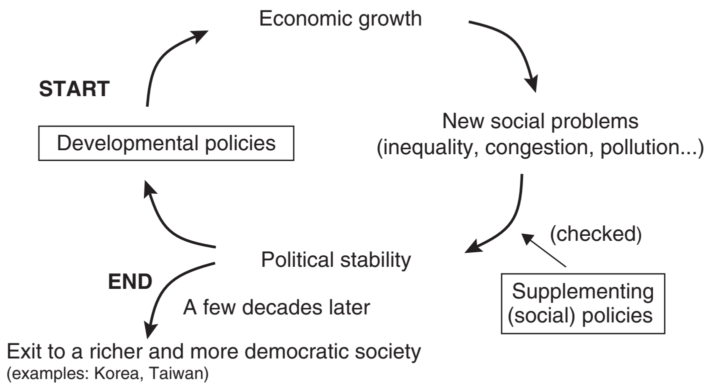

Figure 2.4 East Asia's policy mix

4 Growth driven by regional integration

For latecomer countries, economic development and international integration are one and inseparable. Today's development process is characterized by a continuous inflow of foreign products, ideas, technology, and systems into the country. They are brought through private channels such as human mobility, trade, and investment; through policy initiative; or under the pressure of donors and international organizations. To enhance domestic capability and generate growth, foreign factors must be adopted selectively and with modifications to suit local needs. Integration policy and development policy must be integrated closely and managed by the central government rather than left to private hands or foreign organizations (Maegawa, 1994; Ohno, 1996, 2000, 2003).

This development-integration nexus took a very special form in East Asia. East Asian growth was attained through the very existence of the East Asian region as an arena for economic interaction among its members. One by one, countries in different development stages initiated economic growth by participating in the dynamic production network spanned by private firms. Linked by trade and investment, an international division of labor with a clear order and structure has emerged in the region. Industrialization has proceeded through geographic spreading on the one hand and structural deepening within each country on the other. The term *flying geese* referred to these systematic supply-side developments. To understand this mechanism, evaluating the policies of individual countries is not enough; it is necessary to analyze East Asia as a whole, with its production structure, intra-regional trade, and investment flows.

For countries in East Asia, development was—and is—tantamount to jumping into this regional production network and becoming one crucial

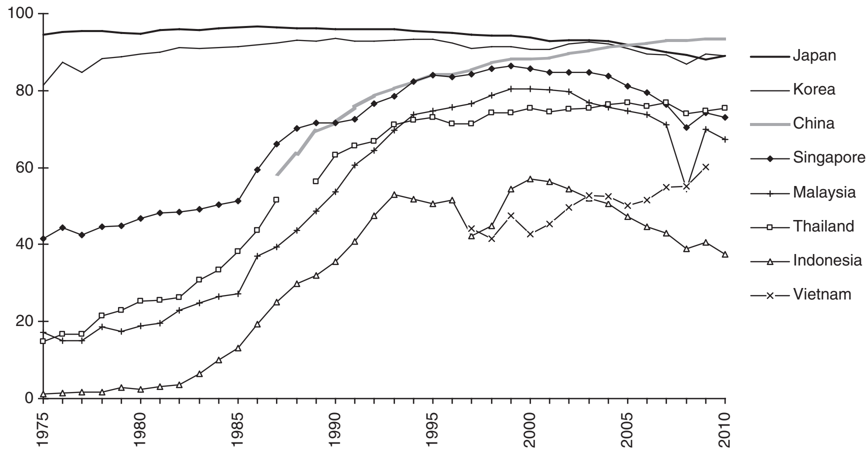

Figure 2.5 Manufactured exports (percent of total exports)
Source: World Bank, World Development Indicators database.

dynamic link in it. Each country is under constant competitive pressure from the countries moving ahead of it as well as behind it, which compels it to continuously climb the ladders of development. What drove these countries was the desire for material well-being and the pursuit of national pride in the context of this regional competition, not policy matrices or governance criteria introduced by international organizations.

Figure 2.5 shows how the East Asian geese have been flying as measured by the ratio of manufactured goods to total exports. The top economies including Japan, Taiwan, and Korea have long exported manufactured goods. The second tier of economies such as Singapore, Malaysia, Thailand, and especially China, have caught up very fast. They are followed by a third group of economies such as Indonesia, Philippines, and Vietnam. On the other hand, Myanmar, as well as the East Asian economies not shown here such as Cambodia, Laos, and North Korea, have not even entered the race.

Industries are constantly passed from the first tier countries to the next and down the line. Since this industrial passing occurs mainly through FDI, countries wishing to strengthen their positions court FDI vigorously. Japanese corporations have long been the chief architect of the East Asian production network, together with EU and US multinationals. The extensive business networks of Taiwan, Hong Kong, and overseas Chinese as well as bold business moves by Korean chaebols have also invigorated this region. Since the 1990s, the emergence of China as a producer and investor has become the important factor. No other developing region has formed such an organic and dynamic interdependence as East Asia. This is one fact that cannot be easily replicated in any other developing regions when East Asian experiences are studied and learned by them.

5 Authoritarian developmentalism

To break away from the poverty trap and initiate growth, most countries in East Asia installed authoritarian developmentalism, or an authoritarian state with high development policy capability.[4] The key ingredients of this regime are as follows:[5]

- powerful and economically literate leader;
- development as a supreme national goal, ideology, and obsession;
- an elite technocrat group to support the leader in designing and executing policies;
- political legitimacy derived from successful development.

Among these, the first ingredient (leadership) is crucial because the other conditions can be created by a competent leader if they do not already exist. The importance of a decisive and enlightened top national leader such as a president or prime minister cannot be over-emphasized. This leader must have a keen sense of what works and what does not in accelerating growth. A Ph.D. in economics or an MBA is not required, but an instinct for selecting the right policies and assigning good people, as well as political finesse, is essential. Strong leaders are many, but strong and wise leaders are rarer. The term authoritarian developmentalism is reserved only for regimes led by the latter.

Gray areas in Figure 2.6 show the countries and periods of East Asia's authoritarian developmentalism. The effectiveness of these "dictators" in promoting growth differed substantially. According to the original classification by Suehiro (2000), on which this diagram is based, the Philippines' Marcos regime was counted as authoritarian developmentalism but we prefer to exclude it from the list, at least the latter years of his regime, due to the fact that it failed miserably in delivering economic results. Three things are clear from Figure 2.6. First, not all East Asian economies experienced authoritarian developmentalism. Second, all successful economies, with the exception of Hong Kong, have adopted authoritarian developmentalism in the past. Third, authoritarian developmentalism typically lasted two to three decades. In this regard, Singapore is the only country that has not abandoned this system even after reaching a very high income level.

East Asia's authoritarian developmentalism often emerged under severe security threat. South Korea was threatened by North Korea, and Taiwan's existence was precarious in the presence of Mainland China. Internal political chaos and ethnic unrest also increased the likelihood of such a regime emerging. In a number of cases, a military coup was staged to replace an ineffective government unable to contain a crisis situation. Under this type of regime, many elements of democracy such as freedom of speech and press, free and competitive election, and the power of parliament were restricted or suspended. For this reason, these regimes were regularly criticized by the

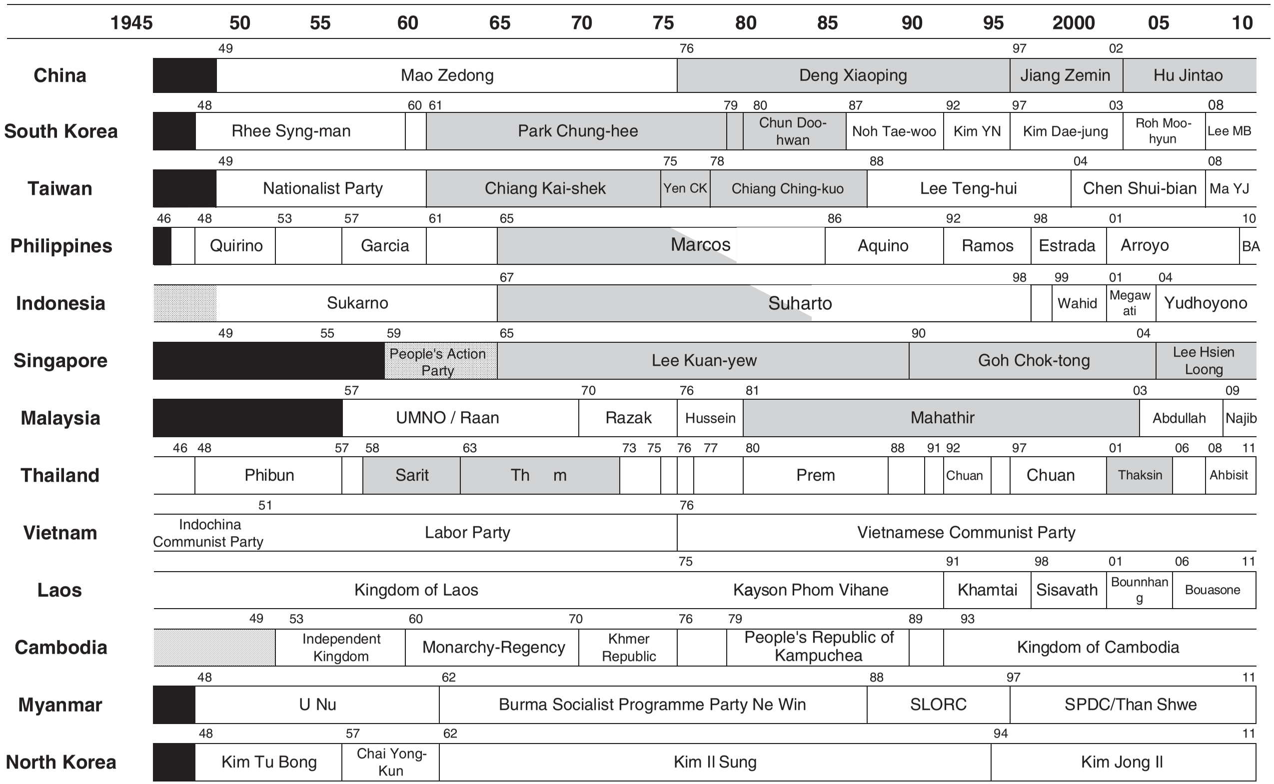

Figure 2.6 Authoritarian developmental states in East Asia

Source: Information in Suehiro (2000, p. 115) was revised, updated, and expanded by the author.
Note: The gray area shows authoritarian developmental leaders and the dark area indicates pre-independence periods. For China, the most influential leader among those holding highest positions is indicated.

West as "undemocratic." However, people may support their dictator, not because he came to power by free election, but because he delivers national security, higher income, and job opportunities to them.

Why do we need an "undemocratic" state to execute development? The fundamental reason is that economic take-off from a low base requires massive and speedy resource mobilization.[6] Adrian Leftwich (2005) points out that democracy and development require different institutional conditions which cannot be easily reconciled:

> The institutional characteristics and requirements for development [accumulation and change] and for democracy [accommodation and compromise] pull in opposite directions … democracies have great difficulty in taking rapid and far-reaching steps to reduce structural inequalities in wealth.

The country must unify different ethnic and social groups into an imagined community, build power supply and transport systems, attract investment, improve skills and technology, build schools and hospitals, crack down on crimes and social evils, relocate residents, manage urbanization and internal migration, conduct macroeconomic and trade policies, cope with global and regional shocks, and the list can go on considerably further. Allowing political participation of all concerned groups and thoroughly debating all laws and policies in the parliament would be more democratic, but would take too much time. If a critical mass of policies is not adopted quickly and simultaneously, the country cannot initiate or sustain growth. This is precisely the failed populist model discussed in Section 3.

One important thing about authoritarian developmentalism is its transitional nature. Unlike democracy, it is not a regime all countries should aspire to and defend in the long run. Rather, it is a short-term regime of convenience whose value lasts only for a few decades. It is an instrument for achieving fast growth at a critical moment in the history of a particular country. Once the desired level of development is attained, it should be thrown away just like the first-stage booster must be ejected when the space craft reaches a certain height. If it is not detached, it will become a serious obstacle for further flight. The evaluation of this regime must be made in this dynamic context, not by static comparison of attained level of democracy.

Another important and related issue is the exit problem. Watanabe argues that "if development under an authoritarian regime proceeds successfully, it will sow the seeds of its own dissolution" (Watanabe, 1998, p. 217, English translation) by providing higher living standards and diversified social strata. New middle mass, consisting of white-collar workers, professionals, small business owners, and students, begin to disapprove of authoritarianism and demand more democracy. However, authoritarian developmentalism may not melt away automatically if there are barriers to transition such as a stubborn leader, bureaucratic resistance, and interest groups. In particular, a strong leader often refuses to step down because of the prospect of being revenged, jailed, or even executed after transition, with most or all of the regime's policies reversed. Unlike well-functioning democracy, this type of regime does not have a built-in mechanism for smooth power transition. Thus, political stability at the time of transition largely depends on the wisdom and self-control of the leader. In East Asia, some exits of authoritarian leaders have been peaceful and others have been violent.

A similar transition problem also arises under one-party rule, be it the Communist Party (China, Vietnam) or the Liberal Democratic Party (Japan). The ruling party that remains in power for several decades generates a web of beneficiaries and supporters who resist reforms. The party's policies, which may have worked well initially, become outdated and renovation becomes imperative. A fight between reformers and conservatives often emerges within the party. External pressure for change also mounts. A smooth transition is possible but not guaranteed.

The fact that a large number of authoritarian developmental regimes emerged in East Asia, but not elsewhere, can be explained by regional contagion. Neighboring countries are always in competition, consciously or unconsciously, for policy initiative and high performance. The last thing that policy makers admit is that they monitor and copy the policies of neighboring countries, but they actually do. They are sensitive to policy shifts in their neighborhood, especially those that give a head start to some and make others feel left behind. This is why policy has a powerful contagion effect within a region. The wave of democratization in Latin America in the 1980s and simultaneous rejection of socialism in Eastern Europe around 1990 are such examples. The high frequency of authoritarian developmentalism in East Asia should also be understood in terms of such a policy domino effect.

From the historical perspective, the popularity of authoritarian developmentalism in the 1970s can be attributed to the Cold War effect (Iwasaki, 2001). Military regimes and one-party rule proliferated in that period when siding with one ideological camp or another was the name of the game. Developing countries could receive military and economic aid and other strategic benefits from the chosen patron without any conditionalities imposed on domestic political reform. Today, the majority of developing countries have already introduced democracy in form, if not in spirit and substance. In the 1990s countries in Africa, Latin America and elsewhere adopted multi-party democracy in droves. Convergence to "international best practices" (Western style market and democracy) has become compulsory if the country is to receive respect and aid from the international community. This may be regarded as a great achievement from the viewpoint of human rights and political modernization. However, viewed from other angles, all is not well.

First, democracy which values procedure and participation tends to slow down policy making and restrain government's hands. Whatever the inherent merits of democracy may be, speed and agility are not among them. This fact must be weighed against the need for a poor developing country to mobilize limited resources effectively and respond to shocks quickly.

Second, the substance of politics is slow to change even though its form is renewed. This is not surprising because political development is a long evolutionary process realized thorough policy effort and transformation of mindset and structure of the public. In many cases, leaders and bureaucrats managing the new democracy are the same folks as before and popular sentiments toward politics also have changed little. The global stampede toward democracy in the early 1990s was a strategic response by developing country governments to the shifting global rules to secure political and economic assistance. In many countries, politics continues to be characterized by radicalism and instability even if democracy is formally in place. Paul Collier reports that democracy has not yet produced accountable and legitimate governments and has rather increased political violence in many developing countries, especially in the societies of the “Bottom Billion” (Collier, 2009).

Third, democracy has no automatic tendency to enhance the capability of government to promote development. Separability of democracy and development means that economic policy capability must be learned additionally and separately. The previous choice between a good dictator who accelerated development and a bad one who did not has been replaced by the problem of how to inspire a benign but average government into developmental action. Latecomer countries must now solve the same developmental problems—leadership, vision, skills and technology, enterprise development, finance, infrastructure, integration, social protection, and the like—under new rules and constraints.

Can a democratic state be developmental at the same time? Can it be decisive, quick, and flexible in policy making? Both democracy and development are worthy goals, and the one should not be sacrificed for the sake of the other. However, interaction between the two is a complex, and sometimes conflicting, one. Promoting one goal may accelerate or deter the other, depending on the country’s social fabric and stage of development. We will come back to the issue in the final section.

6 Case studies

Let us look at South Korea, a country that has already graduated from the authoritarian period, and China and Vietnam, two countries undergoing rapid industrialization and social transformation.

South Korea

South Korea has graduated from authoritarian developmentalism and is moving toward further economic and political transformation. Today, South Korea can competitively produce high-tech products such as cars and consumer electronics. But half a century ago, people did not think that the country had any future. It was a colony of Japan during 1910–1945. The Korean War (1950–1953) devastated and divided the country. In comparison with North Korea, which had heavy industries and ample natural resources, the development prospects of the agriculture-based South seemed bleak. Under the Rhee Syngman government (1948–1960), South Korea was regarded as a corrupt basket case. Its survival depended heavily on American aid.

However, the situation changed dramatically in 1961, when Park Chung Hee, a military general, staged a coup and seized power. His regime was a typical authoritarian developmental state with a very strong will to promote capitalism under state guidance. The Economic Planning Board was created as an executing agency and five-year plans were started. The development strategy focused on export competitiveness, foreign loans, and imported technology. Export subsidies, import protection, foreign exchange allocation, exchange rate unification and devaluation, low-interest rate policy loans, and tax incentives were carried out. Targeted industries shifted from garment and footwear (1960s) and steel, petrochemicals, and shipbuilding (1970s) to automobiles and electronics (1980s). Korea's industrialization was carried out under a serious threat from North Korea and suppressed democracy. It was characterized by the triangular alliance of government, banks, and chaebols (large business groups such as Daewoo, Samsung, Hyundai, and LG). By conducting highly interventionist policies, South Korea became one of the most successful latecomers. Park Chung Hee was assassinated in 1979, but another military general, Chun Doo Hwan, continued to rule until 1987.

With the hypothesis that democracy can be introduced effectively only after a certain development level is reached ("developmental threshold for democracy"), Nguyen Thi Thanh Huyen (2004) analyzes the process of Korea's development and democratization. She contends that economic growth leads to "social mobilization" (social changes such as urbanization, industrialization, and modernization), which breeds two necessary driving forces of democracy, namely political culture and social structure (Figure 2.7). Political culture refers to popular attitudes which support democracy, such as compromise, participation, equality, and moderation. Social structure means a quantitative power shift from the old classes (peasants, military, land owners) to the new classes (white-collar workers, professionals, entrepreneurs). Political culture and social structure interact with one another to prepare conditions under which democracy can be installed and sustained. In 1961, 80 percent of South Koreans were poor farmers. By 1985, workers (over 50 percent) and the middle class (about 40 percent) dominated the social structure. South Korea made a transition to democracy in 1987, when Roh Tae Woo became president through popular election. It could not introduce democracy in the 1960s or 1970s, but socio-economic changes

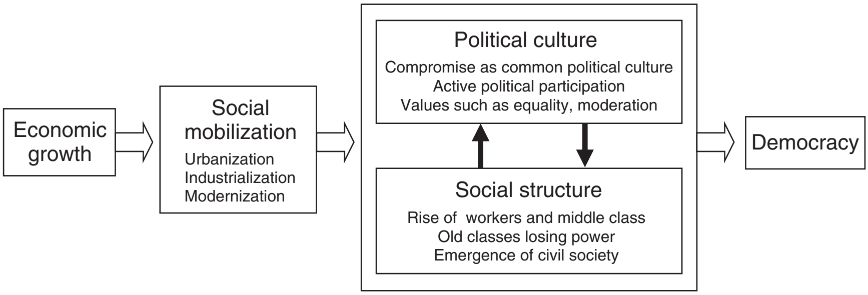

Figure 2.7 South Korea: growth prepares democracy
Source: Compiled from Nguyen (2004).

generated by rapid economic growth prepared conditions for and compelled political transformation by the late 1980s.

China and Vietnam

China and Vietnam are the two fastest-growing countries in East Asia. They are also socialist countries in systemic transition under one-party rule. They are in the midst of rapid industrialization and social transformation that are expected to last at least for a few more decades. Despite differences in size, history, governing style, and the depth of economic planning in the past,[7] the two countries share basically the same dynamic problems. Their main challenge is to cope effectively with social problems caused by fast growth, while fast growth itself is generated by largely uncontrollable private dynamism rather than good policy, as discussed below. Another important issue is to stage a smooth political transition as income rises.

Unlike Japan and South Korea in the past—and also unlike Singapore, Taiwan, Malaysia, and Thailand to a lesser extent—where government played an important role in setting concrete industrial goals, upgrading technology, and guiding investments, the current growth of China and Vietnam is driven largely by strong private dynamism. In these countries, the government makes relatively little contribution to generating growth other than providing what the World Bank (1997) calls "fundamentals," such as unleashing the private sector in pragmatic steps; preparing infrastructure, energy, and raw materials needed for growth; and reforming institutions in response to new challenges. This may already be a great policy achievement but it is much less than what leading East Asian governments did to absorb technology and create new industries in their rapid growth eras.[8] The two Communist governments have been more reactive and less visionary in charting the development paths of their countries. FDI inflows and domestic private investments have been the driving force of structural change, with little effective intervention in the productive sector from the state. Private industries have developed where the state receded.

On the question of balancing growth with social issues, Deng Xiaoping's China (in power 1978–1997) clearly prioritized growth policies over social policies, and brilliantly succeeded in accelerating growth in the 1990s. However, inevitable consequences of fast growth such as inequality, environmental damage, corruption, internal migration, and asset bubbles emerged subsequently to haunt the government. It can be said that the political legitimacy of the Chinese regime now hangs critically on solving these social problems rather than further accelerating growth. In fact, growth has been sufficiently high, and the management of the speed and sectoral content of growth is largely beyond the ability of the Chinese government.

Unlike China, which made a clear shift from growth-first policy to a more balanced policy, Vietnam has long pursued both growth and social objectives with equal weights, and therefore has not made any detectable policy shift in this regard. Poverty alleviation, assistance to ethnic minorities, and regional balance in public investment have always been emphasized. In the future, however, political legitimacy of the Vietnamese Communist Party will also depend heavily on the government's ability to execute policies to cope with social problems similar to those in China, in addition to sustaining growth. Burgeoning social issues in Vietnam include wealth gaps caused by land inflation (especially illegal land speculation based on insider information), rural-urban migration, environmental degradation, traffic chaos, and a triad of social evils (illegal drugs, prostitution, and HIV/AIDS).

In sum, the economies of China and Vietnam are being propelled and transformed by strong private forces, while official capability to manage these changes is yet to be demonstrated. Social transformation, as seen in South Korea in the 1970s and 1980s, is underway in both countries in terms of political culture and social structure. Political stability will depend more on proper execution of social policies rather than acceleration of growth. In the longer run, when income rises further, the political regime must also be adjusted. One option is to greatly strengthen the policy capability of the ruling party, in line with Singapore's People's Action Party (PAP), so as to continue to deliver growth and social achievements under one-party rule. Another option is to usher in political competition in manageable, gradual steps. If both fail, political change will have to be left to less controllable developments.

7 Democratic developmentalism?

When authoritarian developmentalism is mentioned in international conferences, there are typically two types of reaction. The first is acceptance and even praise of this regime as an effective tool for the development of latecomer countries. The second is rejection and abhorrence, with a strong conviction that democracy is sacred and should not be sacrificed in the name of development. Generally speaking, officials and researchers in East Asia who have witnessed the actual working of authoritarian developmentalism have far more favorable views of it than their Western counterparts, although exceptions do exist.

The statement that "the economic success of East Asia is largely attributable to the adoption of developmentalism, i.e., the ideology that places highest priority on economic development" (Watanabe, 1998, p. 204, English translation) neither invites protestation nor adds anything new to the common understanding of former economic officials in East Asian countries which executed such a strategy. However, there are those opposed to such a regime as a matter of principle. Some believe that democracy and development are two separate matters that can be pursued independently from each other.[9] For example, Dani Rodrik (2006) states:

> I do not think there is any tradeoff [between economic growth and democracy]. I do not think the reason democracy is valuable is exclusively or mostly for economic reasons. Nor do I think any country in the world is poor enough that it cannot afford to have democracy or better observances of human rights. I believe that empirical evidence supports that a country does not have to pay an economic cost or penalty when it makes the transition to democracy. I do not subscribe to the idea that you need to delay democratization just so that you can actually have growth or that you can have democracy only when you can afford it … I also do not think that democracy is a precondition of economic growth. I think democracy is good for a whole lot of things. The sooner you can have it the better. Democracy is a largely different issue than the question of development in the narrow economic growth sense.

Others regard the idea of authoritarian developmentalism as defunct. For example, Robinson and White explain:

> This view [that authoritarian states are needed to achieve development in poor countries] lost credibility in the face of a number of developments in the late 1980s and early 1990s. First, the developmental success of a small group of established democracies (Botswana, Malaysia, and Mauritius) demonstrated that democracy (albeit in a formal, procedural sense) and development were not inherently incompatible … Second, the patent developmental failure of the vast majority of authoritarian regimes in Africa and Latin America demonstrated that only a particular variant of this type of regime—the developmental state—could successfully promote sustained economic growth, under a highly contingent set of political and institutional conditions that were not easily replicable elsewhere …
>
> (Robinson and White, 1998, p. 1)

The view that East Asia's past regime cannot be transferred elsewhere prompted a search for the democratic developmental state, in which development is realized in a political context where broad participation is permitted and a pro-poor agenda is prioritized. However, it seems that this quest still remains theoretical and preliminary, and in need of strong empirical backing before the idea becomes feasible and operational in the political reality of low-income countries. For example, one proposal is to build a solid and stable development coalition based on the political support of poor peasants rather than industries and bankers. Another proposal is to install social democracy in poor countries, which tries to combine growth and social justice, rather than liberal democracy, which tends to promote exploitation and inequality.

However, a few basic facts from East Asia, where remarkable development was actually carried out under globalization, should not be forgotten. High-performing economies in East Asia did not initiate growth with broad inclusion, for the reason that quick and decisive actions were needed to break away from the poverty trap (Section 5). Their power base was narrow and included capitalists only. The experience of these economies shows that both markets and democracy grow slowly and in steps, and that economic development usually precedes political development in latecomer countries. The working mass becomes a formidable political force only after a certain level of industrialization is achieved and the necessary political culture and social structure are prepared (see South Korea, Section 6). It is difficult to assume that poor workers and landless farmers in low-income countries can behave as effectively as voters in developed democracies. Premature decentralization runs the risk of repeating the failure of the populist model (Figure 2.3) or causing the basic functions of the state to disintegrate.

Instead of conjuring up a developmental state which never existed in history, our suggestion is to start with the East Asian model but with significant modifications to make it more "democratic." For this, it is necessary to decompose democracy into various components and retain those that do not conflict with immediate requirements of development. In this sense, we concur with Robinson and White (1998, p. 5) that "parts" and "fragments" of democracy should be selectively combined to build a democratic developmental state rather than trying to devise a holistic democratic system.

In the narrowest sense, democracy is said to exist if political representatives are chosen in free elections and the minimum level of human rights are guaranteed. For our purpose, however, the scope of democracy should be broadened to include the following components, which collectively define this political regime:

- *Purposes*—freedom, basic human rights, equality, security, social and economic benefits for all, ethnic and regional coexistence, and so on.
- *Procedural requirements*—legitimacy (election as a means of transition), rule of law, participation, multi-party system, balance of power among legislature, executive and judiciary, local autonomy, transparency, accountability, and so on.

- *Supporting attitudes*—mutual respect, compromise, tolerance, non-violence, patience, and so on.

With these multiple components in mind, the existence of democracy is not an all-or-nothing choice but a matter of degrees. Moreover, different types of burgeoning democracy may be constructed by selecting different components to suit the local situation. Historically, authoritarian developmental states restricted some of these components—such as freedom, election, rule of law, and multi-party system—to attain some goals—such as national security and social and economic benefits for all. Not all components of democracy had to be suppressed to ensure agility in resource mobilization and crisis management. We can legitimately ask whether the scope and amount of suppression are reasonable for the purpose of accelerating growth in each local context.

For example, freedom to criticize the government was not fully granted in authoritarian developmentalism, but random arrests, torture, and execution of political enemies at the whims of a dictator should never be allowed. Many of the procedural requirements listed above, such as free election, participation and balance of power, also tended to be restricted in such a regime, but the same principle should also apply to examine whether these restrictions were "appropriate" for the purpose at hand. In low-income countries, some deviations from the Western norm may be tolerated, such as legitimacy through delivering peace and prosperity rather than through free and clean election, dominance of the executive branch, and lack of decentralization and local autonomy, provided that they are moderate, conducive to economic policy making, and for the apparent purpose of benefiting all social groups.

Clearly, which restrictions are moderate and which are excessive is subject to judgment and also dependent on the development stage. Surely, there will be tension between those who prioritize growth and those who value democracy highly. However, if we accept the notion that democracy is not a static goal but a dynamic process requiring constant policy and popular effort for survival and improvement, just like the market mechanism requires long-term policy and popular effort to grow, the fact that there is no uniform requirement for democracy for all developing countries should pose no big problem.

Perhaps democratic developmentalism is a regime that places much greater weight on democratic components at early stages of development compared with East Asia's authoritarian developmentalism in the past. Under democratic developmentalism, the government must exercise strong self-control in imposing restrictions supposed to be helpful in conducting economic policies, and the situation should be constantly monitored by domestic and international watchdogs. If so, differences between democratic developmentalism and authoritarian developmentalism are a matter of degrees. East Asia's authoritarian developmental states also exhibited a wide range of political practice from the very suppressive Park regime in South Korea to the far more "democratic" rule of Dr. Mahathir in Malaysia.

Since 2008 the author has led industrial policy dialogue between the Ethiopian government and a joint team of the National Graduate Institute for Policy Studies (GRIPS) and the Japan International Cooperation Agency (JICA). This policy dialogue was requested by Prime Minister Meles Zenawi and has been held quarterly until 2011 and semi-annually since then, covering a wide variety of issues from political regime to specific sectors and policy tools with extensive discussion of East Asian experiences. Ethiopia's democratic developmentalism rejects the notion of small government and regards a strong state as the leading agent for punishing rent seekers and encouraging value-creating entrepreneurs and investors. With smallholder peasants, accounting for over 80 percent of the population, as its political ally, the ruling party goes to election every five years with the conviction that its policy performance will keep them in power. Small farmers, together with micro and small enterprise owners, are targeted as drivers of productivity, commercialization, and export. But Ethiopia also promotes medium and large industries and develops industrial zones for attracting FDI. After a number of sessions and a few letter exchanges, Prime Minister Meles insisted that Ethiopia's democratic developmentalism was different from East Asia's authoritarian developmentalism, which aligned with large capitalists and refused election, but he also admitted that the difference was smaller than the distance between his regime and a pure democracy or a pure dictatorship (JICA and GRIPS, 2011).

Both democracy and market should be viewed in relative and pragmatic light with deep understanding of local and global context, not as ideological preconditions that must be imposed on all countries. Both grow slowly as policy, institutions, and people's mindset supportive of their growth are gradually constructed and take root. Moreover, the two are in complex interaction whose precise mode depends on local conditions as well as global trends, which invalidates any simplistic proposals such as democracy must go first or development justifies all suppression. Appreciation of this complexity may be the most important lesson from the experiences of East Asia.

Nation building requires hard policy learning. Backed by an extensive review of international best practices (and worst failures) in development policies and regimes, latecomer countries should choose and combine from a broad spectrum of political regimes instead of between full democracy and no democracy. Similarly, policy capability for economic development should be built up from a rich array of superior international practices. This is an important policy learning process that should be undertaken by all latecomer countries. The important question is whether the selected regime is suitable for the country, and whether national leaders and government are making a serious effort to embrace ever-higher levels of democracy as well as economic development at the right speed and sequence.

Notes

* The author has benefited greatly from the Japan–UK dialogue on ODA policy organized by the GRIPS Development Forum in Tokyo and London (2006–2007); comments at the IEA Roundtable Conference on the Political Economy of Sustainable Growth in Beijing, China (2007); comments at three workshops in Lusaka, Zambia (2007); industrial policy dialogue with the Ethiopian government (2008–2012); and class discussion in the GRIPS master's program (2006–2012). Previous versions of this chapter were presented to a number of development organizations including the World Bank, OECD, UNCTAD, Asian Development Bank, World Summit on Sustainable Development (Johannesburg, 2002) and at workshops in Tokyo, Beijing, Hanoi, London, Lusaka, Addis Ababa, and Yangon. I would like to thank Ms. Takara Tsuzaki for updating figures and tables.

1 At the risk of stating the obvious, it should be added that correlation does not necessarily imply causality, either from income to governance or vice versa. More information and analysis are needed to argue causality.

2 Since 2006, Thailand has faced political and economic difficulties following the ousting of former Prime Minister Thaksin. However, this situation may be temporary given that Thailand has grown fairly consistently in the past despite many political crises and a persistent urban-rural income gap.

3 Some of the old measures such as tariff protection, import quotas and bans, export subsidies, local content requirement, and foreign currency balancing requirement, are now prohibited by the WTO. However, many measures that do not violate WTO principles are still available, as listed in the text, and can be mobilized for industrial policy formulation today.

4 The only exception among the successful economies was the city economy of Hong Kong, which adopted a basically laissez-faire regime to achieve high income.

5 See Watanabe (1995) and Banno and Ohno (2010). The list of ingredients in the text reflects Watanabe's argument with minor modifications by this author.

6 Another reason may be that undemocratic means are necessary to stamp out patronage and rent-seeking which prevent economic growth. We do not deny this factor entirely, but do not at the same time over-emphasize it since even relatively corrupt and inefficient states can make a certain amount of progress in development. For an economic take-off, a discontinuous jump in governance or political development does not seem to be necessary (see Figure 2.1).

7 The major differences between China and Vietnam, other than size, are as follows: (i) historically, Chinese people have boasted superb mercantile talent and global trade networks, which Vietnamese people lack; (ii) China went through traumatic Cultural Revolution whereas Vietnam never had such an experience despite post-unification confusion and North–South psychological divide; (iii) Vietnam's ruling style is much more pluralistic and consensual compared with China's top-down decision making; and (iv) the Chinese history of socialist planning and industrial investment was much longer than in Vietnam, where wars prevented consistent execution of economic planning.

8 For example, the Korean government played an instrumental role, in close cooperation with chaebols and banks, in establishing steel, shipbuilding, and automobile industries. In Meiji Japan (1868–1912), the government vigorously promoted import substitution of marine transport, shipbuilding, cotton spinning, steel, production of locomotives and railroad cars, etc.

9 This view is diametrically opposed to the argument of Nguyen Thi Thanh Huyen regarding South Korea (Section 6 above), which contends that democracy is endogenous to the development stage.

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3 Understanding British aid to Africa

A historical perspective

*Tony Killick**

1 Introduction

This article utilises historical information to throw light on the forces shaping British aid policies towards Africa. It outlines key long-term policy developments, summarises the influences shaping these policies and comments on the present juncture of UK policies. It shows that, while there have been many influences, governments have enjoyed considerable policy autonomy, being largely unconstrained in pursuing their preferences in a top-down manner. This autonomy has mainly been used for the pursuit of long-term development, as against the promotion of the UK's national interest. The present thrust of UK policies to achieve massive increases in aid to Africa is a prime example of this policy autonomy.

This essay utilises historical information to throw light on the forces shaping British aid policies towards Africa. Section 2 summarises some of the key long-term developments in British aid policies towards Africa;[1] Section 3 attempts to summarise the influences shaping these policies; Section 4 comments briefly, in the light of the foregoing, on the present juncture of UK policies towards aiding Africa.

2 Elements of policy

2.1 Aid volumes and concessionality

The volume of direct British aid to Africa is constrained by the substantial level of its contributions to multilateral programmes including those of the EU. The multilateral agencies, of course, also provide large volumes of aid to Sub-Saharan Africa, of which the UK finances its share, but the following discussion is restricted to the bilateral element in British aid to Africa. The share of the multilateral element in the UK total rose strongly in the later-1970s and early-1980s and in recent years has fluctuated at around two-fifths of the total.

Aid to Africa, of course, is also influenced by what is happening to the UK's total aid programme. Relative to GNP, the total started at the

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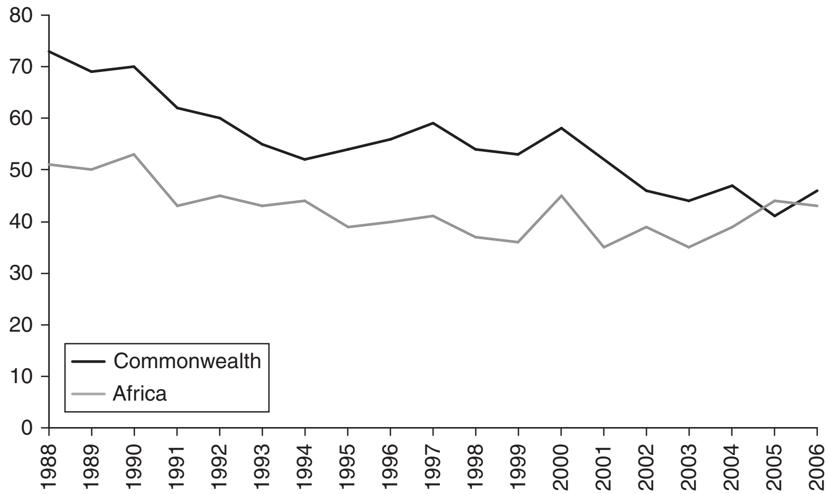

Figure 3.1 Shares of Commonwealth and Africa in total bilateral aid (%), 1988–2006

Note: These statistics relate only to DFID bilateral aid and hence exclude non-DFID debt relief and other forms of assistance provided by other government agencies. They therefore exclude large amounts of debt relief provided to Nigeria in 2005 and 2006, of £1.135bn and £1.164bn respectively.

relatively high figure of about 0.5 per cent in the mid-1960s, then went into fairly steep decline through to the mid-1970s, rose again in the second half of that decade, declined gradually but significantly during the 1980s and much of the 1990s, and has risen sharply since the later-1990s.

How did Africa fare in this context? In real terms, it did quite well, with only relatively modest declines during the retrenchments of the 1980s and 1990s. Figure 3.1 shows Africa's share declining gradually in the first half of the 1990s and then rising to the turn of the century, although note that this excludes humanitarian assistance. In the most recent years its share has stabilised at about two-fifths of the total. However, this was in the context of a rapidly-growing total budget so that the absolute (current price) value of UK aid to Africa more than doubled in 1995/96 to 2006/07.[2] Asia's share rose in the early-2000s, partly because of the emergence of Iraq as a major recipient, but has since fallen back again. The position today remains, as it has always been, that in relative terms Africa is strongly favoured over low-income Asia, as illustrated by the statistics for UK bilateral aid per capita in 2006/07 of £1.57 for Africa and £0.42 for South Asia.

Moreover, British assistance to Africa has always been highly concessional. For the last 20 years virtually all assistance to African (and other least-developed) countries has been in the form of grants, as against loans, but even as early as the mid-1970s UK aid to the least developed is recorded as having a 99 per cent grant element. The UK has also implemented an active programme of bilateral debt forgiveness, in effect converting past loans into grants, as well as supporting the international Heavily Indebted Poor Countries (HIPC) scheme of debt relief, from which African countries have been among the largest beneficiaries.

2.2 Modalities and end-use composition

The dominant form of financial assistance in the earlier years of British aid was to finance discrete development projects, to which was commonly linked the provision of technical assistance. For reasons discussed later, the dominance of the project mode in Africa began to diminish during the 1980s, with the emergence of various forms of programme assistance, generally in support of the 'structural adjustment' programmes of the IMF and World Bank (the international financial institutions or IFIs). The structural adjustment agenda gathered force in the 1980s and continued strongly into the 1990s. However, during the latter part of the 1990s there was a growing acceptance among donors, including the UK, that in Africa conditionality-based structural adjustment was bringing few of the intended benefits.

This realisation fed into a major re-think of aid priorities and modalities, in a landmark report by the Development Assistance Committee (DAC) of the OECD in 1996. Among other things, this report greatly enhanced the priority accorded to the objective of reducing poverty and related variables—a thrust which eventually evolved into today's Millennium Development Goals (MDGs). The DAC also placed issues of aid effectiveness more firmly on the agenda and this latter thrust helped to sustain the trend towards programme assistance, even though structural adjustment was running out of steam. Since the late-1990s, DFID has been among the more aggressive advocates of programme modalities, especially general budget support, as against projects.

How does the actual composition of British aid to Africa marry up with this description of global trends? We only have comparable time series from the late-1980s and these are not as helpful as they might be—see Figure 3.2. In line with the ministry's stated policy preferences, we see there a sharp rise in the share of bilateral aid provided in the form of general budget support in the early-2000s, with a nearly equivalent fall in the share of 'other financial' assistance. Although data are not available on this, it is likely that much of the latter decline was due to reduced amounts of project-specific aid, for the reasons just described. Notice, however, that general budget support's share did not further increase in the last period shown, even though DFID would surely have wanted it to.

The share of technical co-operation is shown as having been in decline since the late-1990s, which is again in line with DFID preferences, although it has remained largely unchanged in absolute terms. Even in 2006/07 £138 million was spent on this. The share of humanitarian assistance has become quite large and has grown rapidly in monetary terms, so that it accounted for no less than £225 million in 2006/07.

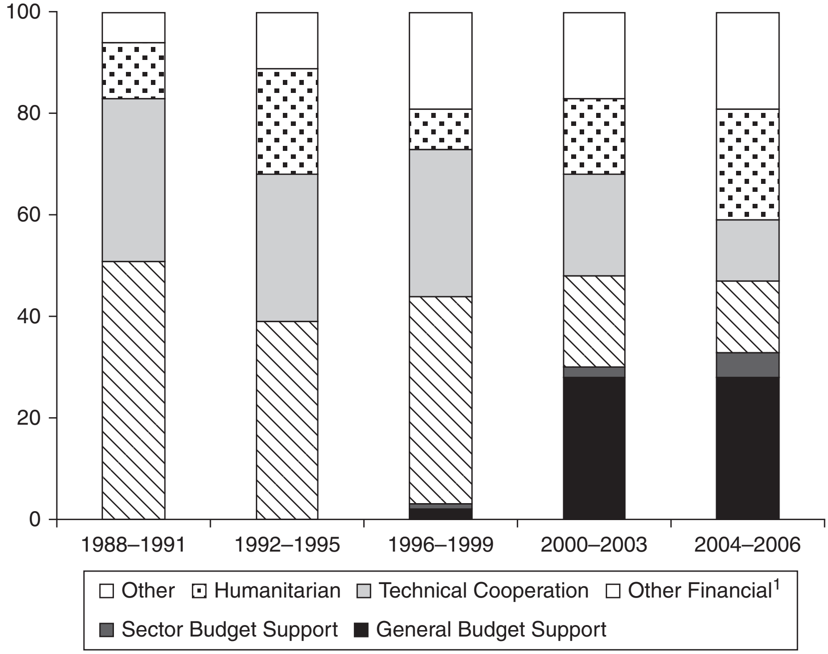

Figure 3.2 DFID bilateral aid to Africa by type
Note: 1 Includes DFID debt relief.

Turning now to the sectoral allocation of support, the figures in Table 3.1 show that recent trends have been strongly consistent with its chosen concentration on reducing poverty and promoting the MDGs. Even though covering only the most recent 20 years, Table 3.1 shows just how far the pendulum has swung away from assisting directly-productive sectors in favour of education, health and other social sectors. Note also the consistently very small share of environmental applications. Humanitarian assistance is excluded from the table; this is apt to fluctuate widely from year to year, but the data show an upward trend during the last decade.

An even more dramatic demonstration of change is given by the following figures, derived from Table 3.1, showing aid to Africa for what can broadly be described as investment in 'directly productive' activities (economic and rural livelihoods) as a percentage of 'social' spending (education, health, social and governance combined):

1988/89–1989/90	371%
1993/94–1994/95	208%
1998/99–1999/2000	49%
2002/03–2003/04	38%
2005/06–2006/07	29%

Table 3.1 DFID aid to Africa by sector of application (percentages of total)

Period[1]	*Economic*	*Social services*[2]	*Environment*	*Governance*	*Rural livelihoods*
1988/89–1989/90	66	17	3	4	10
1993/94–1994/95	57	23	3	8	9
1998/99–1999/2000	24	36	3	29	8
2002/03–2003/04	19	55	2	16	8
2005/06–2006/07	18	57	1	20	4

Note: Figures relate to current-price data on DFID bilateral assistance to Sub-Saharan Africa. The periods shown are to be read that the years in question refer to the financial year commencing in that calendar year. For example, '1988–91' refers to 1988/89 to 1991/92. These figures exclude humanitarian assistance and aid which could not be allocated by sector.
[1] The statistics are means of two-year periods.
[2] A combination of education, health and 'social' categories.

2.3 The evolution of policy priorities

An important feature of the administration of British aid is that, from the creation in 1964 of a Ministry of Overseas Development, execution of the great preponderance of the country's total assistance has been concentrated in a single department of government.[3] However, this does not mean that the disinterested promotion of social and economic development has always dominated the policy priorities of successive administrations. Aid has also, of course, been used to promote Britain's national interest. One obvious issue here is the standing of developmental considerations vis-à-vis foreign policy, security, immigration and commercial objectives. An important clue is provided by the fluctuating status of the government department responsible for aid, which is summarised in Table 3.2.

The points of substance beneath this apparent game of ping-pong were the signals the changes sent about the relative importance attached by successive governments to developmental and foreign policy objectives. Developmental considerations were more likely to be subordinated when the department formally came under the responsibilities of the Foreign Secretary, although the contrasts between the two situations were not in practice as dramatic as might have been expected. Even when part of the Foreign and Commonwealth Office (FCO), the department had considerable latitude in pursuing developmental goals, just as, when independent, it has been far from immune to the influence of foreign policy considerations. Party politics has been a strong influence in these matters, as is described in Section 3.

Just as the influence of foreign-policy-cum-security considerations has waxed and waned, so too has the influence of commercial motives. While these had always been present, the intrusion of commercial motives was given greater formal legitimacy with the introduction in 1977 of the Aid and

Table 3.2 Four decades of governments, prime ministers and aid administrations

Period	*Party and prime minister*	*Aid administration*
1964–70	Labour. Harold Wilson	Independent Ministry of Overseas Development created, with minister having a seat in the Cabinet (1964). Political status downgraded in 1967, with minister losing Cabinet status. Publication of White Paper: *Overseas Development: The Work in Hand* (1967).
1970–74	Conservative. Edward Heath	Department re-named Overseas Development Administration (ODA) and becomes formally part of the foreign affairs ministry (Foreign and Commonwealth Office—FCO), represented in Cabinet by the Foreign Secretary.
1974–79	Labour. Harold Wilson (to 1976) James Callaghan (to 1979)	Reverts to 1964 status—independent of FCO and with Cabinet-level minister. Publication of White Paper, *Overseas Development. The Changing Emphasis in British Aid Policies. More Help for the Poorest* (1975).
1979–97	Conservative. Margaret Thatcher (to 1990) John Major (to 1997)	Reverts to the 1970–74 status.
1997–2010	(New) Labour. Tony Blair (to 2007) Gordon Brown (to 2010)	Reverts to 1974–79 status, re-named Department for International Development (DFID) and with additional responsibilities in international economic issues which have a bearing on developing countries. Publication of three White Papers: *Eliminating World Poverty: A Challenge for the 21st Century* (1997) *Eliminating World Poverty: Making Globalisation Work for the Poor* (2000) *Eliminating World Poverty: Making Governance Work for the Poor* (2006)
2010–	Conservative–Liberal Democrat. David Cameron	

Trade Provision (ATP), which linked the use of aid funds with the provision of non-concessional export credits. This became an obvious target for critics, for what they saw as a misuse of funds intended to promote development, but it should be kept in perspective, for its use was limited to a maximum of 5 per cent of the total aid budget. Moreover, as it developed, it came to be applied largely to subsidise exports to emerging Asian countries and hence had little impact on aid to Africa. This explains the extremely high levels of concessionality in support to Africa reported earlier. The ATP scheme was formally discontinued in 2000.

Of considerably greater importance was the common practice of procurement tying. This meant that imports financed by British aid were restricted to goods and services originating in the UK, a form of protectionism which often much reduced the real value of the "assistance" provided and which effectively reduced its concessionality. In the 1980s nearly half of total UK bilateral aid (to all countries) was tied in this way, although this reduced in the 1990s and was applied to only about a seventh of total bilateral aid by 1996. It was abolished altogether in 2001.

Lessons of experience also led to changes. This was particularly the case with project-based and technical assistance modes of aid delivery, with neither of these now viewed as having been very effective, partly because of the high transactions costs which they involve. Along with other donors, the UK has therefore turned towards programmatic forms, as mentioned earlier.

British aid policies to Africa have changed in other major ways. Among the most obvious in recent years is the extent to which DFID's agenda has shifted from a project-led promotion of economic growth to concentration on the goal of poverty reduction and achievement of the MDGs. Indeed, DFID's mission statement is now officially summarised as to 'eliminate poverty in poorer countries, in particular through achievement by 2015 of the Millennium Development Goals' and the Public Service Agreement which it has with the Treasury defines its aims exclusively in terms of progress towards the MDGs and the reduction of poverty (DFID, 2005). The poverty goal is reflected in the shift in the end-use of aid to Africa away from directly productive economic sectors in favour of social services and 'governance' noted earlier. It is true that it was the 1975 White Paper which first gave prominence to the poverty-reduction objective but this was a less dominant theme and was viewed more in terms of rural development.

The nature of the relationships which the UK as a donor has sought to establish with recipient governments has also undergone substantial change. This has been partly the result of the waxing and waning of non-developmental foreign policy and commercial motivations. It has also resulted from the move from project to programmatic modalities. This shift first achieved prominence in the 'structural adjustment' era of the 1980s and earlier 1990s, when the IFIs were highly active in the placing of adjustment credits, especially in Africa, and when an increasing share of British aid was used in support of these. As this developed, relationships became increasingly based on donors' desire to improve economic and institutional policies within recipient countries, attempting to use financial leverage through the application of extensive policy conditionality. During the 1980s, the UK was largely content to piggy-back on the conditionality of the IFIs, especially the

IMF, generally making access to its own programme assistance conditional upon a country's continued satisfactory implementation of IFI adjustment programmes (Hewitt and Killick, 1996).

An extension of conditionality-based assistance occurred in the early 1990s with a sharply increased use by the UK and other bilateral donors (and with the IFIs this time trailing behind) of political and governance-related conditionality. In the words of the then Foreign Secretary, Douglas Hurd, in 1990,

> Countries tending towards pluralism, public accountability,[4] respect for the rule of law, human rights and market principles should be encouraged. Governments who persist with repressive policies, with corrupt management or with wasteful and discredited economic systems, should not expect us to support this folly with scarce aid resources.
>
> (quoted in Cumming, 2001: 176)

In practice, neither the IFI's policy conditionality nor the political conditionality of the bilaterals was pursued with consistent rigour and recipient governments quickly learned how to play the conditionality game without prejudicing continued inflows of assistance (Killick et al., 1998). It is perhaps not surprising, therefore, that a major feature of the 1997 White Paper was an announced move away from relationships based on conditionality in favour of more even-handed 'partnerships' involving mutual recipient-donor responsibilities. Policy and governance issues were still regarded as of central importance but these were henceforth to be based on local ownership, policy dialogue and mutual agreements among parties. An implication of this shift was also that the UK would henceforth be more selective in the African (and other) governments it supported, reducing its aid to those which did not meet minimum conditions of trustworthiness and desire to promote poverty reduction. However, it is not clear that there has since been any decisive move towards greater selectivity. Moreover, it has proved difficult to draw and maintain the line between a relationship based on conditionality and one rooted in ownership and partnership. It is likely that only in a few British-aided African countries has there been a clear and generally-recognised change in relationships, although DFID's desire is undoubted.

Lastly and related to the moves towards programme aid and policy dialogue, the substantial decentralisation that has occurred in DFID's operational structure has been another important development. In virtually all major African recipients, substantial financial and policy authority is vested in local DFID representatives, with reference back to London restricted to the most major or sensitive issues. A possible down-side of this is that DFID headquarters may now find it harder to secure uniform implementation of its policy intentions.

To sum up, it is evident from the above account that there has been quite a lot of fluidity in British aid policies towards Africa over the last four decades. Major movements have occurred in almost every dimension, although inevitably the reality of change on the ground has often been less dramatic than the observable shifts in headquarters policies. The main task of the remainder of this paper is to try to identify the main determining influences on the evolution of policy described above.

3 Determining influences

The long-term course of the policies of any institution is the result of interplay between inertial forces, tending to perpetuate the *status quo* and active forces for change. Policy-makers are constrained by history, by special interests which benefit from existing policies, by settled ways of viewing problems, by the perceived dangers or uncertainties of changing course. The extent to which they are free of inertial forces—especially the restraining hands of interest groups—shows the extent of their *autonomy*, a concept which became popular in the literature explaining the relative success of East Asian 'miracle' economies, where policy-makers were seen to have enjoyed substantial autonomy from special interest groups.[5]

In what follows, both inertial and proactive forces are described but what is already suggested by the policy fluidity described in Section 1 is that British aid administrators have enjoyed quite a high degree of autonomy, although more so at some times than others. The following account identifies three broad influences: historical; ideological and intellectual; and what is termed the global politics of aid.

3.1 The influence of history

British imperialism—and post-colonial guilt—offers an obvious starting point. A direct line can be traced back from the creation of the Ministry of Overseas Development (ODM) in 1964 to grants in aid provided to colonies from the 1870s. Such assistance was more formally organised under the 1929 Colonial Development Act and the Colonial Development and Welfare Acts of 1940 and 1945 (White and Wade, 1998). The provision of this support was intended to end as colonies became independent, with what would now be called development assistance then to be restricted to the provision of some technical assistance and contributions to multilateral institutions like the World Bank. The strength of the British anti-colonial movement, adoption elsewhere of bilateral aid programmes and a change of government altered that, however, and led to the creation of ODM in 1964.

Forty years later the influence of the UK's colonial history is still evident, even if it is gradually being eroded. The persistently large share of Commonwealth country recipients is illustrated in Figure 3.1 (page 54).

As recently as 2000 well over half of DFID's total bilateral aid went to Commonwealth countries, about the same as 10 years earlier. This share has since diminished but was still as high as 46 per cent in 2006/07, when 10 of the top 15 recipients were Commonwealth countries. Former British colonies in Africa have benefited from this bias. Ten of the top 15 recipients were African countries, of whom all but 3 (Ethiopia, D.R. Congo and Sudan) were Commonwealth members.[6]

The lingering influence of British imperialism, then, has acted as an inertial force. A more recent historical development, however, served as a spur to change. This was the end of the Cold War at the beginning of the 1990s. This undermined the *raison d'être* for supporting certain corrupt and anti-developmental regimes which, however, had enjoyed geopolitical importance during the period of East–West standoff—although this factor had not much influenced the distribution of British aid to Africa.

More widely, the end of the Cold War reduced the weight attached to foreign policy considerations in British aid allocations. It was not a coincidence that the political conditionality referred to earlier did not begin to assume prominence until the 1990s (Cumming, 1996, 2001). In principle, the collapse of communism as a possible threat could have brought a 'peace dividend' to the aid budget but the priorities of the government of the time did not favour that. Indeed, the decision of the incoming Labour government of 1997 to stick with the announced spending plans of its predecessor for two years meant that it was not until the end of the 1990s that the aid budget could begin a period of real growth—a rapid expansion which, however, was planned to continue at least until 2010.

History enters the story in another way too, through its influence on the course of British domestic macroeconomic policies. There were long periods during the post-Second World War period when, from today's perspective, successive administrations pursued inappropriate macro policies which, in turn, impacted on the scale of the country's aid budget. Thus, throughout much of the 1960s and 1970s governments sought to maintain relatively fixed ('adjustable peg') exchange rates which were inconsistent with governments' fiscal stances and the relative inflexibility of the economy. This led to sometimes acute balance of payments difficulties ('sterling crises'), which governments sought to resolve through imperfectly executed policies of financial stringency. As an economic advisor in the then Ministry of Overseas Development in the late-1960s, the present writer well remembers the balance of payments justifications offered for the squeeze on the aid budget of that time. The huge macro pressures that were generated during the first years of the 1990s by Britain's attempts to sustain a stable exchange rate at an inappropriately high rate through membership of the EU's Exchange Rate Mechanism are a more recent memory, as is the financial stringency which followed its collapse. Interestingly, the move since to a policy of market-determined exchange rate flexibility has assisted the aid programme, not only eliminating the foreign exchange constraint but also, via a competitive exchange rate, removing the last rationale for protecting British exporters through aid tying and the ATP.

Of course, Britain's aid budget is a small part of total state spending (under 1½ per cent in 2006/07), so it has always been possible to argue that it would not matter in macroeconomic terms if the government of the day chose to give priority to maintaining the aid budget even during periods of general financial stringency. It is certainly the case that the administrations in power in the periods when aid was in decline—the second half of the 1960s, the 1980s and much of the 1990s—demonstrated a relatively low regard for aid (Mrs Thatcher, who was premier for much of the latter period, famously dismissed it as 'hand-outs') but even with good will it could be electorally difficult to justify such special treatment when the domestic provision of state services was being squeezed. As it is, although the existence of an aid budget enjoys considerable public support, questions about the level and composition of aid have had little influence on general election results.

3.2 Ideological and intellectual influences

The last paragraph brings us naturally to consideration of ideology and party politics. The design of aid strategies and the specifics of policy have, by and large, not been the subject of any deep disagreement between the two main political parties, although differences have arisen in the past on the extent to which aid should be used explicitly to promote British interests and on the desirable scale of the aid budget.

As regards the pursuit of British interests, the main contrast that is often drawn is between the view of successive Conservative administrations during 1979–97 and their Labour predecessors and successors. Although the Conservative administrations chose not to fully articulate an aid policy, it was significant that early on, in 1980, the then Minister for Overseas Development, Mr Neil Marten, announced the intention to 'give greater weight in the allocation of our aid to political, industrial and commercial considerations, alongside our basic development objectives'. Although developmental concerns throughout were still accorded considerable weight and most Conservative ministers responsible for aid were generally held in good regard within development circles, there was a real shift of emphasis, a greater willingness to use aid to protect commercial and investment interests and to promote such foreign policy objectives as maintaining the UK's leadership role in the Commonwealth and its permanent seat on the UN Security Council. Conservative ministers of development shied away from giving more prominence to the goal of poverty reduction for fear of an adverse reaction within their party.

That these were real differences has been demonstrated by the changes introduced by Labour since 1997. As we have already noted, tying and the mixed-credit ATP scheme have been ended. The status of DFID—and its ability to resist pressures from the ministries responsible for foreign affairs and trade—has been enhanced. In fact, one of the ways in which party politics has played out over the years has been over the status enjoyed by the aid administration. The history of this was set out earlier (Table 3.2), one of the main points at issue being the extent of independence which the department should enjoy from the foreign policy establishment. Historically, Labour stood for a relatively strong and independent aid ministry, the Conservatives for a weaker department formally located within the FCO, although that is not the Conservatives' position today.

Another important change, already noted, was that aid tying and the mixed-credit ATP scheme were ended—perhaps the clearest indication of the degree of autonomy of aid policy-makers which is the theme of this essay. It is worth speculating on why it proved possible to make these changes without any large public controversy. A number of factors came together to produce this result. First, the British political culture gives rise to an executive power which is large vis-à-vis special interest groups. Such groups have influence, of course, and some in earlier periods have had major power (e.g. the trade unions in the 1960s and 1970s) but governments are usually able to implement policy changes which they regard as important even in the face of interest-group opposition. Second, by no means all British industry is protectionist (tying, of course, is just a form of protectionism) and protectionist lobbying had to be set against the anti-tying propaganda of campaigning NGOs. Third, as evidence accumulated on the high costs of tying to recipients, the British experience was that only a relatively few firms, mainly in the construction and power equipment industries, actually benefited much from it, so the base of their support within industry was not broad.

Fourth, the credibility of the old defence of tying—that it should be retained as a bargaining weapon in efforts to induce other donor governments to reduce their tying—became seriously eroded over time, as other donors continued to drag their feet. Fifth, as noted earlier, the change to a competitive, market-determined exchange further eroded the intellectual case for protection. Sixth, the shift away from project-based aid in favour of more programmatic forms meant that, in any case, there were fewer opportunities for tying. Finally, there was the sheer inefficiency of using an aid programme as a way of supporting domestic industry. If the government wished to engage in protectionism, it was seen as more efficient (to the extent that protectionism can ever be described as efficient) and equitable to do so through the normal instruments of unfree trade, rather than using a spending programme ostensibly intended for quite different purposes.

In any case, within the UK, since 1997 the primacy of developmental considerations has been powerfully reasserted, not least through publication of three White Papers and supporting legislation. In fact, the 2002 International Development Act made it unlawful for British aid to be used for any purpose other than the furtherance of sustainable development or improving the welfare of the populations of assisted territories. Interestingly, these changes were not the subject of much party-political controversy. The

Conservative response to the seminal 1997 White Paper was muted but essentially supportive. More recently, the Conservative Party has formally pledged to match Labour's commitment to achieving the UN target of an aid programme equivalent to 0.7 per cent of GDP by 2013 (although with more of it going through bilateral programmes). Indeed, in the specifics of aid policy, there has throughout been a degree of consensus between most interested members of both parties.

We should also not neglect the changes that can be brought about by Ministers with political standing and strong personalities. The first candidate here was Barbara Castle, appointed Minister when ODM was created in 1964. Lynda (now Baroness) Chalker proved a good friend of Africa during her years as Minister, 1989–97. A more recent example is Clare Short, Secretary of State from 1997 to 2003. Without question, her political strength and willingness to fight her Department's corner within government had a great deal to do with the changes that occurred in British development policy under the Blair administration, albeit with the strong support of the Prime Minister and Chancellor of the Exchequer, and subsequently Prime Minister, Gordon Brown. As her former Permanent Secretary has written, the incumbency of Clare Short meant a change 'from Administration to Delivery', to a far stronger focus on getting developmental results (Vereker, 2002).

What have these political-cum-ideological influences meant specifically for aid to Africa? Obviously, as discussed earlier, what happens to the total aid budget has a strong bearing on how much can be provided for Africa. Beyond that, a more aggressive use of aid to promote British interests, under Conservative administrations, might have favoured economically and politically more important countries in Asia but the sheer number of African countries meant they were bound to carry weight when Britain looked for support at the UN or in the Commonwealth. In the design of aid policies towards Africa, it is not clear that inter-party differences have made much difference.

Changes in the intellectual climate have had more impact. Evolving perceptions of the meaning and nature of 'development', and of how aid can best contribute to this, have certainly fed into the redesign of aid policies. In the 1960s and beyond, an economistic view dominated, in which development was largely seen in terms of economic growth, with the pace of growth largely viewed as a function of the rate of investment. Poor countries were seen as having limited saving capacities, resulting in major gaps between domestic investible resources and the volume of investment required to raise per capita incomes at an acceptable pace. Aid, then, was to help fill this financing gap (and also a foreign exchange gap). One way of ensuring that aid was indeed used for investment (it was then believed, before the subversive notion of fungibility took hold) was to devote it to the financing of development projects, hence the dominance in this earlier period of the project mode in aid delivery.

In this period the UK, like others, was concerned to get out of budgetary aid and to use projects to boost official development expenditure—on education and agriculture as well as infrastructure. There was heavy emphasis on technical and administrative assistance, to build up African cadres to replace British technical assistance personnel. Faithfully reflecting the dominant view of the time, aid administrators believed in the efficacy of a state-led 'big push'.

Thinking about development has since moved on in many ways that have had a bearing on aid policies. A more multi-dimensional view is now taken, with social, quality-of-life and 'governance' variables now also seen as central, alongside economic ones. While poverty has always been a concern of development economists, there is now much less willingness to take for granted that economic growth will provide a sufficient solution, not least because poverty is now viewed as involving more than material deprivation, with important non-economic dimensions. Even in the economic sphere, experience has taught that there is more to achieving growth than simply maximising the rate of investment: the quality of investment decisions, the productivity of past investment and associated rates of technological progress are all important. In turn, these variables came to be seen as crucially determined by the policy environment, and a more sceptical view was taken of the efficacy of the state as an economic agent.

Among students and some practitioners of development, there has also been a growing awareness of the limitations of what can be achieved by external assistance, and of the centrality of domestic sources of change within poor countries (although the most recent developments imply a return to the aid-optimism of an earlier time—see Section 4). It is this realisation, partly fuelled by the perceived ineffectiveness of conditionality and financial leverage, which lies behind the present-day emphasis on the salience of domestic ownership of policies and institutional development. Thus, a DFID policy document states explicitly, 'The UK Government accepts the evidence that conditionality cannot "buy" policy change …' (DFID, 2005, para 5.13).

Mention should also be made of the existence within the UK of a strong and increasingly sophisticated group of civil society organisations which have been supportive by raising public awareness of the problems of Africa (e.g. by mobilising the public during the Ethiopian famine of 1984) and other poor countries. Although these bodies have not always enjoyed the influence to which they aspired, they have undoubtedly had a strong bearing on specific UK policies relating to the quality of aid (for which the Independent Group on British Aid was an effective lobby during the 1980s and into the 1990s). The umbrella NGO group Jubilee 2000 was highly effective in campaigning for debt forgiveness at the turn of the millennium, while well resourced and organised NGOs like Oxfam and Christian Aid exert an ongoing influence through research-based campaigning.

3.3 The global politics of aid

It is sufficiently well known to need no elaboration here that, by comparison with other developing regions, Africa has emerged as the most problematical and the biggest challenge to all who aspire to end poverty in the world, although this is subject to the usual caution against over-generalising about a continent that actually contains a wide range of experiences. The long-term lagging pace of growth and development in much of Africa, the tendency for poverty to increase overall, rather than decline, its record of failed states, of international and internal conflicts and associated mass movements of refugees, is well known. It is this which explains the extent to which international aid efforts became especially concentrated on Africa during around the turn of the century. The UK, as shown earlier, shared in this concentration.

Conditions in many African countries also help explain other aspects of the changing policies recorded above. These include the extremely high levels of concessionality and provision of debt relief, the retreat from project assistance, the intense focus on structural adjustment in the 1980s and beyond, the growing interest in issues of 'governance' and institution-building, and the rise in the scale of humanitarian assistance. To a substantial extent UK policy changes have been a response to conditions in Africa, its limited access to global capital markets and the slow progress of much of the continent.

British policies have also been shaped by other agencies working in the aid field. The IFIs have been particularly important, not least through their influence on the changes in attitudes towards development sketched earlier. The direct influence of the IFIs on British policy during the structural adjustment phase of the 1980s–1990s has already been noted, formalised by cross-conditionality between country execution of IFI (especially IMF) adjustment conditionality and access to British programme aid. It is similarly said that the theme of the 1975 White Paper on the need to meet basic needs was a result of work by the Bank's staff. More generally, the Fund has been important in changing developing-country attitudes towards the importance of sound macroeconomic management, while the Bank's research and publications have influenced thinking about many aspects of development. The IFIs have exerted influence in more personal ways too. It is likely that Clare Short was influenced by her good relationship with the Bank's President, James Wolfensohn. And both IFIs have provided key individuals to work within DFID in recent years.

In parallel with this, the Development Assistance Committee (DAC) of the OECD has been working quietly, trying to induce bilateral donors to co-ordinate better and to reform practices, like tying, which reduce the value and effectiveness of aid. For long an ineffectual talking shop, the DAC has become somewhat more influential over the past decade, as concerns with aid effectiveness and transactions costs have grown. A process was initiated which culminated in the formulation of the MDGs and then adoption of the 2005 *Paris Declaration on Aid Effectiveness*. The work of the DAC and the views of other members of that Committee have undoubtedly fed into the evolution of British policies, which are nowadays focussed around achievement of the MDGs and are strong on the desirability of donors working collectively to harmonise their efforts and to become more cost-effective. There have been other external influences too: various United Nations conferences (e.g. the 2002 Monterrey conference on financing for development), the work of the UNDP on country-level aid co-ordination and other UN agencies, the Development Committee, the Strategic Partnership for Africa, and others. 'Like-minded' aid ministers and their agencies—a shifting body of alliances—have also been influential at different times.

However, while these various donor-based activities have doubtless fed into UK policies, it is probably accurate to say that DFID and its predecessors, as among the most professional of the bilateral aid agencies, has been more leader than follower. From as far back as the 1970s successive Chancellors of the Exchequer, from both parties, took the lead in pressing for debt relief for poor countries. However, UK leadership has been at its strongest more recently, when, working with other 'like-minded' donors, DFID rather self-consciously sought a leadership role, in advocacy of harmonisation around the MDGs, in favour of direct budget support and other measures to lower aid's transactions costs, and working towards collective donor decisions to increase their aid budgets. In other words, participation in the various collective forums was more often seen as a platform than a source of external inputs into UK policies.

4 Conclusion and implications for the future

We have shown that there have been many influences on British aid policies, both generally and towards Africa. There have been some important forces making for continuity: the influence of the country's imperial past; the influence of commercial interests intent upon preserving trading and investment advantages; delays in turnaround leading to discrepancies between what headquarters says its policies are and what actually happens in the field.

Overall, however, it is change, not inertia, which marks the record of British aid policies towards Africa. On election to power, political parties have been relatively unconstrained in pursuing desired policies in a top-down manner—what we earlier called policy autonomy. What governments have wanted to do has, in turn, been influenced by the evolving intellectual climate, by what the IFIs and other bilateral donors are doing, and by the campaigns of civil society organisations. Parliament has rarely been much of an influence, because of the degree of cross-party agreement, because of the general weakness of Parliamentary scrutiny in the UK, and because the specifics of aid policies have largely been seen as technocratic matters in which Parliament has little expertise or interest. On the face of it, the relatively recent introduction of a Public Service Agreement between DFID and the Treasury could be seen as constraining the freedom of DFID's policy-makers but, at present at least, the goals written into this are highly congruent with the Department's own priorities (and were probably drafted by it), so it operates more as a constraint on any who would wish to dilute DFID's development priorities than it does on the department itself.

It is possible to go further, to say that, by and large, policy autonomy has been used for the pursuit of long-term development goals, as against the promotion of the UK's national interest. There are specific exceptions to this but it would be difficult to interpret the history of UK aid to Africa as a cynical and exploitative promotion of national commercial or foreign policy objectives. Development goals have been particularly dominant in the most recent years.

This policy autonomy is important in understanding the present juncture of British policy towards Africa, for the government elected in May 2005 has consistently pushed for massive increases in assistance to reduce poverty in Africa. It used its 2005 Chairmanship of the G8 and Presidency of the EU to push for a doubling of aid to Africa. The then Prime Minister, Tony Blair, initiated and chaired a Commission for Africa which backed calls for a doubling of aid to achieve the MDGs when it reported in the spring of 2005. Both he and his successor, Gordon Brown, continued to promote this agenda. Moreover, the government has demonstrated its commitment in its own expenditures, with DFID aid to Africa increasing two-and-a-half-fold between 1998/99 and 2006/07. No less notably, announced expenditure plans for 2007/08 to 2010/11 envisaged total aid to rise by nearly 17 per cent annually *in real terms*, in the context of a generally rather stringent fiscal settlement for most other aspects of state spending. Africa is expected to receive a full share of these increases.

To those who are sceptical about such a shift, it represents a reversal of the greater realism that emerged during the previous two decades about what can be achieved by external assistance and an implicit rejection of the primacy of domestic ownership. The intended scale of the operation and the enormous pressures to spend which it will create would, the critics argue, undermine the efforts of the recent past to enter into partnership-based relationships. On this view, by going beyond countries' absorptive capacities, it would also undermine efforts to improve the cost-effectiveness of aid.

Whether or not these fears are justified, the changes now planned by the government represent a prime example of the top-down policy autonomy which has been the theme of this paper. Of course, the change would not be unconstrained. Above all, the government wants to carry other donors with it and a good few of them are reluctant. Indeed, at the time of writing only Japan and the UK appeared to be meeting the commitments entered into at the 2005 Gleneagles G8 summit. However, it is clear that the government will go ahead unilaterally if necessary. The lead time between announcement of a major change and its implementation is bound to be substantial, just as DFID has found it difficult to shift further towards direct budgetary support as fast as it wishes. Moreover, there is likely to remain a strong Anglophone bias in DFID's aid programmes in Africa, although this is being diminished by the emergence as substantial recipients of such countries as Ethiopia and Mozambique.

There will be constraints, then, but nothing powerful enough to frustrate a governmental exercise of political free-will in favour of much more aid to Africa.

Notes

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1 'Africa' is throughout used to mean Sub-Saharan Africa.
2 This increase excludes exceptional amounts of Export Credits Guarantee Department debt relief to Nigeria in 2005/06 and 2006/07.
3 There were aid elements in the activities of the Export Credit Guarantee Department and the Commonwealth Development Corporation but these were always minor parts of the total, so that the policies of the aid department almost represent the totality of the picture.
4 For an attempt to strike a balance between these alternatives see the 2005 statement of policy on the use of conditionality (DFID and HM Treasury, 2005).
5 For an exposition of the concept of autonomy and an application to the East Asian case see Wade (1988).
6 The picture is made a little more complicated, however, by the fact that one of these Commonwealth recipients was Mozambique, a former Portuguese colony which, uniquely, opted to join the Commonwealth.

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4 The rise of the East

What does it mean for development studies?

*Hubert Schmitz**

1 Introduction

The world has changed dramatically over the last 30 years. The Second World has virtually disappeared. The Third World has gone in different directions, with some areas declining and other areas experiencing the fastest sustained economic growth in history. And the First World, so jubilant over the demise of the Second World (the fall of the Berlin Wall and disintegration of the Soviet bloc), is now struggling to maintain its high living standards against competition from the formerly poor countries in the East. The speed of industrialisation in China and other Asian countries is breathtaking. They are not just catching up, they have begun to drive the changes in the rest of the world. This article is particularly concerned with this rise of the East and asks what it means for development studies. Does development studies have a place in this new world? Which strands have something to offer, which strands should be discarded? What challenges need to be taken on for development studies to thrive and avoid becoming irrelevant?

The article starts by highlighting the rise of the East, focusing in particular on the growth and transformation of China. It then distinguishes between four broad strands of development studies and shows how each strand is affected by the rise of the East. It concludes by discussing the need for a new vocabulary to make sense of the new world and—closely related to this—the need to break through a psychological barrier: analysing how the former 'periphery' is now driving change in the 'centre'.

Because the issues raised are large and so as to keep the sweep, I have refrained from including literature references. In order to provoke discussion, I have also refrained from qualifying the main propositions with footnotes.

2 The rise of the East

It is only 30 years ago that the 'great proletarian cultural revolution' came to an end. The revolution made China materially and culturally poor but egalitarian in a way the world had not seen before. Today the country is

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booming materially and culturally, but it has also become a very unequal society. What happened in China over this period is unbelievable: 30 years of economic growth at a yearly average of 9 per cent. Without exaggeration, *Newsweek* calls it 'the most successful case of economic development in human history' (6 March 2006).

Full explanations of this growth and transformation have yet to emerge but the key factors seem clear.

Internally it was the unlikely combination of the ideas of Adam Smith and the Chinese Communist Party. Adam Smith's central message was that economic development depends on the depth of the division of labour which in turn depends on the size of the market. China's internal market is big and it is growing fast with the removal of internal barriers and rising incomes. The depth of specialisation within China is little recognised but it is becoming visible to any visitor to industrial clusters and the emerging 'commodity markets'. The contribution of the Chinese Communist Party lies in governing this market and controlling the transition to a new system. The Party experimented with transitional institutions, which made it possible to move in stages from a society without private means of production to a capitalist society, and which made it possible to move gradually from a centrally planned to a market economy.

Externally, the key explanatory factor lies in what one can call 'China plus'. The country's rapid success in global markets cannot be explained merely by reference to internal factors. One needs to consider China plus key neighbours; China plus Hong Kong and China plus multinational companies. To explain each in turn: first, the equipment and complicated components for many products 'made in China' come from neighbouring countries (in particular, Korea, Taiwan and Japan). Second, China's strength in transforming these inputs into final products is formidable but not sufficient; it was Hong Kong that provided the trade networks and logistics to link Chinese factories with their foreign customers. Third, China is able to move rapidly into producing more sophisticated products (in particular electronics) because multinational companies have established their factories—and in some cases also research and development (R&D) departments—in the country.

From a developmental viewpoint, China provides a fascinating case study of a country that was poor until relatively recently but is now catching up with the advanced countries very fast indeed. The speed and manner of this catching up is itself a very interesting topic, central to the development debate, and is one of the reasons why China has attracted much attention internationally. The main reason, however, for the global attention is that China's rise has major external repercussions. China and its neighbours have become the drivers of global change. At the Institute of Development Studies (IDS), the University of Sussex, it has led us to open a new line of research on what we are calling the 'Asian Drivers of Development'. We are trying to understand the enormous opportunities that arise for some but also the big threats confronted by others.

The positive and negative external effects are significant because three things come together: China's size, fast growth and openness. The first two are clear, the third less so. Trade in goods and services (imports plus exports) amounts to around 70 per cent of gross domestic product (GDP), compared with 25–30 per cent in the cases of the USA, Japan or the European Union. China's economic growth has required huge increases in imports and resulted in huge increases in exports. This combination of large size, rapid growth and openness is historically unprecedented.

The resulting effects are felt throughout the world. Countries in Latin America, Africa and the rest of Asia feel the difference, as do the advanced countries of North America and Western Europe. We have reached a new stage in the development of the global economy. The former periphery has become the driver of change in the (former?) centre.

Those tempted to rejoice might want to hold back with their celebration. Enormous new problems have emerged, both internal and external to China. Starting with the external: *feeding the dragon* requires natural resources, which China lacks. International resource wars loom over water and fuel. The internal problems are many, for example 16 of the 20 most air-polluted cities in the world are in China; inequality is increasing rapidly within cities and between regions; massive bad debts highlight the danger of financial instability. In short, there are doubts about the economic and political sustainability of further growth, but so far, there is little sign of a slowdown.

My own impression is that reference to the herd instinct is essential to help explain the current situation. Most Chinese investors, public and private, seem to believe that fast growth will continue; foreign investors, large and small, believe that China is the place to be, and the government matches this enthusiasm with massive infrastructure investment. So with one reinforcing the other, continued fast growth becomes a self-fulfilling prophecy. But there is no inevitability in this process. The Chinese government has the financial and political power to intervene. Over the last 30 years, it has used this power in remarkably shrewd ways—experimenting and finding unorthodox solutions in the process.

Whatever scenario one believes in for China and East Asia, there is little doubt that we have entered a new chapter in world history. But those taking the long view might say that history is merely getting back on track—with Asia resuming its superior and dominant place in the world. In contrast, this article is comparatively short term, stretching back over the last 30 years—or at the most 50 or so years when development studies began.

3 What is 'development studies'?

What does the rise of the East, in particular China, mean for development studies? This is the question driving this article. Answering this question requires defining what 'development studies' is. This is not an easy task. There is no agreed definition and controversy is inevitable if one tries to provide one. I adopt here a pragmatic definition which comes from observing what development studies institutes (e.g. members of the UK's Development Studies Association) actually do. They:

- study economies, societies, polities in Africa, Latin America and Asia;
- consider OECD countries only to the extent that they have an influence on or serve as reference points for African, Latin American and Asian countries;
- are (or strive to be) interdisciplinary and multimethod in their approach.

This descriptive definition has its problems. It gives the impression that development studies is a branch of Area Studies with specialists in, for example, East Africa or South Asia—on a par with specialists in, for instance, North America or Scandinavia. No doubt country- or region-specific expertise is considered important but most development studies researchers would claim that they have something more fundamental in common:

- the need for analytical frameworks and concepts which capture the different stages, structures and attitudes in Africa, Latin America and Asia, which are different from those found in OECD countries;
- the concern to understand poverty and inequality, analyse its causes and show ways of improving people's life chances, which are often much worse than those found in OECD countries.

Whichever way one defines development studies, any detailed discussion will quickly find the need to distinguish between different strands. Again there are different ways of identifying strands, none of them right or wrong, but more or less useful depending on the purpose of the exercise. Since this article is particularly concerned with the rise of the East and its implications for development studies, it seems important to pay attention to the strands which (continue to) analyse reality through the Western lens and those which regard Western dominance as the key obstacle for progress. But two other strands of development studies will also be examined. I will call them 'find your own way' and 'putting the poor first'. These four strands do not cover all work carried out under the rubric of development, but they capture major lines of work that have been carried out across the disciplines. I have deliberately kept away from disciplinary discussion. If there is any pride left in belonging to development studies, it resides in being able to observe strengths and weaknesses across the disciplines.

4 'West is best' or 'the overdue burial'

The first strand of development studies to be examined here is one which has been influential since the 1950s and continues to be so up to this day: adopting the Western lens. I refer here to those studies which analyse, interpret and measure by using a Western reference point. Often this reference point is an idealised version of Western practice: the achievement society, the market economy, parliamentary democracy, the innovation system. Typically, these studies ask in which respect does reality in, for example Bangladesh, differ from a model defined elsewhere (usually in the West); why does the reality not live up to this model? What needs to be done to close the gap?

Such questions pervade all disciplines. In sociology, the Western lens was particularly powerful because of the strong influence of modernisation theory. Development was seen by most modernisation theorists as the evolution from traditional to modern society. Progress could be assessed by indicators of modernity, derived from the experience of the most advanced modern society: the USA. Most contemporary sociologists would dissociate themselves from such thinking, but the practice of adopting the idealised Western lens remains surprisingly common in many lines of research and policymaking:

- Political science and the push for democratisation—Western-style democracy is considered so superior that it is thought legitimate to introduce it by force. Little consideration is given to other forms of participation which might look second best but turn out to be more meaningful to local people and give them the chance to find their own 'voice'.
- Economics and the investment climate—the rediscovery of the importance of economic growth has led to concern with improving the climate for investment. Particular importance is given to the institutional infrastructure (legally enforceable property rights and contracts). The concern with institutions seems right but using models derived from the West provides few insights for moving forward in countries where such institutions are absent.
- Innovation studies and the search for systemic gains—participating in the global economy seems essential for improving earning opportunities but how to escape the 'race to the bottom'? Competing by innovating is seen as part of the answer but does the innovation system approach (derived originally from Scandinavian experiences) provide a fruitful analytical and practical way forward? Probably not.

Many other examples could be given. Unfortunately, they are not limited to academia. They seem even more common in advisory and consultancy work. Overwhelmed by the complexity of the real world, the German consultant often retreats to what he knows best and derives his recommendations by comparing Central Java with Baden-Wuerttemberg. Japanese consultants seem no better. On the contrary, much of their work consists of lamenting that the developing regions are not like Japan and then making recommendations based on the Japanese experience. In some form or other they repeat the mistaken choice of the modernisation theorists: adopt the best practice of the most advanced region or remain underdeveloped.

I am not arguing here against learning from success. I have emphasised that the idea of 'West is best' (or 'Japanese is best') continues to be prominent. This seems problematic for two reasons. Transplanting ideas and practices without due consideration to differences in context rarely works. This is old hat but deserves to be repeated time and again. The second reason is new and brings us back to the central concern of this article. The legitimacy of adopting the Western lens always rested on the superior performance of the Western economies and societies. This superiority is increasingly questionable. China's growth record over the last 30 years is superior to anything Western nations have ever achieved in their long history. China's ability to manage the transition from a materially impoverished, centrally planned economy to an efficient state-governed market economy is superior to that of the obvious comparator: the Soviet Union. Even though the Soviet Union started at a higher level, and even though (or because) it adopted many ideas recommended by Western advisers, the ex-Soviet republics are being overtaken by China on many fronts.

The key point of this section is that the 'West is best' idea, which has long been suspect, has now lost its last bit of legitimacy. For a long time, this way of analysing and advising derived its justification from the superiority of the Western models and practices. Now that the East is out-competing the West and demonstrating more effective ways forward, using the Western model as a reference point—or the model to live up to—is hard to justify. The burial is overdue.

5 The West undermines

The previous section discussed—and dismissed—the influential body of literature which explicitly or implicitly sees development as progress towards idealised Western models. In the conventional political spectrum, this can be seen as literature leaning to the right. In contrast, much of the literature leaning to the left sees development as a process which has been disrupted, undermined or stifled by the West. This includes the classical theories of imperialism, which precede development studies, neo-Marxist theory of underdevelopment, dependency theory, world systems theory, and more recently, some of the anti-globalisation work, for example John Pilger's 2001 programme for ITV, *The New Rulers of the World*. In spite of differences between them, there is a common core: they regard the interaction with the West as the main obstacle to development.

What does the rise of the East tell us about this body of work? If one is restricted to a short answer, one has little choice but to dismiss it as overtaken by events. China trades intensively with the West (and everybody else), no other country has received more foreign direct investment from the West, no other country absorbs Western technology and design more enthusiastically, no other country sends more students to Western universities. China's fast growth would not have been possible without integrating deeply into a global economy dominated by the West. Bill Warren—the British Marxist who in the late 1970s and early 1980s so severely criticised his colleagues on the left—has won the argument: capitalism is fulfilling its historical mission in the developing world. More than that, in East Asia it has been so successful that it is now driving the change in the West.

A more detailed answer would be useful here. The writers in the imperialism/dependency/anti-globalisation strand are right to draw attention to the relationship with the West as important, but wrong to assume that the relationship is always negative. The outcome depends on the circumstances. For example, global value chain analysis suggests that the upgrading opportunities of local producers vary with the way the chains are organised. In the case of foreign direct investment, the outcome for national development depends on the terms which the state has been able to negotiate. The East Asian experience shows that national policy helps to be selective with regard to foreign direct investment and then harnesses the muscle of transnational companies to national development.

Some of this strand recognises that the outcome depends on the interaction between external and internal forces but proposes that the outcome is negative for the majority of the population. This proposition turns out to be right in many instances in Latin America but much less so for East Asia, giving rise to a host of new research questions for which we do not seem to have convincing answers: why is it that enterprises, local government and central government show so much more strategic intent in East Asia?

While it is right to draw attention to the importance of external forces, the new external forces come increasingly from the East rather than the West. This is why IDS has initiated the Asian Drivers programme. China in particular is driving global changes in:

- the quantity and direction of trade, resulting in major changes in relative prices;
- the way production and trade are organised, resulting in a shift in locus of coordination of global value chains;
- the location of innovation activities, prompting a shift in the global knowledge divide;
- global governance, leading to a new unstable multipolarity.

None of this is to suggest that these changes driven by the East produce better developmental outcomes. The outcomes are likely to vary a great deal.

Couching the change as being Western- or Eastern-driven has its problems. In some sectors, the success of China is due to Western companies' massive investment in factories, supplier development, research facilities and managerial and technical staff in China. In other sectors, East Asian companies have substantial investment in the West. And there are sectors in which new multinational companies originating from South Africa, Mexico, Brazil, India or Russia are challenging old and new leaders from the West and East. The corporate world has become truly transnational. Understanding this new corporate world is not easy, but critical for a revitalised development studies.

The idea that these transnationals will now rule the world is also unhelpful. In many sectors, there has been a major change from transnational conglomerates prioritising control to rapidly changing alliances of companies which prioritise core competence and strategic flexibility.

In many sectors, an organisational decomposition has occurred, not just in production processes but also in marketing and innovation processes. The much lamented decline in state powers has its parallel in fragmenting corporate power. The world is much less predictable and more exciting than most of us would have expected a few years ago.

6 Find your own way

There is another strand of development studies which not only survives but is boosted by the rise of the East. I call it 'finding your own way'. Like the other strands discussed before, it can be detected among writers from several disciplines. 'Find your own way' has been advocated by many, but as a research perspective, it has been practised surprisingly little. It certainly requires an open-mindedness which the two previously discussed strands do not allow.

Its most explicit author was the historian Alexander Gerschenkron. In his book *Economic Backwardness in Historical Perspective* (1962) he argued that latecomers have to plot their own distinctive path of development. Repeating what others have tried before is rarely possible because each country has its own specific internal conditions and because the rise of the early developer changes the external conditions for the latecomer. Analysis of early industrialisation in continental Europe led Gerschenkron to this conclusion. Ron Dore came to the same conclusion in his analysis of Japan: the country succeeded by not simply emulating the West. Non-blinkered analysis of the more recent East Asian experience takes us in the same direction.

The key feature of China's development strategy and that of other East Asian countries is that they did not follow models from elsewhere. In *Institutions and Economic Growth*, Stephan Haggard (2004) emphasised how East Asia succeeded through a long process of 'transition' that was highly experimental in nature. Similarly, Mike Hobday, in a 2003 review of Asian industrial development, concludes that it is diversity rather than uniformity in the institutional arrangements and development policy that characterises the innovation experience of the Asian Tigers.

The importance of step-by-step experimentation comes out most strongly in the Chinese experience of the last three decades. Yingyi Qian shows this convincingly in his article ‘How Reform Worked in China’ (2003). ‘Transitional institutions’ rather than ‘best practice institutions’ were the key. He stresses that the adopted institutions need to take account of the conditions at each stage of the reform process. In China, a market was created through a dual-track approach to liberalisation, enterprises were created through the non-conventional ownership of township-village enterprises and government was reformed through a particular type of fiscal federalism. These institutional innovations worked for a while and then had to be replaced. Not all of them succeeded but there was a common thread to those that did: ‘pragmatic innovation’ and aligning the interests of the newly enabled decentralised actors with those of the reformers in central government.

By implication, this strand of development studies, which stresses the need to find one’s own way forward, also warns us against seeking to replicate elsewhere what seems to have worked in East Asia. Each country needs to find its own way forward, based on understanding its own strengths and weaknesses and based on understanding the new external context which has been influenced in such a major way by the Asian Tigers and China.

In principle, proponents of this line of development studies should be able to push at open doors. Economics, the dominant discipline in development studies, has finally taken an ‘institutional turn’, recognising that institutions need more attention in research and advice. In practice, however, this has not led to greater space for context-specific solutions. As stressed by Peter Evans (2004), the attention given to getting the institutions right has led to ‘institutional monocropping’, advocating the same way forward in vastly different circumstances.

One of the main reasons seems to lie in the internal organisational dynamics of donor agencies. A large part of development research and advice is funded by donor agencies that operate in many countries. The agencies seek internal coherence around particular aims and approaches; they seek to disburse funds for activities which can be shown to promote these aims and use these approaches. There is thus a conflict between respecting diversity and the priorities of recipients on the one hand, and the agency’s internal aims and pressures on the other. Because of the need to disburse funds against deadlines, the scope for letting poor countries find their own way in their own time is constrained, particularly in aid-dependent countries. It remains to be seen whether the change to budget support will make a significant difference.

7 Putting the poor first

Some of the finest achievements of development studies lie in the analysis of employment, inequality and poverty in Africa, Asia and Latin America. These issues were put on the agenda of both the academic and policy debate by the three International Labour Organization Missions to Colombia, Sri Lanka and Kenya in the early 1970s. Ever since, development studies has been concerned with 'redistribution from growth' and with tracing the implications of policies or projects for poor people.

IDS is closely associated with this. When Dudley Seers asked in his 1972 article 'What we are trying to measure?', he brought out the importance of going beyond growth and measuring the implications for inequality and poverty. Today we have a sophisticated human development index (to which Richard Jolly—a former IDS Director—contributed so much) and we have a new participatory methodology for observing changes through the eyes of the poor (pioneered at IDS by Robert Chambers and the Participation Group). This is a proud legacy, which has led to reams of in-depth poverty analysis and has been very influential in the policy debate worldwide.

For many, this analysis of the poor has become the trademark of development studies. The mission is to focus on the poor and on the poorest countries. While filling a vacuum and reflecting strongly held values of researchers and practitioners, it has also become a problem. Targeting the poorest directly and immediately is often given priority in discussions of research design and funding. This leads to development studies being reduced to studying the dependent variable. I am not implying here that the poor are passive: there are impressive stories of the poor organising to defend their rights, as shown by the self-employed women's association in India, the street traders' union in South Africa or the landless rural workers' movement in Brazil. The point I am trying to make is that where development studies confines itself to the study of the poor, it runs the risk of giving up on understanding and influencing the forces, which bring about the big changes and differentials in wealth and poverty. This is not a straw man: some researchers have willingly cut themselves off from the big picture, others have failed to obtain funding because they did not deal with the poor directly.

How does all this relate to the rise of the East? If development studies defines itself as the study of the poor and of the poorest countries, then studying the rise of the East is not a central concern. Development studies would perhaps contribute to analysing poverty within East Asia, but would concentrate on the poorer countries in the rest of Asia, Latin America and in particular Africa. Many aid agencies have gone along this route. Should development studies as well? Should it concentrate on the 'rump' of the developing world?

In my view, this would be a grave mistake. It fails to recognise that China and the East Asian production system have become drivers of change worldwide, including Latin America, Africa and the rest of Asia. What is at stake is whether development studies is concerned with the dynamics that drive this change. Of course, what happens in the rest of the world is not only determined by the East, but this is where the main changes come from. And the effects are not just felt in Africa, Latin America and Asia, they are felt also, or perhaps even more so, in North America, Western Europe and Japan. It is a true revolution: what used to be part of the 'periphery' is now driving changes in the ‘centre’. Perhaps development studies should put this reversal on its research agenda. This would show that it has—at last—freed itself from its post-colonial origins.

Development studies is certainly well equipped to take on this new challenge. Unlike most other bodies of work it has a tradition of interdisciplinary analysis, of combining different methods and drawing on the tools developed by other disciplines.

8 Finding a new language

As shown in the course of this brief article, the rise of the East poses major challenges to development studies. I have suggested that one strand should be discarded, two need to reposition themselves and only one strand comes out strongly. No doubt, some of the arguments which led to these conclusions are controversial, but hopefully there is less controversy on what I would call the two minimum requirements for moving forward:

- more analytical space for detecting the ‘solutions’ which come up from below; and
- capturing the global changes which produce wealth and poverty.

The latter requires more than international studies, it necessitates enquiry along the global–local axis.

For development studies to reinvent itself and be at the forefront of new analysis, rather than a relic from the past, it needs to confront a number of further challenges. These challenges arise not just from the rise of the East but also from changes elsewhere. I will merely raise them here, without being able to go into detail, let alone offer solutions.

Current analysis and communication is hampered by poor language. The most frequently used categories such as ‘developed/developing countries’ or ‘North/South’ do not help us to understand the new world. Over the last 30 years, the former Third World has become so heterogeneous that the use of current categories becomes an obstacle. Brazil and Tanzania have very little in common. China and Sri Lanka similarly. The terms ‘newly industrialised countries’ and ‘least-developed countries’ are an improvement, but still not sufficient.

The most grotesque category is that of ‘industrialised’ countries for the countries of the OECD, given that de-industrialisation has been one of their main characteristics in recent years. In English, this has become less common but not yet in other languages, for example in German, ‘Industrieländer’ is the most frequently used term.

Creating a new language which is universally acceptable and has measurable categories will be difficult. A strong candidate is a typology of countries according to sources of state revenue. Such typology would help to bring about an overdue shift to more political analysis. At IDS Mick Moore has shown that state revenue based on taxation, as opposed to foreign aid or export of abundant raw materials, has a major bearing on the likelihood of state formation and effective government. There now seems a case for going one step further and using this line of work on taxation for a categorisation of countries. In discussing this and other candidates, some might worry about a proliferation of terms used concurrently, but this is unlikely to do more damage than continuing with the current language for distinguishing between (groups of) countries.

The problem of course is that there are enormous country-internal differences. Osvaldo Sunkel captured this very well in a 1973 article 'Transnational Integration and National Disintegration'. His central concern was to show the connection between, on the one hand, the economic and cultural integration across countries and, on the other hand, the economic and cultural disintegration within countries. This is precisely what happened in Latin America at the time. And is precisely what has happened in East Asia since then. The difference is that the transnational integration has been much deeper and wider in East Asia and the drivers of the process come increasingly from within the region. Why is it that Sunkel's combined analysis of transnational integration and national disintegration has not entered the mainstream of development studies and produced measurable categories to understand this process more deeply and comparatively? Perhaps the original article was too close to dependency analysis and its pessimistic conclusions.

The transnational integration keeps reproducing itself and the resulting process of inclusion and exclusion changes the world in a fascinating and outrageous way. Understanding this world requires a language which revolves around connectivity or the lack of it. Such language exists for example in global value chain analysis and in social network analysis, but it needs to be brought into the centre of the new development studies. The challenge is to understand:

- the business and professional networks that make transnational integration work;
- the disconnects and lock-outs that lead to misery and injustice, often across national borders;
- the new and invisible transnational networks that terrorise the world;
- the policy networks that need to be developed along the local–global axis.

This is not to suggest that we abandon a concern with the national or local state. What seems needed is a shift in paradigm about what the state needs to do. The critical capacity of the future state is the management of relationships. Managing relationships is not an end in itself but is critical for securing peace, integrating different cultures, accelerating private investment, delivering services to the poor and many other state functions. Once the management of relationships is at the centre of new analytical and practical work, it becomes more likely that we will escape futile linear ideas of policymaking and find a framework for dealing with the proliferation of actors that have an influence on policy.

Notes

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5 Governance and development

The perspective of growth-enhancing governance

Mushtaq H. Khan

1 Introduction

Most economists would agree that governance is one of the critical factors determining the growth prospects of countries. However, there is considerable controversy about governance priorities and the types of governance capabilities that are critical. These disagreements are related to fundamental disagreements on the role of markets versus other social, political and technological characteristics that need to be fulfilled for sustainable growth to take off. The contemporary good governance agenda is based largely on governance capabilities that are required to create the conditions for markets to be efficient. While these are important and desirable conditions, we argue that they are second order conditions, in the sense that without other state capacities that directly promote sustainable growth, market conditions for efficiency are on their own insufficient and ultimately unsustainable.

The point about sustainability of particular reforms is particularly important. There are a number of critical structural features of developing countries that prevent the achievement of significant progress on the good governance front. These factors make the good governance agenda doubly problematic: it sets many developing countries goals they cannot achieve, and in addition, even if they could have been achieved, these goals are not sufficient to ensure sustainable growth. The task of this paper is to outline some of the governance issues that we already know about, and identify other areas where more research is necessary to assist policy.

2 Three phases in the history of governance and growth policies

It is useful to recall that the consensus on economic policy and appropriate governance capacities for developing countries has gone through radical changes over the last 50 years. The first phase of growth and governance policies describes the economic strategies adopted by most developing countries from their decolonization at different stages of the last 50 years

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to sometime in the early 1980s. The concern of most developing countries and international agencies during this period was to accelerate the creation of growth-enhancing sectors in developing countries. However, they failed to give much attention to the development of governance capabilities appropriate for the effective implementation of these strategies. The governance discussion that did take place came from the modernization school that tried to justify the lack of democracy and the presence of corruption in many of the developing countries that had become Cold War allies of the US during this period (Huntington, 1968). Critically, there was no discussion within developing countries about the governance capabilities required to effectively implement the different growth strategies they were following.

The results of this first phase of post-colonial growth strategies were therefore very mixed. A few countries did break out of poverty in a sustained way by the late 1960s. These countries, like South Korea and Taiwan, emerged by the late 1960s as emerging economic giants (Amsden, 1989; Wade, 1990). A number of other countries like Brazil, Pakistan and India initially achieved much higher growth rates compared to their growth rates in the first half of the twentieth century. But in these countries productivity growth in the emerging industrial sectors was not high enough and there was a growing perception by the mid-1960s that these strategies were becoming unsustainable. But most worrying was a larger group of countries, many of them in Africa, where import-substituting industrialization resulted in much more limited growth and industrialization.

The results, while very encouraging for a small number of countries, were not widely-enough shared for this strategy to survive in many developing countries, or receive the continued support of international agencies. With the impending collapse of the Soviet Union, the Cold War imperatives of providing support to undemocratic and corrupt regimes also began to suddenly disappear.

A second phase of development policy dates roughly from the 1980s when structural adjustment began to be promoted precisely because previous strategies had resulted in serious budgetary crises in many developing countries. Rent seeking, corruption and other governance issues now became policy concerns, but the expectation was that liberalization would resolve these governance issues by removing the incentives for rent seeking. John Toye described this as the ‘development counterrevolution’ (Toye, 1987). The results of this phase of policy were, if anything, even more disappointing, with no discernible improvements in either the growth prospects of developing countries or their governance conditions.

While governance reform was not yet at the centre of the reform agenda, reforming the state was an essential component of the structural adjustment programme. However, it was believed that the reform of the state would follow from and be achieved through the structural adjustment itself, by removing the incentives for rent seeking and corruption. These ideas followed from the development of what came to be known as new political economy. This school was the result of many related theoretical contributions (Krueger, 1974; Posner, 1975; Bhagwati, 1982; Bardhan, 1984, Colander 1984, Alt and Shepsle, 1990; Lal and Myint, 1996; Bates, 2001).

The results of structural adjustment policies in the 1980s were generally very poor. Recessions followed in many African countries, and growth was poor in other countries that adopted these policies. More worrying was that despite significant liberalization and cutbacks in subsidies, together with privatization programmes in some developing countries, there was little apparent reduction in rent seeking anywhere. In almost every country where liberalization was carried out, there appeared to be an *increase* in corruption and rent seeking (Harriss-White, 1996; Harriss-White, and White, 1996). The realization that market-promoting governance capacities on the part of the state required specific attention led to the third, and current stage of governance approaches.

The poor performance of structural adjustment programmes in the 1980s led to the emergence of a new focus on the role of the state to ensure the conditions necessary for market economies to work efficiently. The development of *New Institutional Economics* had brought to the fore economic theories that identified governance capabilities that states needed to have to create the conditions for low transaction cost (efficient) markets. In addition, the poor performance in the 1980s and the growing perception of persistent poverty in developing countries also brought to the fore the requirement of pro-poor service delivery as a necessary capability for developing country states. The convergence of these different perspectives led to the emergence of a set of policy priorities for governance in developing countries that has come to be known as the good governance agenda.

Many of these governance conditions were also desirable on their own: low corruption, democratic accountability, the rule of law and pro-poor service delivery. With the end of the Cold War, many constituencies, including many civil society organizations in developing countries had been demanding these conditions in developing countries. The coming together of a large number of different constituencies behind the good governance agenda explains its impressive influence and hold in the development community. But while many people in developing countries demand good governance as an end, the governance policy agenda sees it as a set of preconditions to enable market-driven development to take off.

The new consensus builds on the earlier commitment to liberalization and market-driven growth, but now the development of good governance capabilities has come to occupy the heart of development strategy. As the good governance approach began to be adopted as the mainstream development agenda in the 1990s, a few countries had already been enjoying accelerated growth since the mid-1980s by finding niches in increasingly integrated global value chains. Most of these growth experiences were, however, based on already existing comparative advantages that some developing countries had developed. Economic performance in many of the poorest developing countries remains low, and growth in others is based on vulnerable low technology sectors and commodities that are sensitive to terms of trade changes and are unlikely to display the growth in productivity that is necessary to achieve sustainable improvements in living standards.

This brief look at the historical evolution of the good governance agenda highlights a number of critical observations. Governance capabilities are closely connected to the development strategies that states are supporting. The strategies many developing countries followed in the 1960s and 1970s are fundamentally different from the ones they are following now. There were successes and failures in each of our three phases and these can be related to the match or mismatch of the requirements of the economic strategy being followed and the governance capabilities that were required for effectively implementing it. To elaborate this critical observation, and to draw out the research and policy implications, we will first discuss the theory and evidence supporting the good governance agenda. We will then discuss the theory and evidence supporting a more extensive view of governance.

3 Theory supporting the good governance agenda

The dominant analysis of *good governance as a market-promoting governance strategy* emerged in what we have described as phase 3 of the development strategies attempted by developing countries. Government capabilities for delivering good governance were now argued to be essential for maintaining efficient markets and restricting the activities of states to the provision of necessary public goods so as to minimize rent seeking and government failure. The relative failure of many developing country states during the first phase of development strategy could be explained (by good governance theories) in terms of attempts by states to do too much. This resulted in the unleashing of unproductive rent-seeking activities and the crowding out of productive market ones. Empirical support in favour of this argument is based on cross-sectional data on governance in developing countries that show that in general, countries with better governance defined in these terms performed better.

The importance of markets in fostering and enabling economic development is not in question. Economic development is likely to be more rapid if markets mediating resource allocation in any country become more efficient. The policy debate is rather about (i) the extent to which markets can be made efficient in developing countries, and (ii) whether maximizing the efficiency of markets (and certainly maximizing their efficiency to the degree that is achievable in developing countries) is sufficient to maximize the pace of development.

Heterodox *growth-promoting* approaches to governance have argued that markets are inherently inefficient in developing countries and, even with the best political will, structural characteristics of developing economies ensure that market efficiency will remain low till a substantial degree of development is achieved. Given the structural limitations of markets in developing countries, successful development requires critical governance capacities of states to accelerate private and public accumulation and to ensure productivity growth.

In support of these arguments, heterodox economists point to the evidence of the successful East Asian developers of the last five decades, where strong governance capacities existed, but these were typically very different from the good governance capacities necessary for ensuring efficient markets. In fact, in terms of the *market-enhancing governance conditions* prioritized by the good governance approach, East Asian states often performed rather poorly. Instead, they had effective institutions that could accelerate growth in conditions characterized by technological backwardness and high transaction costs. The heterodox argument is that Asian success can be better understood in terms of a different set of governance capabilities that can be described as *growth-enhancing governance*. Growth-enhancing governance should not be confused with interventionism. Achieving market-enhancing governance also requires intervention. The question is whether the market efficiency *that can be feasibly achieved* in developing countries (through good governance reforms) is sufficient for achieving development or is an additional set of governance capabilities required?

Good governance reforms aim to promote governance capabilities that are *market-enhancing*: they aim to make markets more efficient by reducing transaction costs. *To the extent that these reforms can be implemented* they are likely to improve market outcomes in developing countries. However, there are structural problems that prevent significant implementation. Moreover, market efficiency does not address significant problems of catching up that require specific governance capabilities to assist developing countries move up the technology ladder. *Growth-enhancing* governance capabilities are capabilities that allow developing countries to cope with the property right instability of early development, manage technological catching up, and maintain political stability in a context of endemic and structural reliance on patron-client politics.

While both sets of governance capabilities are important, the first is not significantly achievable in poor countries and an excessive focus on these market-enhancing capabilities can take our eye off critical growth-enhancing capabilities important for development in these contexts. Ironically, effective growth-enhancing governance capabilities can create the preconditions for achieving good governance and greater market efficiency over time.

The distinction between market-promoting and growth-promoting governance does not need to be very starkly drawn, and it is not necessary for policy-makers to choose just one or the other. It has been unfortunate that a somewhat artificial chasm emerged between these positions with the growing dominance of the liberal economic consensus of the 1980s. Indeed there may be important complementarities between the two sets of governance

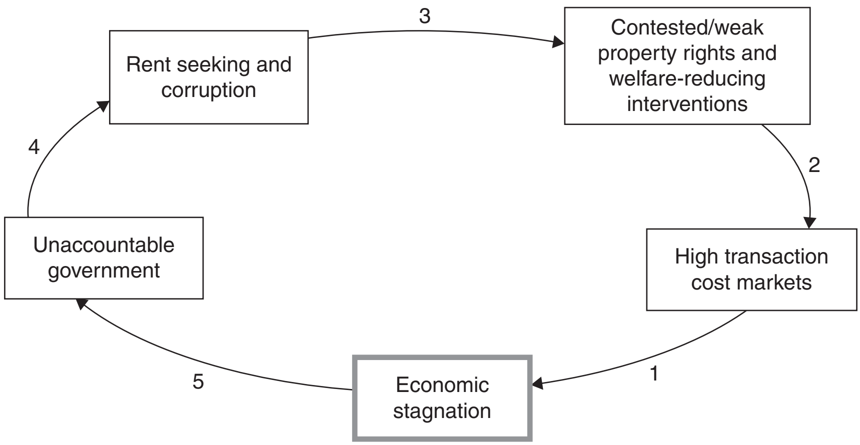

Figure 5.1 Theoretical linkages in the good governance analysis

requirements in specific areas, provided these can be properly identified and prioritized for policy attention. Our intention in reviewing the evidence is to show that market-promoting governance as a general goal for governance policy is (i) difficult to achieve to any significant extent in developing countries and (ii) is insufficient as a condition for ensuring sustained economic growth in developing countries. We will then review the evidence to see what we know about growth-enhancing governance and the policy implications that follow.

The consensus behind the good governance agenda draws heavily on a large body of theoretical contributions that were part of the New Institutional Economics that emerged in the 1980s. The significant theoretical contribution of this school was to point out that efficient markets actually require elaborate *governance* structures and will not just emerge simply because the government withdraws from the economy. Although the language varies across this literature, there is a broad consensus that the goal of governance should be to enhance these *market-enhancing* governance capabilities of the state (North, 1984, 1990, 1995; Matthews, 1986; Clague et al., 1997; Olson, 1997; Bardhan, 2000; Acemoglu et al., 2004). The main theoretical links identified in New Institutional Economics that explain economic stagnation are summarized in Figure 5.1.

The fundamental link in all market-focused approaches to development is link 1 in Figure 5.1: economic stagnation is explained primarily by inefficient markets. High transaction costs are simply a technical description of inefficient markets. These high transaction costs are in turn explained by link 2: weak and contested property rights and unnecessary state interventions. In the second phase of growth-governance policies, the focus of economic policy was limited to link 2 in Figure 5.1 and that too, on the

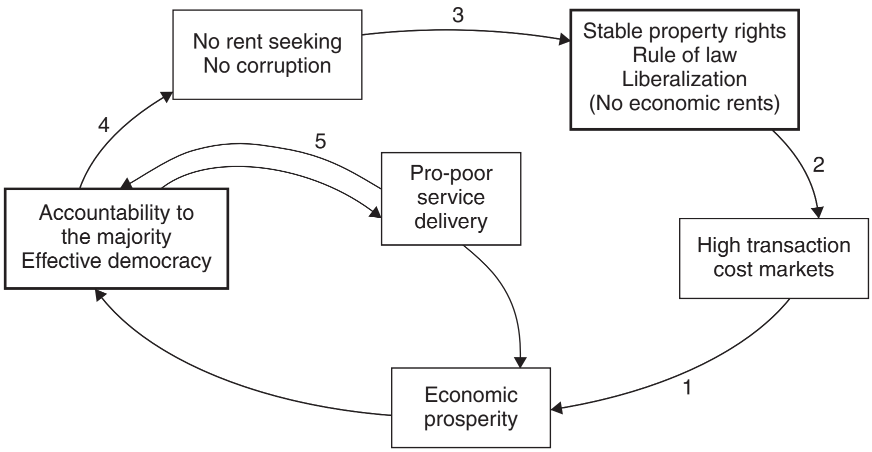

Figure 5.2 Policy links in the good governance approach

removal of unnecessary state interventions as a way of improving the efficiency of markets. As we discussed earlier, the expectation was that these reforms would suffice to make markets more efficient through link 1, as well as feed back to reduce rent seeking and corruption through link 3 in Figure 5.1 as these links operate in both directions and a reduction of intervention reduces the *incentives* for rent seeking.

The good governance agenda emerged in the third phase of governance policy to develop an integrated analysis of market efficiency (Khan, 2004). For the first time, the argument was that unless *all* the links in Figure 5.1 were simultaneously addressed, market efficiency would not improve. The logic was that rents and interventions could not be reduced unless rent seeking and corruption were directly addressed, and in turn, these could not be significantly tackled unless the privileges of minorities engaged in rent seeking and corruption that harmed the majority could be challenged through accountability and democratization. The policy implication was an integrated reform agenda summarized in Figure 5.2.

The first theoretical difference compared to earlier approaches was the recognition that transaction costs could be high not only because of government interventions, but also because governments lacked the capacity to reduce transaction costs by effectively protecting property rights and enforcing contracts. Progress required an integrated approach on links 3 and 4, to fight corruption and rent seeking that disrupted property rights and contracts, and to ensure accountability to fight corruption and rent seeking. A further theoretical development was the idea that pro-poor service delivery was a way not only of directly attacking poverty, but also of empowering the majority and creating expectations that would drive a popular demand for greater accountability.

Table 5.1 Contemporary governance priorities and their links to theory

Policies to improve accountability of government (arrows 4 and 5 in Figure 5.2)	*Policies to counter corruption and rent seeking (arrow 3 in Figure 5.2)*	*Policies to stabilize property rights across the board (arrow 2 in Figure 5.2)*
Poverty Reduction Strategy Paper & Partnership General Budget Support (in some countries), accountability reforms, decentralization	Anti-corruption policies, liberation, WTO restrictions on subsidies, IMF fiscal requirements	Policies to improve rule of law, reduce expropriation risk, strengthen judiciaries

Table 5.1 shows that all the main policy planks of contemporary governance and economic policy reform strategies are derived from the links shown in Figure 5.2. The contemporary reforms to improve accountability and pro-poor service delivery (links 4 and 5 in Figure 5.2) are the theoretical basis of reforms shown in column 1 in Table 5.1. Policies to counter corruption and rent seeking that are becoming increasingly important in World Bank strategies are derived from link 3, and shown in column 2 of Table 5.1. Finally, policies to strengthen property rights and the rule of law are derived from link 2 and shown in column 3 of Table 5.1.

The importance of the good governance perspective in informing contemporary development policy and discourse cannot be overemphasized. A powerful way of evaluating the appropriateness of the relationships between growth and governance asserted in the good governance agenda is to look more carefully at some of the data and evidence that is used by proponents of the agenda to support the programme.

4 The empirical evidence

The market-enhancing view of governance appears to explain the observation of poor performance in many developing countries attempting import-substituting industrialization in the 1960s and 1970s. Market-enhancing governance capabilities were poor in these countries, as was their long-term economic performance. However, the test that is required is to see if countries that scored higher in terms of market-enhancing governance characteristics actually did better in terms of growth. If they did, they would be more likely to *converge* with advanced countries. When we conduct such a test we find that the evidence supporting the market-enhancing view of governance is weak, even using the largely subjective indicators of governance constructed by researchers broadly sympathetic to the theoretical conclusions of the good governance analysis.

We find that these data tell us that while poorly performing developing countries did indeed fail to meet the governance criteria identified in the market-enhancing view of governance, so did high-growth developing countries. *These observations are fairly systematic, and hold for all the governance indicators and time periods for which we have any evidence*. The evidence suggests that it may actually be difficult for *any* developing country, regardless of its growth performance, to achieve the governance conditions required for efficient markets. This does not mean that market-enhancing conditions are irrelevant, but it does mean that we need to qualify some of the claims made for prioritizing market-enhancing governance reforms in developing countries.

Making sense of this data is particularly important since an extensive academic literature has used the same data to establish a positive relationship between market-enhancing governance conditions and economic performance (Knack and Keefer, 1995, 1997; Mauro, 1995; Barro, 1996; Clague et al., 1997; Johnson et al., 1998; Hall and Jones, 1999; Kauffman et al., 1999; Lambsdorff, 2005). This literature typically finds a positive relationship between the two, supporting the hypothesis that an improvement in market-enhancing governance conditions will promote growth and accelerate convergence with advanced countries. The studies use a number of indices of market-enhancing governance. In particular, they use data provided by Stephen Knack and the IRIS centre at Maryland University, as well as more recent data provided by Kaufmann's team and available on the World Bank's website. If market-enhancing governance were relevant for explaining economic growth, we would expect the quality of market-enhancing governance at the beginning of a period (of say ten years) to have an effect on the economic growth subsequently achieved during that period.

However, the Knack–IRIS data set is only available for most countries from 1984 and the Kaufmann–World Bank data set from 1996 onwards. We have to test the role of market-enhancing governance by using the governance index at the *beginning* of a period of economic performance to see if differences in market-enhancing governance explain the *subsequent* difference in performance between countries. This is important, as a correlation between governance indicators at the *end* of a period and economic performance during that period could be picking up the reverse direction of causality, where rising per capita incomes result in an improvement in market-enhancing governance conditions in high-growth countries.

There are good theoretical reasons to expect market-enhancing governance to improve as per capita incomes increase (as more resources become available in the budget for securing property rights, sustainably running democratic systems, policing human rights and so on). This reverses the direction of causality between growth and governance. Thus, for the Knack–IRIS data, the earliest decade of growth that we can examine would be 1980–90, and even here we have to be careful to remember that the governance data that we have are for a year almost halfway through the growth period. The Knack–IRIS indices are more appropriate for testing the significance of governance for economic growth during 1990–2003. The World Bank data on governance begin in 1996, and therefore these can at best be used for examining growth during 1990–2003, keeping in mind once again that these indices are for a year halfway through the period of growth being considered.

Stephen Knack's IRIS team at the University of Maryland compile their indices using country risk assessments based on the responses of relevant constituencies and expert opinion (IRIS-3 2000). These provide measures of market-enhancing governance quality for a wide set of countries from the early 1980s onwards. This data set provides indices for a number of key variables that measure the performance of states in providing market-enhancing governance. The five indices in this data set are for (i) corruption in government; (ii) rule of law; (iii) bureaucratic quality; (iv) repudiation of government contracts; and (v) expropriation risk.

These indices provide a measure of the degree to which governance is capable of reducing the relevant transaction costs that are considered necessary for efficient markets. The IRIS data set then aggregates these indices into a single 'property rights index' that ranges from 0 (the poorest conditions for market efficiency) to 50 (the best conditions). This index therefore measures a range of market-enhancing governance conditions and is very useful, within the standard limitations of all subjective data sets, for testing the significance of market-enhancing governance conditions for economic development. Annual data are available from 1984 for most countries.

A second data set that has become very important for testing the role of market-enhancing governance comes from Kaufmann's team (Kaufmann et al., 2005) and is available for most countries from 1996 onwards on the World Bank's website (World Bank, 2005a). These data aggregate a large number of indices available in other data sources into six broad governance indicators. These are:

1. *Voice and Accountability*, measuring political, civil and human rights;
2. *Political Instability and Violence*, measuring the likelihood of violent threats to, or changes in, government, including terrorism;
3. *Government Effectiveness*, measuring the competence of the bureaucracy and the quality of public service delivery;
4. *Regulatory Burden*, measuring the incidence of market-unfriendly policies;
5. *Rule of Law*, measuring the quality of contract enforcement, the police and the courts, as well as the likelihood of crime and violence;
6. *Control of Corruption*, measuring the exercise of public power for private gain, including both petty and grand corruption and state capture.

We have divided the countries for which data are available into three groups. Advanced countries are high-income countries using the World Bank's classification with the exception of two small oil economies (Kuwait and the UAE), which we classify as developing countries. This is because although they have high levels of per capita income from oil sales, they have low capacities of producing their own wealth compared to other high-

Table 5.2 Market-enhancing governance: composite property rights index (Knack–IRIS data set) and economic growth 1980–90

	Advanced countries	*Diverging developing countries*	*Converging developing countries*
Number of countries	21	52	12
Median property rights index 1984	45.1	22.5	27.8
Observed range of property rights index	25.1 – 49.6	9.4 – 39.2	16.4 – 37.0
Median per capita GDP growth rate 1980–90	2.2	–1.0	3.5

Sources: IRIS-3 (2000), World Bank (2005b).

Note: the IRIS property rights index can range from a low of 0 for the worst governance conditions to a high of 50 for the best conditions.

income countries. From the perspective of understanding the relationship between governance and growth, the small number of developing countries that have enjoyed significant natural resource windfalls should really be classified as developing countries. We also divide the group of developing countries into a high- and low-growth group. We define 'diverging developing countries' as the ones whose per capita GDP growth rate is *lower* than the median growth rate of the advanced country group, and 'converging developing countries' are ones whose per capita GDP growth rate is *higher* than the median advanced country rate.

Table 5.2 summarizes the available data for the 1980s from the Knack–IRIS data set. For the decade of the 1980s, the earliest property rights index available in this data set for most countries is for 1984. Table 5.3 shows data from the same source for the 1990s. A very similar result is achieved using the six governance indices from the Kaufmann–World Bank data set (for a full set of data plots see Khan, 2006b). Figures 5.3 and 5.4 show the same data in graphical form. These tables and plots show some remarkable patterns and demonstrate that market-enhancing governance conditions cannot explain much of the differences in growth rates between developing countries. The main empirical features of the available data sets are as follows:

1. There is virtually no difference between the median property rights index between converging and diverging developing countries.
2. The range of governance observed in converging and diverging developing countries almost entirely overlaps.
3. The positive slope of the regression line in the pooled data is therefore misleading.
4. The market-enhancing governance indicators do not help to identify the critical governance differences between converging and diverging developing countries.

Table 5.3 Market-enhancing governance: composite property rights index (Knack–IRIS data set) and economic growth 1990–2003

	Advanced countries	*Diverging developing countries*	*Converging developing countries*
Number of countries	24	53	35
Median property rights index 1990	47.0	25.0	23.7
Observed range of property rights index	32.3 – 50.0	10 – 38.3	9.5 – 40.0
Median per capita GDP growth rate 1990–2003	2.1	0.4	3.0

Sources and note: see Table 5.2.

The absence of any clear separation between converging and diverging developing countries in terms of market-enhancing governance conditions casts doubt on the robustness of the econometric results referred to earlier that find market-enhancing governance conditions have had a significant effect on economic growth. It suggests that the positive relationship routinely identified in econometric studies depends on different types of specification problems. In many studies, the problem is that the sample includes a large number of *advanced countries* having high scores on market-enhancing governance (shown as diamonds in Figures 5.3 and 5.4) while the bulk of developing countries are low-growth and low-scoring on market-enhancing governance (triangles in Figures 5.3 and 5.4). However, if we only look at these countries, we are unable to say anything about the direction of causality as we have good theoretical reasons to expect market-enhancing governance to improve in countries with high per capita incomes. The critical countries for establishing the direction of causality are the converging developing countries (squares in Figures 5.3 and 5.4). By and large, these countries do not have significantly better market-enhancing governance scores than diverging developing countries. This is particularly striking when we use the Knack–IRIS data on aggregate property rights for the 1990s, which is the only period and data set for which we have a governance indicator *at the beginning* of a relatively long period of growth.

The policy implications of these observations are rather important. Given the large degree of overlap in the market-enhancing governance scores achieved by converging and diverging developing countries, we need to significantly qualify the claim made in much of the governance literature that an improvement in market-enhancing governance quality in diverging countries will lead to a significant improvement in their growth performance. These conclusions are often derived mechanically from the small positive slope of regression lines, without looking at the weak relationship or the distribution of developing countries in the way we have done.

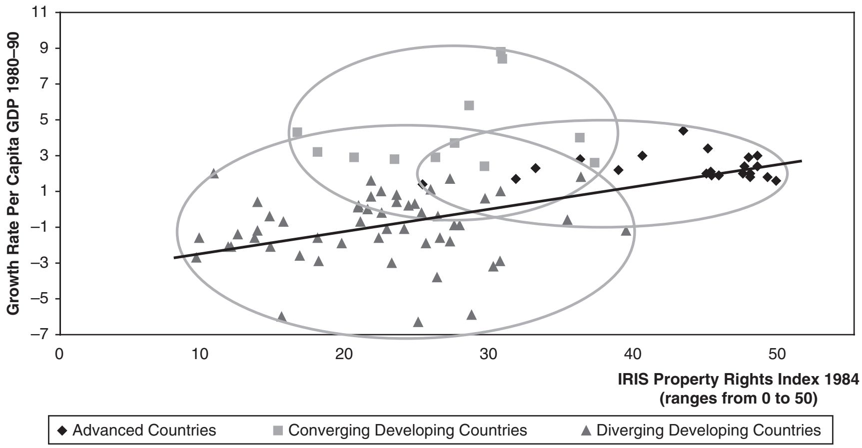

Figure 5.3 Aggregate property rights and growth, 1980–90

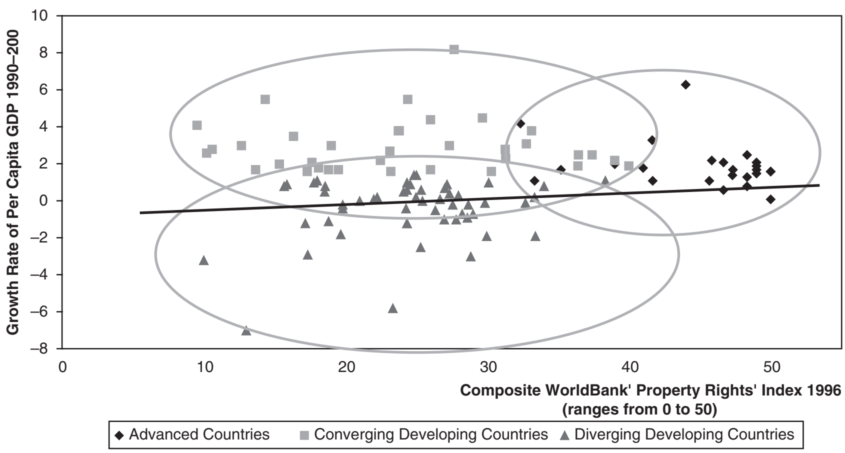

Figure 5.4 Aggregate property rights and growth, 1990–2003

Clearly, there are significant differences in growth rates between developing countries, and these suggest significant differences in the efficiency of resource allocation and use. Moreover, we agree with the general premise of institutional and governance policy that these differences are very likely to be related to significant differences in governance capabilities between converging and diverging developing countries. Based on Khan (2004), Figure 5.5 summarizes the data plots in Figures 5.3 and 5.4, and also shows what we may be missing by using the data in a particular way. The data suggest that differences in market-enhancing governance capabilities are

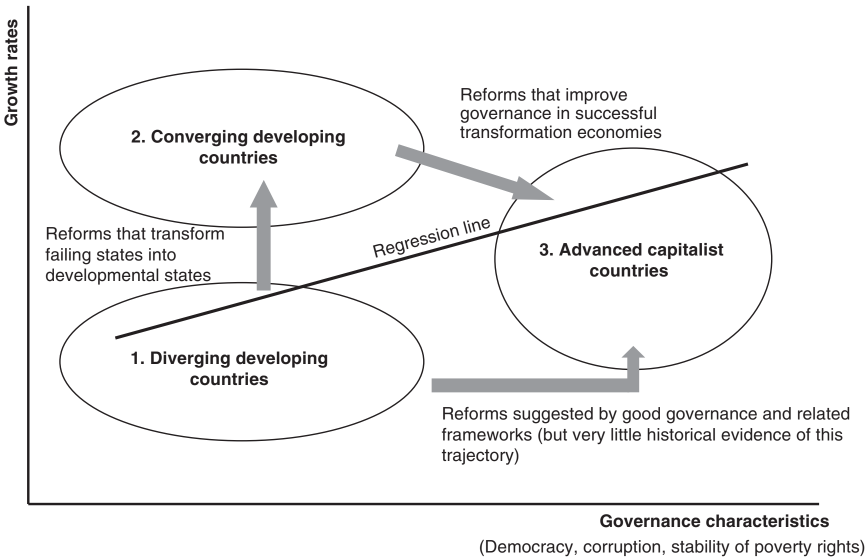

Figure 5.5 Stylized relationship between governance and growth
Source: Khan (2004).

not significant between converging and diverging countries, and that the relationships within the data may actually be telling us something about the importance of other dimensions of governance capabilities that could explain differences in growth performance.

The reform agenda identified by the good governance theories uses the data to argue that improvements in growth performance require a *prior improvement* in market-promoting governance. But this conclusion is based on a statistical result that is misleading as it pools countries and does not adequately adjust for initial conditions. The data are actually telling us that no developing country achieved advanced country governance characteristics as measured by market-promoting governance. But, in fact, converging and diverging developing countries do not differ in terms of these indicators. The interesting governance differences are more likely to be ones that have been discussed in the literature on catching up and developmental states, and we need to return to that literature to see if any significant governance differences have been identified that are consistent with the case study and other empirical evidence.

Our results are entirely consistent with Sachs et al. (2004) who show that when initial incomes are taken into account, (market-enhancing) governance quality does not explain any significant part of growth differences within Africa. A similar conclusion is reached by Glaeser et al. (2004) in a wide-ranging examination of market-enhancing governance indicators and economic performance. However, we do not conclude like Sachs and

Glaeser that governance is therefore a red herring. Our argument is that governance does matter, but we are looking at the wrong kinds of governance. There are indeed no significant market-enhancing governance differences between group 1 and group 2 countries in Figure 5.5, but there may be significant growth-enhancing governance differences that we should be looking for.

5 Growth-enhancing governance and economic growth

The good governance agenda ignores a number of critical structural challenges faced by developing countries going through the transformation from low productivity pre-capitalist societies to higher productivity capitalist ones. We review four structural features of developing countries that require very different governance capabilities if developing countries are to make successful and sustainable transformations into higher productivity economies.

The first governance capability is required to manage the structurally weak property rights that characterize developing countries. Theory and evidence suggests that contrary to good governance theory, the weakness of property rights in developing countries is structural and not due to the greed of political leaderships or their inadequate political will in enforcement. Countries differ widely in the capabilities of their governments to manage these weak property rights in ways that enable the emergence of a productive capitalism.

Second, emerging capitalists in developing countries face a structural problem with acquiring the tacit knowledge and learning that is essential for achieving international competitiveness. Achieving these capabilities requires complementary governance capabilities on the part of the state to manage incentives and opportunities for technological catching up, while creating compulsions for capitalists not to waste resources. Countries differ widely in these capabilities.

Third, developing countries suffer from structural political corruption due to the difficulty of managing political stabilization using fiscal processes. This explains the widespread role of political corruption and patron-client politics in developing countries. The common analysis of neo-patrimonialism in developing countries points to the need to move beyond patron-client politics. But this ignores the fact that modern political systems require significant fiscal resources if political competition is to focus on how to spend the budget, resources that are just not available in any developing country. As a result, even the most successful developing countries could not be characterized as Weberian states. Success in economic transformation has rather required governance capabilities in managing patron-client politics in ways that allow political stability sufficient for capitalist accumulation to continue. We now look at these issues in turn.

5.1 Weak property rights and the prevalence of non-market asset transfers

A critical structural problem in many developing countries is that property rights across the board are weakly protected because of the *limited public resources* available for defining and protecting property rights. In much of the conventional analysis of governance and corruption in developing countries, it is implicitly assumed that the protection of property rights can be dramatically improved through governance reforms and by reducing corruption. This analysis ignores the economic fact that constructing a nation-wide system of stable property rights is an extremely costly enterprise. Advanced countries only achieved significant stability in their property rights at a relatively late stage of their development when most assets had achieved high levels of productivity (Khan 2002, 2004, 2006a).

There is considerable controversy within institutional economics about whether stable and well-defined property rights are a precondition for growth. In an influential paper Acemoglu et al. (2001) argue that the achievement of stable property rights centuries ago enabled some countries to become prosperous while others who failed to achieve these conditions did not. This argument uses proxy indicators to measure the stability of property rights a century or more ago. Their now-famous indicator is the relative frequency of deaths of white settlers in different parts of Africa that determined whether or not Europeans set up settler colonies with stable property rights. Where malaria deaths were high, white settlers did not come but they set up extractive colonies where property rights were destabilized by colonial powers. This analysis is seductive in its use of innovative statistical techniques but suffers from serious historical problems. Most significantly, *the countries where settlers went did not enjoy stable property rights while the settlers were taking over these societies.* Indeed, they suffered from precipitous collapses of traditional property rights as large tracts of land were expropriated by the colonial settlers. In some cases the expropriation was so severe and rapid that indigenous populations collapsed entirely, sometimes in genocidal proportions. To describe this as the establishment of stable property rights does violence to the historical facts.

It is more accurate to say that where the transformation of property rights to capitalist ones happened very rapidly, capitalist economies emerged earlier than in other cases where the process of property right transformation is still going on. The rapid emergence of viable capitalist economies then allowed property rights to be protected and become stable in the way we would expect. In one sense, we could even argue that property rights were more stable in the non-settler countries because a precipitous historical rupture did not occur there. The problem for these countries is that similar property right transitions have to be organized today, but we hope with less violence and more justice. Of course once a viable capitalism becomes established, property rights become well protected. In settler colonies this happened quite a long time ago, but the stability of property rights across the board in these societies did not *predate* the establishment of a productive capitalism. In other words, Acemoglu et al.'s argument suffers from exactly the type of causality problem as the good governance arguments we discussed earlier, despite their use of more sophisticated econometrics and proxy variables.

The unlikelihood of establishing stable property rights in developing countries *before* the establishment of a productive capitalism is actually well supported by New Institutional Economics. However, most researchers subscribing to this school have argued that modern economies emerged as a *result* of stable property rights being established. But, in fact, one of the significant conclusions of the New Institutional Economics introduced by Douglass North and others was to point out that the protection and exchange of property rights is an extremely costly business. These costs are part of the transaction costs of a market economy, and New Institutional Economics pointed out that in advanced economies, transaction costs may account for as much as half of all economic activity (North and Wallis, 1987; North, 1990).

An efficient economy has slightly lower transaction costs than others, but not zero transaction costs or anything approaching that. In an efficient market economy transaction costs may be low for individual transactors at the point of exchange (this is the definition of an efficient market) but collective transaction costs for the economy as a whole are not low at all. These collective transaction costs can be paid because almost all assets in an advanced country are productive (by definition) and so owners can pay taxes and incur the private expenditures on legal and security systems that ensure that at the point of exchange, transaction costs are low. In a developing country, most assets are of low productivity and cannot pay the cost of their own protection. It is not surprising that *every* developing country suffers from contested and weak property rights.

Figure 5.6 shows the drivers of this governance failure in graphical form. When most of the assets in a country have not yet achieved high productivity uses (which is by definition the case in a developing or transition economy), it is difficult to imagine how the protection of property rights *across the board* can be paid for. Developing countries have to live with a much higher degree of property right instability compared to advanced countries, but this is not entirely or even largely due to the greed and discretion of their public officials. When property rights are not secure to any satisfactory extent, and transaction costs at the point of exchange are high, inevitably many transactions will be too expensive to conduct through the market. This would be the case even with honest officials and transparent political processes, but in fact officials and politicians are also likely to exploit opportunities provided by such a context. How they do this, and the capacities and incentives they have to govern this process determine the outcomes. Thus, while non-market transfers are ubiquitous and much more significant in developing

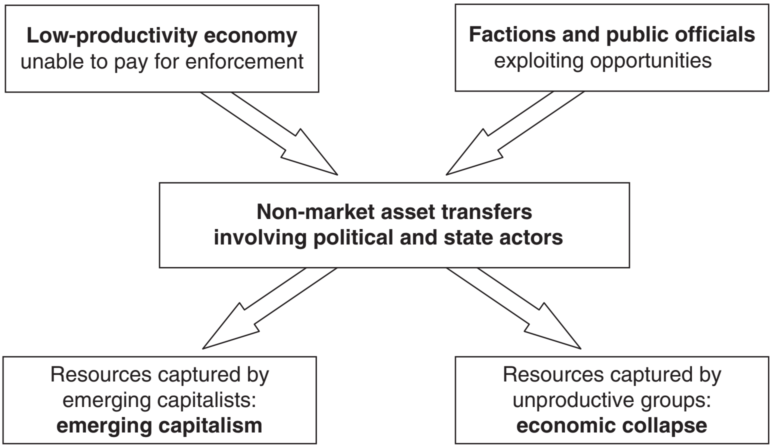

Figure 5.6 Drivers of property right instability in developing countries

compared to advanced countries, the outcomes of these processes can be radically different across countries, as Figure 5.6 summarizes.

Non-market transfers include not just high-profile cases of appropriation and theft using political power, but also cases of legal non-market transfers through land reform, state allocation of land for development and the use of the right of *eminent domain* in allocating public resources. The right of eminent domain is regularly used to transfer assets even in advanced countries when the transaction costs of market transaction would be too high. For instance, when a road is to be constructed, the transaction cost of purchasing many small plots of land and negotiating prices with individual owners would be too high. In these cases, the state uses its right of eminent domain to fix a price for the affected land through bureaucratic processes and then purchases the land using compulsory purchase orders. The only difference in developing countries is that the range of asset transfers where market transaction costs would be too high is even greater because of the many property rights that are contested or otherwise difficult to transact.

Non-market asset transfers of different types can thus be structurally necessary in developing countries but do open up the possibility of abuse and corruption. But they are not likely to be stopped by simply addressing the greed and discretion of public officials as there are deeper structural factors driving these processes. Rather, the critical issue for policy is that the outcomes of these non-market asset transfers can result in a successful transition to a modern capitalist economy or to predation and loss of resources to overseas tax havens. The governance capabilities that are relevant here are the institutional and political factors that ensure that non-market transfers enable investment in productive enterprises.

The case study evidence strongly supports our analysis. Not surprisingly, a significant part of the asset and resource re-allocations necessary for accelerating development in developing countries have taken place through semi-market or entirely non-market processes. These processes have been very diverse. Examples include the English Enclosures from the sixteenth to the eighteenth century; the creation of the *chaebol* in South Korea in the 1960s using transfers of public resources to these privileged groups; the creation of the Chinese TVEs (township and village enterprises) using public resources in the 1980s and their privatization in the 1990s; and the allocation and appropriation of public land and resources for development in Thailand.

Successful developers have displayed a range of institutional and political capacities that enabled semi-market and non-market asset and property right re-allocations that were growth enhancing. In contrast, in less successful developers, the absence of necessary governance capabilities meant that non-market transfers descended into predatory expropriation that impeded development. This analysis should not give us cause for complacency about the importance of governance. Rather it should direct our attention to a more critical set of governance reforms that are able to create stable expectations for critical sectors to enable accelerated investment and growth. In contrast, trying to implement reforms that attempt to achieve property right stability *across the board* in poor countries that lack the economic resources to make it feasible is likely only to result in frustration and eventually the abandonment of the reform programme.

The significant differences between successful countries suggests that there are no general institutional characteristics that all successful countries possessed but rather that they used different institutional mechanisms to achieve some common outcomes (Rodrik, 1999, 2002, 2003). We need to understand better why different institutional capabilities and incentives for non-market transfers have been effective in different contexts given differences in political organizations and structures.

5.2 Catching up, technology acquisition and governance capabilities

A significant reason why developing countries, even successful ones, persistently diverge from the efficient market model is that even reasonably efficient markets in developing countries face significant market failures when it comes to *organizing learning* to overcome low productivity in late developers (Khan, 2000b). Growth in developing countries requires catching up through the acquisition of new technologies and learning to use these new technologies rapidly. Markets, even the most efficient ones possible in a developing country, are typically inadequate on their own for attracting capital and new technologies in high value-added sectors. Efficient markets generally attract capital and technology to countries where these technologies are *already profitable* because the requisite skills of workers and managers already exist.

In theory, free markets should lead to rapid convergence if capital could flow to developing countries to use their cheap labour. But this theory only works if labour productivity in developing countries is not so low that it wipes out their wage advantage. Unfortunately, there are relatively few sectors in developing countries where this is true, and in some countries, there may be no sectors at all where capital would voluntarily wish to come. The problem is not only due to infrastructure and governance, but more fundamental. Developing countries have lower technological capabilities and therefore lower labour productivity in most sectors compared to advanced countries, and this low productivity wipes out their wage advantage even without taking into account problems of infrastructure and governance.

The real problem lies elsewhere, in a range of issues that economists have explained in terms of the time and effort it takes to *achieve labour discipline, tacit knowledge and learning-by-doing*. The knowledge about how to operate a modern factory at optimum or near-optimum efficiency has to be learned by both managers and workers by operating in the factory for a time, even if optimum efficiency cannot be immediately achieved. For instance, US productivity per worker in simple cotton spinning *using identical technology* was 7.8 times higher than Indian workers in 1978. And even in 1990 Indian textile workers were achieving 25 per cent of US productivity in 1959 (Clark and Wolcott, 2002). These massive differences can help to explain why there was so little inward investment in India during its period of virtually free trade with Britain during the colonial period. In addition, during the colonial period there were virtually no tariffs or restrictions on capital inflow or profit repatriation. Reproducing these colonial free trade conditions in developing countries today is likely to produce similar outcomes in the absence of growth-enhancing strategies to improve productive capacities in these countries.

The productivity gap is less marked in low technology and low value-added sectors compared to higher technology and higher value-added sectors. This explains why when capital does come, or investment is organized within the developing country, it is almost always in lower technology and lower value-added activities. Productivity *growth* in low productivity sectors is in general slower than in higher productivity sectors. Compare, for instance, the potential productivity growth in stitching garments compared to the potential productivity growth in making fabrics. This is not necessarily true for every sector that starts from a low technology base, but there are theoretical reasons why we would expect it to be true. Technologies that are already very high productivity by definition have a lot of embedded technology in them, and these are technologies where incremental technological progress is most likely. This explains why countries can get trapped into low technology sectors from which there is no automatic escape till the productivity gap to the higher level technologies can be jumped.

Overcoming the productivity gap is not just a question of setting up infant industries and letting them run, but also of setting up institutional compulsions that ensure that the effort involved in learning is forthcoming (Khan 2005a). This explains why catching-up strategies failed in almost every country except a few. The few that were different had institutions that could exert the requisite compulsions on learning sectors so that learning did happen and these countries moved rapidly up the technology ladder.

These observations can help to explain why even with complete trade openness and protection of expatriate property rights, colonies like India did not do too well in terms of industrialization or poverty reduction in the nineteenth and early twentieth centuries. Indeed, even in terms of property rights and general governance, India under colonial rule would score reasonably highly. Not only did India not catch up with Britain and other advanced countries during this century and a half, it fell precipitately behind. From 1873 to 1947 Indian per capita income declined from around 25 per cent of US per capita income to under 10 per cent. This experience has been almost entirely forgotten with the resurgence of confidence in liberalization and market openness as strategies that will ensure moving up the technology ladder and reducing poverty in poor countries.

The empirical evidence that is available from relatively successful developing countries suggests that the opportunities and compulsions for learning can be created by very different types of institutions and policies. Opportunities were created using many different mechanisms including tariff protection (in virtually every case but to varying extents), direct subsidies (in particular in South Korea), subsidized and prioritized infrastructure for priority sectors (in China and Malaysia) and subsidizing the licensing of advanced foreign technologies (in Taiwan). With the advent of a new consensus on international trade through the WTO, tariff protection is no longer an option for most developing countries, but historical experience tells us that this is not the only way, or even the most effective way in which to organize support for the learning processes through which productivity is raised in catch-up sectors. The common feature of successful learning strategies was the ability to create compulsions for successful learning because states had the institutional and political capacity to ensure that non-performance was not tolerated for too long (Amsden, 1989; Khan, 2000a).

The mechanisms through which this was achieved were very different in different countries, but the common feature of success was that failure led to corrective action that was effective. For instance, in South Korea, not only could subsidies be withdrawn, but failing enterprises were rapidly transferred to new ownership. In Malaysia, managements of public enterprises could be changed rapidly (compared to other developing countries) and private investors faced declining benefits over time. These compulsions were in turn credible because investors knew they could not protect themselves by buying factional political support. The mechanisms that ensured compulsions for learning in successful countries are, however, not well enough understood or studied and there is a need for careful research in these areas.

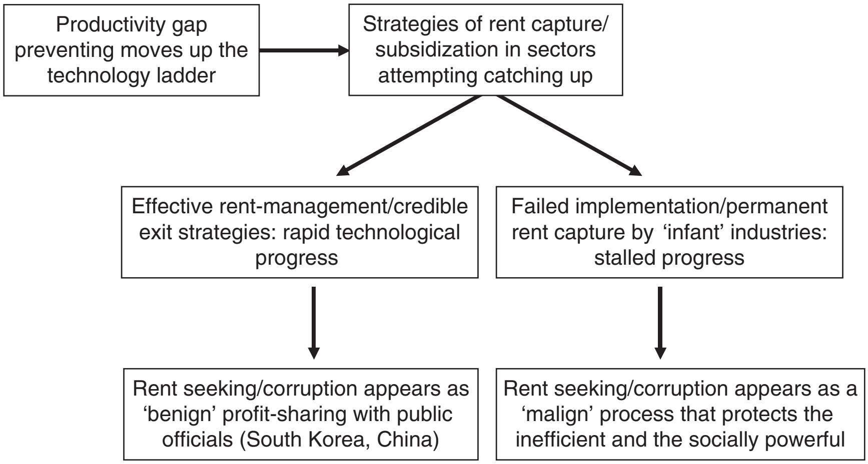

Figure 5.7 Governance capabilities and catching up through technical progress

Figure 5.7 shows that in the context of productivity differentials that cannot be overcome without non-market facilitation, there are strong incentives for emerging entrepreneurs to create these possibilities for themselves through the exercise of political power through the state. As soon as this happens, rent seeking and corruption are likely to emerge. The real difference in governance with respect to the management of learning processes (between successful and less successful countries) has *not* been the presence of rent seeking and corruption in some cases and its absence in others (both the left and right hand forks in Figure 5.7 are associated with rent seeking and possibly corruption). The real difference is rather that only a few countries had governance capabilities that created opportunities and compulsions for technological progress. The identification of these capabilities is critical to see how they can be replicated in different political and institutional contexts.

If the requisite governance capacities for effective rent management are missing, a growth-enhancing strategy that implicitly creates rents to accelerate learning may deliver worse outcomes than a market-led strategy. Badly managed rents can mean permanently poor resource allocation as well as high rent-seeking costs. But even a failed growth strategy can sometimes have unintended consequences that are potentially useful if it develops human capital even though it fails to profitably employ these resources. These can often be exploited in new ways if the growth strategy fails. The interactive relationship between growth strategies, governance capabilities and technological capabilities of producers can help to explain:

- why many *different* strategies of industrial catching-up were successful in East Asia;

- why at the same time apparently *similar* growth-enhancing strategies have worked in some countries and failed dismally in others;
- why some countries like India have done reasonably *well* with liberalization by using some of the capacities developed by previous growth strategies in new ways;
- why other countries in Africa, the Middle East and Latin America have fared rather *less well* in terms of growth after liberalization when they allowed markets to significantly guide resource allocation to areas of current comparative advantage. In Latin America liberalization has in many cases resulted in a shift towards less productive technologies in manufacturing or towards commodity production.

The success of liberalization in a number of countries, including India and Chile in the 1980s, can also be explained rather better from this perspective. Growth in these newly liberalizing countries occurred in three types of sectors. First, there was growth in a small number of sectors that had already acquired international competitiveness like parts of India's machine tools or pharmaceutical sectors. These sectors had been beneficiaries of previous technology acquisition strategies, and benefited from the physical and human capital accumulation that had taken place earlier. Second, there was growth in low value-added sectors that benefited from the capital accumulation and entrepreneurial skills that had been accumulated in the previous period. Examples of these sectors include ready-made garments and grey cloths. They also include relatively low value-added sectors like call centres that benefited from human capital that had been created for high value uses (call centres in India are often manned by university graduates). And finally, liberalization allowed some countries to grow by exporting commodities or natural resources. Success in these sectors was dramatic in some cases because they benefited from the growth in demand for commodities in the US and China.

The liberalization in the Indian subcontinental countries has to be distinguished from China, which emerged as the fastest growing economy in recorded history in a context of gradual and measured liberalization. To a far greater extent than other countries, including India, China combined growth-enhancing strategies with market-promoting strategies to move into mid-technology manufacturing. Many aspects of the successful growth-enhancing strategies of the past continue to be effectively implemented and appropriate growth-enhancing governance capabilities exist to implement them effectively. These strategies include the strategies of local and central government in China to make land and infrastructure available on a priority basis to investors in critical sectors, and to offer fiscal incentives and attractive terms to both foreign and overseas Chinese investors engaging in investments critical for economic progress (Qian and Weingast, 1997).

These 'subsidized' inputs allow Chinese firms to set up in global production before they have necessarily achieved global competitiveness as determined by the market. Indeed, Indian manufactures complain bitterly at the way in which Chinese manufacturing can enter markets at below the 'true' cost of production to establish economies of scale and learning advantages. Thus, while compared to the earlier generation of East Asian developers, the Chinese state appears to be doing less in terms of actively supporting technology upgrading, it still has very strong institutional capacities to ensure the allocation of land, resources and infrastructure to critical investors and to ensure that unproductive firms are not able to retain support. With its vast internal market and the broad-based technological capabilities it has already achieved, Chinese manufacturing has been able to acquire scale economies that enable it to compete in price almost without challenge in the low- to mid-technology manufacturing industries.

In contrast, the countries of the Indian subcontinent have had a different experience with liberalization. Here, previous growth-enhancing strategies had succeeded in creating technological capabilities that were less broad-based than in China. Political fragmentation was much greater and the governance capabilities of states to direct resources to investors were significantly lower than in China. As in China, liberalization in the textbook sense has proceeded at a very slow pace. Growth has been led by sectors that had already achieved the minimum technological capability for international competition taking the opportunity to start producing aggressively for domestic and international markets. The results were higher growth rates than in the past, led by a small number of sectors that had acquired enough technological capability to enjoy comparative advantage in international markets. These sectors differed across South Asia, ranging from the garment industry and shrimps in Bangladesh, low-end textiles in Pakistan to diamond polishing, call centres and software in India. India's global presence has been exaggerated by the outward investments of a small number of Indian multinational companies, which were more interested in purchasing high technology companies abroad than developing these capacities within India. But on the whole, South Asia has relatively weak growth-enhancing strategies and capabilities on the part of government, with the result that ongoing technology acquisition is much more narrowly focused, and driven by firms that are already quite advanced engaging in partnerships with foreign firms. This process has resulted in limited learning in new sectors in India compared to China, and even less in Pakistan and Bangladesh.

Our analysis suggests that while it is desirable over time to improve market-enhancing governance, the comparison of liberalization in China and India suggests that market-enhancing governance cannot explain their relative performance. Case studies of China and India do not suggest that China performed much better than India (if at all) along critical dimensions of market-enhancing governance such as the stability of property rights, corruption or the rule of law *before* it began its takeoff. Where it does do better is in having governance capacities for accelerating resource allocation to growth sectors, prioritizing infrastructure for these sectors, and in making credible and attractive terms available to investors bringing in advanced technologies, capabilities that we have described as growth-enhancing governance capabilities.

Latin America provides even more compelling evidence that a focus on market-enhancing governance alone cannot provide adequate policy levers for governments interested in accelerating growth and development. Compared to China and the Indian subcontinent, liberalization in Latin America has been more thoroughgoing and has extended in many cases to the liberalization of the capital account and much freer entry conditions for imports into the domestic market. In terms of market-enhancing governance, Latin America on average scores highly compared to other areas of the developing world. This is not surprising given higher per capita incomes, a much longer history of development and relatively old institutions of political democracy (even though in many cases these institutions were for a while subverted by military governments).

Yet its more developed market-enhancing governance capabilities and deeper liberalization did not help Latin America beat Asia in terms of economic development in the 1990s and beyond. In fact, relative performance was exactly the opposite of what we would expect from the relative depth of its liberalization strategy and its relative governance indicators. This should not be entirely surprising given our analysis. Latin American countries shifted even more rapidly to producing according to their comparative advantage, and in most Latin American countries this meant a shift to lower technology industries and to commodity production. This has produced respectable output growth in some countries, but productivity growth has been low.

Table 5.4 summarizes several historical observations to highlight some of the key characteristics of successful and less successful technology acquisition strategies. The technology acquisition strategies of the 1960s and 1970s produced dramatic success but only in countries that by good fortune happened to have the institutional and political conditions that allowed them to create both opportunities and compulsions for rapid learning. In other developing countries, similar strategies allowed high levels of accumulation and more rapid growth than under imperial rule when free markets dominated. But they did not achieve the productivity growth that would have allowed their emerging industries to become truly viable for facing international competition. The eventual fiscal crisis that some of the less successful countries faced as a result of the failure to discipline non-performing industries led to strategies of liberalization being adopted in many of these countries. And finally, liberalization in some countries that had achieved some success with technology acquisition allowed growth spurts to begin in the 1980s in the Indian subcontinent and parts of Latin America.

This complex picture suggests that in Figure 5.5, the group of converging countries shown as group 2 includes countries of several different types and not all of them may be enjoying sustainable growth. Some are countries

Table 5.4 Technology acquisition strategies and experiences

	Critical components of technology acquisition strategy	*Supportive or obstructive governance capabilities*	*Economic outcomes*
South Korea, 1960s to early 1980s	Non-market asset associations to growth drivers (consolidations, mergers and restructuring of *chaebol*).	Centralized governance by agencies with long-term stake in development.	Very rapid growth and capitalist transformation.
	Targeted conditional subsidies for *chaebol* to accelerate catching up.	Effective implementation assisted by weakness of political factions so that inefficient subsidy recipients are unable to buy protection from them.	
Malaysia, 1980s to 1990s	Public sector technology acquisition by public enterprises with diffusion to private sector firms through subcontracting.	Moderately effective centralized governance.	Rapid growth and capitalist transformation.
	Targeted infrastructure and other incentives for MNCs with conditions for technology transfer.	Assisted by centralized transfers to intermediate classes which reduced incentives of political factions to seek rents by protecting inefficient firms.	
Indian subcontinent, 1960s to 1970s (with some variations these characteristics describe many developing countries of that period)	Target subsidies to accelerate catching up in critical sectors (using protection, licensing of foreign exchange, price controls and other mechanisms).	Moderate to weak governance capacities to discipline non-performing rent recipients. Agencies often have contradictory goals defined by different constituencies.	Public and private sector infant industries often fail to grow up.

	Public sector technology acquisition in subsidized public enterprises.	Fragmented political factions help to protect the rents of the inefficient for share of these rents.	Rent-seeking costs are often the most visible effects of intervention.
	Resource transfers to growth sectors using licensing and pricing policy.	State capacities decline as committed public officials leave.	Moderate to low growth and slow transformation.
Indian subcontinent, 1980s to 1990s	Liberalization primarily in the form of a withdrawal of implicit targeted subsidies, in particular through the relaxation of licensing for capital goods imports.	Moderate to weak governance capabilities to implement remain but do less damage as the scope of growth-enhancing policies declines.	Growth led by investments in sectors that already have comparative advantage.
	Much more gradual withdrawal of protection across the board for domestic markets.	Fragmented political factions continue to have an effect on market-enhancing governance by restricting tax revenues and making it difficult to construct adequate infrastructure.	Higher growth but limited to a few sectors.
Latin America, 1950s to 1970s	Domestic capacity building through selective tariffs and selective credit allocation.	Governance effective in directing resources to import-substituting industries but weak in disciplining poor performers. Weakness linked to 'corporatist' alliances that constrained disciplining powerful sectors.	Initial rapid growth slows down. Many infant industries fail to grow up.
Latin America, 1980s onwards	Rapid liberalization across the board.	Breakdown of corporatist alliances allows liberalization to be implemented (to varying extents in different countries).	Output growth in sectors that already have comparative advantage, in particular in commodities.

that have sustainable technology acquisition strategies and are therefore on sustainable growth paths based on continuous productivity growth and the maintenance of competitiveness and improvements in living standards. But group 2 countries could also include countries attempting technology acquisition without adequate governance capabilities to make this truly sustainable. For instance, Pakistan in the early 1960s was a converging country, but its growth spurt was unsustainable because its growth-enhancing governance capabilities were not adequate for ensuring the successful implementation of its technology acquisition strategy. And today, group 2 countries include several that have abandoned technology acquisition strategies in the formal sense, but which are growing rapidly because they have already acquired physical and human capital in some niche sectors that give them international competitiveness. The long-term sustainability of these strategies is also open to question.

By integrating into global markets and production chains using already competitive sectors, some liberalizing countries have achieved significant growth rates and joined the converging group in the 1980s and 1990s. The question is whether countries like Bangladesh or Uganda that have enjoyed convergence growth rates in the 1990s have discovered a new growth strategy that dispenses with a technology acquisition strategy, or are these spurts going to prove short-lived, as much of the historical evidence on purely market-driven growth would suggest. If we assume that some countries in group 2 are on sustainable convergence paths while others are not, we need to identify the governance conditions that differentiate them. Clearly good governance does not help us very much in this respect, because as we have already discussed, the countries in group 2 have the same mean and dispersion as group 1. Our hunch is that the sustainable sub-group within group 2 are the countries that have a sustainable technology acquisition strategy based on effective governance capabilities to effectively implement the strategy they are following. This is a critical research and policy question that needs to be examined further.

Of course, it would be simplistic to suggest that within group 2 there are countries that do have the governance capabilities to follow a technology acquisition strategy, and others who have *no* capability to implement technology acquisition strategies. Even countries that are following largely market-driven growth strategies have elements of formal or informal strategies to promote technology acquisition and discipline these processes. This is particularly the case in countries like India where government–business relationships are quite well developed in pockets. But there are elements of informal government–business relationships in countries like Bangladesh that also assist some sectors to acquire technology by gaining temporary advantages that allow them to start producing before achieving international competitiveness. It is also important for policy to identify these processes and examine how policy can assist in deepening these trends.

5.3 Governance and the management of political stability

One of the main reasons why developing countries as a group diverge so significantly from good governance conditions is that their political systems do not operate with formal and transparent rules for public officials that ensure their accountability to elected bodies. There is a large and growing gap between the reality of developing country politics and the policy prescriptions coming from good governance theory. Once again, the question is why this is so systematic.

A powerful set of analyses of the political economy problems of developing countries comes from the neo-patrimonial school that sets up a contrast between typical developing country political structures with the Weberian ideal of a rational and formal state based on impersonal political relationships (Eisenstadt, 1973; Médard, 2002). The core argument of this emerging analysis was that the absence of democracy and accountability in developing countries allowed political bosses to use personalized power to run patron-client networks with their clients. This explained the persistence of patron-client politics, the importance of informal rather than formal rules and widespread corruption. The result of these processes was the politically driven accumulation that produced economic and political underdevelopment in developing countries. The main links in this argument are shown in Figure 5.8. The early theory has been added to by subsequent analysis that has focused on the contribution of ethno-linguistic fractionalization and economic inequalities in perpetuating personalized politics and its damaging effects (Engerman and Sokoloff, 2002; Blair, 2005; Barbone et al., 2006).

The policy conclusion of these approaches is that democratization and other strategies to weaken personalized politics will weaken the hold of patron-client politics and move these economies towards modern polities. However, there is a growing recognition that in the presence of severe ethno-linguistic fractionalization, democratization may not work in weakening patron-client politics, and may even strengthen these tendencies (Barbone et al., 2006). Moreover, as Barbone et al. point out, sometimes patron-client politics appears to operate even in the absence of fractionalization (as in Tunisia or Bangladesh). However, the expectation is that patron-client politics is *avoidable* in developing countries, that there are specific institutional failures that enable its continuation, and that the *desirable and achievable* state of affairs is a democracy that is accountable, with political institutions that work on principles of impersonal politics (AFD et al., 2005). Such a political system is an integral part of the good governance framework described in Figure 5.2.

The problem is that no examples exist of such a state of politics in the developing world. Even in India, the world's most attractive model of a working and sustainable democracy in a developing country, we know that the Indian political system is riven with corruption, that patron-client politics

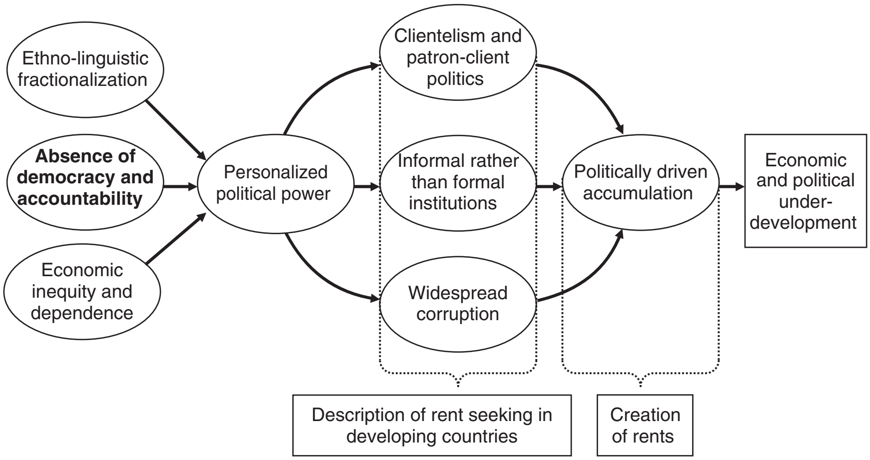

Figure 5.8 The neo-patrimonial analysis of the causes and effects of patron-client politics

rules, and that economic reform, when it happens, takes place because reformers can work the patron-client system, not because they have overcome its limitations by progressing towards a modern Weberian political system (Jenkins, 2000; Harriss-White, 2003; Khan, 2005b).

An alternative explanation for the persistence of patron-client politics is developed in Khan (2005b). The alternative argument is that there are significant structural factors that make patron-client politics a rational response to the problem of maintaining political stability in a developing country. The main drivers of this type of politics are shown in Figure 5.9. The critical constraint is that all developing countries suffer from limited fiscal resources (even apart from the political failures to collect tax) because by definition the development of their formal taxable sectors is limited. At the same time, managing political stability is even more demanding than in an advanced country because of the deep social dislocations caused by the economic and social transformations of development. The option of managing social stability through transparent and legal transfers through the fiscal system simply does not add up. This does not mean that tax collection cannot be increased and that this would not help the situation. But in most developing countries, feasible increases in tax collection would not solve the fundamental problem that the tax take would still be insufficient to pay for all necessary services and still be able to pay for the necessary political stabilization of society through transparent fiscal transfers.

The recourse to patron-client politics as a universal response in all developing countries regardless of culture, politics or economic strategies can be better explained by this fundamental structural driver. Patron-client politics makes sense because it allows the governing group to identify the

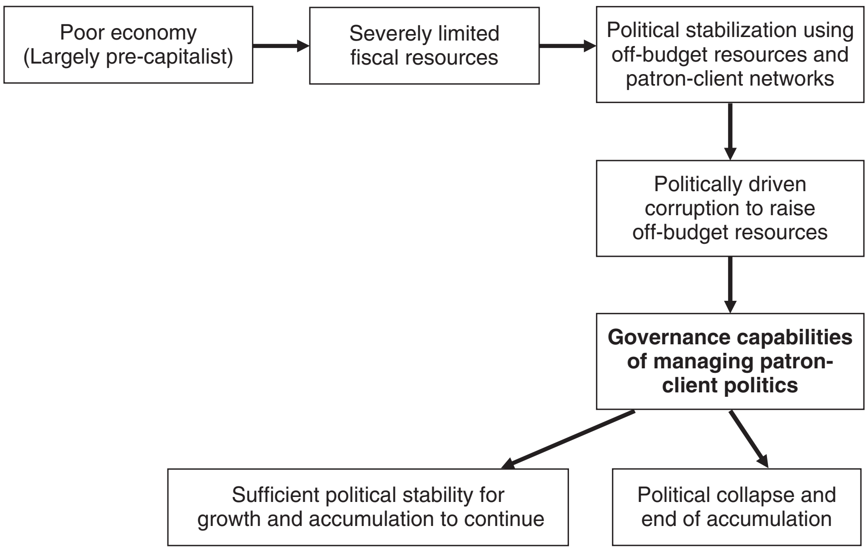

Figure 5.9 Structural drivers of patron-client politics

most critical, the best organized, the most troublesome or simply the most dangerous constituencies and buy them off selectively. By definition, such a selective strategy of buying off specific constituencies cannot be done in a transparent way, and in any case the fiscal resources for satisfying even limited constituencies often do not exist in the budget. The most important politics in developing countries therefore often takes place off-budget, with off-budget resources being raised for redistribution down patron-client networks.

Sustainable growth paths in developing countries have not been associated with Weberian states behaving in impersonal and formal ways because all developing countries suffer from patron-client politics. Rather, sustainable high-growth strategies have been associated with governance capabilities that allowed the maintenance of political stability *through* patron-client politics (as in contemporary India), while in other countries, political stability could not be maintained and a descent into political fragmentation took place. The governance challenge is to understand how in specific contexts, the management of political stability is being achieved using the historical endowments of institutions and power structures, and whether feasible changes in political institutions and political organizations can assist in strengthening political stabilization. Here too, the priorities of market-enhancing governance may be misplaced. What we need is a much better understanding of the types of patron-client networks through which political stabilization and political accumulation take place in different countries, so that governance interventions can be designed to improve sustainable growth and development outcomes.

As with the other processes that we have discussed, success in managing political stabilization has depended on the *compatibility* of institutional structures with pre-existing political structures of political organization and patron-client structures that are part of the political settlement. For instance, in the 1960s attempts at authoritarian limitation of patron-client demands worked in South Korea but failed in Pakistan because the organization of patron-client networks in Pakistan was much stronger and more fragmented, requiring a degree of repression that was ultimately not feasible. In turn, the feasible strategy of political stabilization that was consistent with the political settlement in Pakistan limited the possibility of success of the technology acquisition strategies that Pakistan was attempting at the time (Khan, 1999). It is often forgotten that the South Korean technology acquisition strategy of providing conditional rents to learning industries in fact emerged first in Pakistan in the 1960s. Ironically, it proved impossible to implement effectively in Pakistan because the fragmented clientelism in that country allowed individual capitalists to buy themselves protection at a relatively low price. The absence of fragmented clientelism in South Korea allowed the effective implementation of the same strategy that had failed in Pakistan. Malaysia too initially suffered from fragmented clientelism, but was able in the early 1980s to overcome this constraint through a change in the dominant political organizations. This change in the political settlement enabled a more centralized version of clientelism to emerge. Malaysia's centralized clientelism of the 1980s, although it was still a costly system to run, allowed the implementation of a different type of learning strategy based on multinational companies with conditions and incentives for technology transfers and learning. These interdependencies between political stabilization strategies, learning strategies and asset transfer strategies are critical for devising feasible improvements in growth-enhancing governance capabilities. Widening our knowledge of these interdependences will allow us to deepen our analytical and policy understanding of these processes.

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6 Governance for growth

Improving international development through Anglo-Japanese cooperation

*Max Everest-Phillips**

1 Introduction: improving the governance behind economic growth

Nothing is more important for implementing the ambitions of international development than the uncertain impact of governance on economic growth—a heady mix of obdurate politics, confused economic theory and complex, often contradictory historical evidence. We still know too little about what dimensions of the governance agenda really influence the dynamics of sustainable economic growth.

Over the last few years, past certainties for achieving international development have disappeared: The World Bank's seminal study 'Economic Growth in the 1990s: Learning Lessons from a Decade of Reform' (2005b) stressed that there is no one path to growth, no one set of effective institutions, but that 'politics trumps economics'—good economic principles can only be implemented when in accord with both the local political climate and administrative capacity. Without engagement with the detail of a country's governance, growth strategies are futile. Many in development feel unnerved. What are the guiding principles between universal principles—the investment climate[1] and good governance—and the local 'varieties of capitalism'?

To address this development challenge, the UK and Japan are well placed to provide the international community with leadership through increased collaboration. Japan (and later East Asia) and the West had different paths to development, creating a different understanding about what dimensions of governance really matter for economic growth. With the bursting of the Japanese 'bubble' economy 15 years ago, UK interest in Japanese insights on world development has faded. At this important juncture for DFID (with the UK 2006 White Paper on international development highlighting the importance of governance, and a renewed understanding that economic growth is crucial to poverty reduction) closer development cooperation between Japan and the UK would strengthen understanding of divergent paths to sustainable development.

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Fortunately in recent years the international development community has rediscovered that countries need economic growth if they are ever to escape aid dependency. We are now much clearer that local context—history, political processes, institutions, social attitudes—is crucial for achieving sustainable economic growth. Increasingly we agree that there is no 'international best practice' to be parachuted in by development experts and expensive consultants from Washington or other Western capitals; good principles like 'accountability' or 'transparency' can only emerge gradually from 'what really works' in local circumstances.

The case for promoting 'governance for growth' through Anglo-Japanese collaboration builds on three opportunities that present themselves: the G8, the fourth Tokyo International Conference on African Development, and Japan's reformed development agency. Second, 'governance for growth' plays to combined strengths—DFID has been highly influential in shaping the debate on governance in the international development community; while Japan has maintained its high reputation for practical expertise on growth. Third, much of the international analysis of the governance determinants of economic growth is too dominated by Anglo-American economic perceptions of how development happens, based on a narrow focus on 'institutions' as 'technical fix' rather than an evolving process of political governance. This is a poor reflection of the complexities of history beyond the US and UK experience—in particular, despite the voluminous literature on the 'East Asian Miracle', a limited appreciation of the political governance characteristics of Japan and subsequent 'later developers' that were the critical dimension to their sustained high economic growth.

Development policy prescriptions, such as free markets or 'rule of law', while claimed to be universal, are all too often devoid of history. Practitioners usually lack a sense of the different paths to economic growth from the variety of states and markets. Orthodox dogma on the causes of economic growth (the 'Washington Consensus' of the 1980s and 1990s) has given way, in the face of practical failure around the developing world, to a search for political feasibility in local contexts—what really works. Economic growth requires more than just 'the maintenance of macroeconomic and political stability'. No successful high-growth country from China to Botswana has ever followed any policy prescription on 'good' governance, growth or the investment climate: but understanding how basic principles of economics need to engage with local politics and history remains a challenge of mindsets, professional expertise and knowledge. 'An effective state is the single most important factor determining whether development takes place' (DFID, 2007, p.1). The most important development of recent years has been the recognition that 'good governance is about good politics' (DFID, 2006, p.23). Political governance is also central to economic growth: 'modest changes in institutional arrangements and in official attitudes to the economy can produce huge growth payoffs' (Rodrik, 2003, p.16). There is an increasing acceptance by the international development community that 'just getting markets and the investment climate right' is not enough: governments need to take more proactive steps to support and sustain growth (Hausmann et al., 2005).

The governance dynamics of economic development need to be reflected better into developing countries' growth strategies. The international community must get better at finding ways to support effective political governance underpinnings that generate long-term growth. Reforms require careful priorities and sequencing. Changing power relations and the way that decisions are made in a society may take decades, but when opportunities do occur, change can happen with surprising speed. History suggests cautious optimism is justified, but progress requires international collaboration built on practical experience and expertise which JICA and DFID, and the international development communities in both countries, are well placed to promote. This chapter is a manifesto for collaborative action playing to the comparative strengths of two major developed countries at a key time for 'governance for growth' as the crucial underpinning for all hopes of delivering the MDGs.[2]

2 Governance for growth

Faced by the turgid jargon of contemporary political science, economics and political economy, the concise and elegant insight of great thinkers of the past is often the most inspiring. The renewed interest in 'governance for growth' reflects the advice Machiavelli gave Renaissance monarchs that that they would be stronger in a prosperous realm than in an impoverished and discontented one:

> [The Prince] ought accordingly to encourage his subjects by enabling them to pursue their callings, whether mercantile, agricultural, or any other, in security, so that this man shall not be deterred from beautifying his possessions from the apprehension that they may be taken from him, or that another refrain from opening a trade through fear of taxes; and he should provide rewards for those who desire so to employ themselves, and for all who are disposed in any way to add to the greatness of his City or State.
>
> (*The Prince*: 1992 edition, p.61)

Economists have in recent decades rediscovered the truth best expounded by the great English seventeenth-century political philosopher Thomas Hobbes that without the effective institutions of the state,

> there is no place for industry, because the fruit thereof is uncertain: and consequently no culture of the earth; no navigation, nor use of the commodities that may be imported by sea; no commodious building; no instruments of moving and removing such things as require much force;

> no knowledge of the face of the earth; no account of time; no arts; no letters; no society; and which is worst of all, continual fear, and danger of violent death; and the life of man, solitary, poor, nasty, brutish, and short.
>
> (Hobbes, 1651, Chapter 13)

But progress in explaining why, how and when effective states and markets emerge, and what the international community can do to promote this outcome, has been frustratingly slow.

Economic growth is essential to delivering the MDGs. Yet the proportion of British aid to Africa devoted to 'directly productive' activities (growth and rural livelihoods), expressed as a percentage of aid for 'social' spending (education, health, social and governance), had fallen from 371 per cent in 1988/9–1989/90 and 208 per cent in 1993/4–1994/5, to only 45 per cent by 2003/4 (Killick, 2005). OECD–DAC data on sector-specific aid from all donor sources shows the ratio of assistance to 'social', as against 'economic', sectors changed in a continuous—and continuing—trend from 1:4 in 1978 to 4:1 in 2004 (Killick and Foster, 2006). Optimists may point to 'convergence'—poor countries will catch up with the rich (notably China and Vietnam at present; East Asia and Botswana in earlier decades); pessimists highlight non-convergence—the rich countries carry on getting richer (per capita income in many African countries is roughly where it was at independence 40 years ago: Pritchett, 2006). But in either case, economic growth really does matter for poverty reduction. And while few now doubt that governance is critical, what aspects of governance really matter to deliver the economic growth needed for sustained poverty reduction is still far from clear.

Governance is defined in various ways by different international development agencies. The basic concept seeks to capture the *process* of governing, distinct from the government as the individuals holding state authority at any particular moment. Governance contains two different elements—the aspects of governing the state that are of *intrinsic* importance to the population, such as respect for human rights; and the *instrumental* dimensions of governance—the attributes of the quality of governance that delivers on the needs of the population. Governance affects all aspects of growth dynamics in different ways, via such diverse areas as investment, finance, education, health and innovation. Property rights, contract enforcement and markets—in labour, property and capital—are socially constructed and politically regulated (Harriss-White, 2005). Governance can impact through many channels: political systems and processes; national legal systems; state bureaucratic policy process and its implementation: policy, policy action and policy outcomes often differ significantly from the plan, depending on capabilities (Pritchett, 2004).

Yet what aspects of political systems and government capabilities are necessary to deliver growth in different developing country contexts remains far from clear. Successful high growth in East Asia was due to the existence of strong states with a clear growth agenda. While few would doubt that governance and economics are closely connected, what is being measured as 'governance' may not capture the relationship: not only that high-growth and low-growth developing countries have had the same governance quality over the last two decades according to standard indicators of governance, but that the average high-growth developing country actually had slightly worse governance in the 1990s than the average low-growth country (Khan 2006). This suggests greater effort is needed to identify better the dimensions of governance that actually deliver growth.

Governments that are concerned for the long-term good of their general population and responsive to their needs are likely to be supportive of economic growth that will deliver better livelihoods for all; the intrinsic and the instrumental dimensions to governance are intertwined: respect for civil liberties and human rights is correlated with growth outcomes (Rodrik, 1998; Stiglitz 2002). Government determined to deliver economic growth must maintain political stability and show long-term commitment. The wide variety of historical trajectories towards 'best practice' in developed economies shows there is no one path to sustainable growth (Hall and Soskice, 2001).

> Once one moves beyond general statements of the kind that property rights are good for growth and corruption is bad, there is much that remains unclear. Which institutions demand priority? What are the specific institutional forms that are required? Do these differ across countries according to the level of development, historical trajectory, and initial conditions?
>
> (Rodrik, 2003, p.8)

'Government failure' and 'market failure' remain contested concepts: whether and how much the state should interfere in markets, and how far private sector can or should deliver functions of government. Some countries have made rapid transitions to growth without profound governance reforms, while governance reforms supposedly crucial for growth have had no effect on economic performance of African countries (Sachs et al. 2004). China has significantly higher growth rates than India but does not perform better along the supposedly critical dimensions of 'Investment Climate' governance such as property rights or the rule of law.[3] So causality is unclear between governance, investment and growth: for example, India and Brazil with similar rates of investment (21 per cent of GDP) grew at rates as different as 5.7 per cent and 2.1 per cent between 1980 and 2004. Substantial intra-national growth differences exist that cannot be explained by broad generalisations about institutional factors: there are significant examples of rapid growth and investment in some sectors within countries that are otherwise regarded as having poor growth and investment climates (Haber et al. 2004). Growth differs widely by locality within countries, with local governance factors often explaining the marked regional variations in growth performance—for example, across the Indian states of Gujarat, West Bengal and Tamil Nadu that were at a comparable level of development at the time of Independence;[4] and across China (World Bank, 2006).

How much then does governance 'matter' for growth? Political power influences what growth strategies are realistic, and the governance capabilities needed to implement them. Growth can be politically desirable to achieve political stability, or can be politically threatening if socially divisive, so governments must also be concerned about the social impacts of growth—economic transformation inevitably causes some social upheaval including localised unemployment from 'churning' as companies enter and exit the market place with improvements in competitiveness and productivity. Governments always require the capacity to buy off resistance to change and providing a social safety-net for those adversely affected is crucial to facilitating modernisation of the economy. Successful growth economies have all had the state playing an important but varying role: attracting investment; improving productivity, technology and competitiveness; delivering economic and political stability seems critical. To achieve this, political leadership, vision and achieving a sense of national purpose have always been decisive factors.

Political competition may have differing effects on components of both conflict and growth dynamics.[5] So what matters is how the political arrangements deliver effective legal systems, regulation and competition, an efficient public sector, and stable fiscal and monetary policies. What seems critical for investment and sustainable growth is that political conflicts can be settled by agreed rules, without violence, even if the institutions and the rules are highly biased to elite interests (Przeworski et al., 2000). The World Bank summed up its key lesson from the 1990s as the need not just to get the economics right, but to 'get the politics behind the economics right' (World Bank, 2005b). This requires getting beyond the imprecise, ahistorical and non-political use of terms such as property rights, institutions and infrastructure. Property rights, for example, are constructed through a process of constant political contestation—requiring enough stability in the process to maintain positive risk perception while allowing property rights to adjust to new conditions and technological change. Confusion over the historical evolution of 'secure' property rights is often based on the shaky historical justification of the supposed impact of the Glorious Revolution of 1688 as creating constraints on government in England; yet hardly explains the impact on property rights in Japan of the 1868 Meiji Restoration (Everest-Phillips, 2007a). Ha-Joon Chang (2006) observes that Korea's economic performance over the last four decades is the equivalent of turning Haiti into Switzerland.[6] Politics has to be put back into 'political economy' to answer how this can happen.

3 Japanese development experience matters

Growth only happens when it is politically possible. One crucial dimension to Japan's economic recovery was the era of Prime Minister Ikeda for whom delivering economic growth meant political survival. In 1960 the renewal of the Japan–US Security Treaty provoked violent nationwide protests. A sense of national crisis shook the confidence of the Japanese political, business and bureaucratic elite, and the previous government resigned in an atmosphere of political chaos. The new Ikeda government, from 1960 to 1964, deliberately sought a new national vision to avoid confrontation over political ideology. Ikeda, a former MITI minister, successfully refocused national attention on his plan to double Japanese GDP within a decade—this had succeeded by 1967. Ikeda was described as 'the single most important figure in Japan's rapid growth. He should long be remembered as the man who pulled together a national consensus for economic growth' (Nakamura 1987).[7] Japanese politics now turned on the *seichoritsu* (growth rate). Charles De Gaulle offered another epitaph, allegedly asking after meeting Ikeda: 'Who is that transistor salesman?'

Europeans who managed to visit Japan before the end of the Tokugawa regime's policy of isolation in the middle of the nineteenth century were always surprised to discover how effectively the country was run. The Swedish surgeon and naturalist Peter Thunberg, for example, travelling from Nagasaki to Edo (Tokyo) in 1776, was impressed how

> both the supreme government and the civil magistrates make the welfare of the state, the preservation of order, and the protection of the persons and property of the subject, an object of greater moment and attention in this country than in most others.
>
> (Voyage de C.P., 1796, IV, p.11)

This political strength combined with a strong work ethic developed a political system of reinforcing the state's legitimacy through building its administrative capabilities and political responsiveness to the needs of the population, with long-term consequences for commitment to the success of the private sector (Morishima, 1982). Japan successfully evolved from feudal to global power within two generations, but Japanese industrialisation was by no means self-evident. A German economist visiting Japanese factories in the late 1880s reported that 'Japanese workers work relatively little and that all work progresses only slowly' (Rathgen, 1891, p.422). The political elites of the Meiji Restoration that overthrew the feudal Tokugawa regime in 1868 were determined to preserve Japan's political independence through economic wealth and military power. Aware of the dangers of dependency, their unifying vision was to overcome this external threat: subservience to foreign powers 'is a deep-seated disease afflicting vital areas of the nation's life' (Fukuzawa, 1875 [1931], p.189). An effective state was essential and, mirroring continuing argument about modernisation theory about autocratic rule 'to get things done', even ardent democrats throughout the Meiji period were much concerned that the constitutional government could lead to violent rifts in the national political consensus that would set back progress in both political and economic development (Przeworski et al., 2000).[8]

British observers of Meiji Japan's early development prospects were however scathing:

> In this part of the world, principles established and recognised in the West appear to lose whatever virtue and vitality they originally possessed and tend fatally towards weediness and corruption … The Japanese are a happy race and, being content with little are not likely to achieve much.[9]

That concern then about corruption remains a timely reminder to understand governance challenges in a broader context of how development really happens. The Japanese in turn noted what the British advocated for development was not actually how Britain had developed. When the Iwakura Mission of 1871–3 visited Europe and the US to unearth the secrets of modernisation, the Mission's members discovered that both technology adaptation and constitutional arrangements mattered, but also that Britain had abandoned protectionism for free trade only after it had achieved industrial leadership and skills that enabled the country to benefit. The Mission summarised for the former samurai warriors now running the Emperor Meiji's government, the challenges Japan faced to catch up with the developed world:

> The strength of a country depends on the prosperity of its people which, in turn, is based on the level of output. To increase output, industrialisation is essential. However, no country has ever initiated the process of industrialisation without official guidance and promotion.[10]

In the early 1990s when the Japanese economy was still booming and the US felt in retreat politically and economically, much attention was devoted by the World Bank—thanks in part to strong Japanese lobbying and its then rising IDA funding contribution—to learning from the East Asian experience: most notably the World Bank report of *The East Asian Economic Miracle* (World Bank, 1993) and supporting studies on how Japan had led the region (the 'flying geese' phenomenon) in creating 'Communism that Works'—high growth with equity. The collapse of the Cold War provoked a considerable surge of interest in possible lessons for developing countries in this 'unorthodox' route to development. Japan and East Asia suggested a key role for some form of 'industrial policy' that, when done right, showed the state, not just markets, really did shape effective economic development.

The post-1945 state-led reconstruction of the Japanese economy had been achieved through 'a greater centralization of economic authority than had been achieved at the peak of Japan's mobilization for war' (Dower, 1999, p.544). Japanese post-war recovery and the subsequent success of East Asia were not built on any unique set of guiding principles or institutional arrangements (Haggard, 2004).

But the subsequent collapse of Japan's 'bubble economy' and the following decade of economic malaise, along with the Asian financial crisis of 1997–8, caused a precipitous decline in attention to what Japanese experience and ideas had to offer the international development community. This was unfortunate not least because those studies paid scant or inadequate attention to the importance of governance, a topic in itself then more focused on technocratic intervention than on learning the lessons of politics and historical experience. The inaccuracy of so much growth diagnostics often lies in limited understanding not just of government capacities but more importantly of political intentions critical for sustained economic success.

4 The 'dialogue of the deaf' on industrial policy

The debate over 'market' or 'government' failure posits a false dichotomy: effective development is 'a synergy between state action and market functioning' (Lange and Rueschemeyer, 2005). Yet exactly what form or function for these governance capabilities and political systems to transform an economy into high, sustainable growth is far from certain: state-led development has been highly effective in both authoritarian (e.g. Korea; Taiwan; apartheid South Africa) and democratic (e.g. Kerala; Mauritius; Costa Rica) regimes, but nothing is worse for sustainable economic growth than state-led development led by an anti-developmental state. The result has been a 'dialogue of the deaf' using selective evidence to assert 'market failure' or 'government failure' while ignoring politics and giving short shrift to history.

Successful development has always included some state manipulation of economic incentives. All developed countries became rich on the basis of policies contrary to strict prescriptions of free market and free trade. The debate around the 'proactive state' and the feasibility for developing country governments of trade and industrial policies focuses on the economics, yet the political governance is the critical dimension to success or failure: only governments can address political risk. The theological camps, concerned with belief systems more than evidence, can be divided as follows:

- *Atheists* question the efficacy of state policies, arguing away East Asian success that it would either have happened anyway or did not matter, and that outside the East Asian context industrial policy invariably ends up in failed inward-looking, import-substitution with open-ended interventions and protectionism (e.g. Krueger, 1990).

- *Agnostics* argue that East Asia only really saw modest gains from industrial policy, that it already had the seeds of its own success in high standards of bureaucracy, health and education, and that, given the high risk of rent-seeking and other potentially adverse effects, developing countries 'should be exceptionally cautious before embarking on such policies' (Pack, 2000, p.64). This line of argument asserts that in the new era of WTO and globalization the context and 'rules of the game' have completely changed: 'the role of activist industrial policies is still controversial but is likely to have been important' (World Bank, 2005b, p.83) in the past but no longer feasible under different circumstances.
- *True Believers* point to the 'East Asian Miracle' and seek to explain how industrial policy elsewhere usually failed to conform to the Asian experience (e.g. Rodrik, 2004). They argue that 'industrial policy … is an imperative. The idea that the government can disengage from specific policies and just focus on providing broad-based support to all activities in a sector neutral way is an illusion based on the disregard for the specificity and complexity of the requisite publicly provided inputs or capabilities' (Hausmann and Rodrik, 2006).

These entrenched positions in economic belief systems have obscured the importance of variations in the governance dimension as the key determinant: the balance between political structures and administrative capabilities that produce development outcomes. Institutional arrangements across East Asia may have been highly varied (Haggard 2004); but the political determination to overcome external and domestic threats was a universal characteristic.

Effective industrial policy principles are surprisingly clear: government support to the private sector that is always time-bound, and assessed by transparent performance criteria often linked to export orientation that provides market discipline through learning international competitiveness, as well as access to bigger markets; a concern to promote innovation and technological upgrading fostering of efficient local linkages; coordination of public and private initiatives; flexibility in adapting policy instruments to changing circumstances (Amsden, 1989; Wade, 1990; Evans, 1995). Industrial policy is not about 'picking winners'[11] but 'as a *process* whereby the state and the private sector jointly arrive at diagnoses about the sources of blockage in new economic activities and propose solutions to them' (Rodrik, 2004, p.24). It is an 'action science', learning by doing, including how to recognise and then close down failure. Industrialisation in developing countries involves high risks because learning is costly with uncertain returns. The state, in early levels of development, needs to foster entrepreneurship through promoting technological and marketing knowledge, developing a shared vision of the future, creating a willingness to take calculated risks and an ability to raise capital—all in ways that promote rather than thwart the development of private entrepreneurship (Stiglitz, 1996).

Successful industrial policy can support private sector innovation through a process of rewards and constraints to support efforts to adopt imported technologies to work under local conditions including protecting property rights enough to incentivise the development of new technologies; to offer educational facilities promoting appropriate technology and vocational training that support international competitiveness through diversification and technological upgrading; and enforcement of performance criteria using the disciplines of the international market. Time-bound subsidies to investment in new goods or production only work if the political determination exists for closing down failure before it becomes a new vested interest—the political and administrative capacity to do this was one of the major achievements of East Asia (Harrold et al., 1996; Aryeetey et al., 2003).

East Asia's iron triangle of political, bureaucratic and business consultation and collaboration was built on 'embedded autonomy', a meritocratic bureaucracy's capacity to manage the institutionalised dialogue between ministries, industry associations and research institutions without capture and distorting rampant corruption presents many major governance challenges. At the same time some 'infant industry' will not develop without import protection or support for domestic sales; and the start-up costs in some strategic industries do require state support to survive. The post-WWII patent system in Japan was specifically 'designed to promote technological catch-up and diffusion through incremental innovation' (Maskus and McDaniel, 1998).

Cartels have often been instrumental in establishing an industry and then creating the international competitiveness needed to allow gradual opening up: the continuing success of Swiss banking can be traced to the creation of the Swiss Bankers Association in 1912 that, in acting as a cartel in the Swiss banking sector, was instrumental in the emergence of the Swiss financial centre (David and Mach, 2006). In Switzerland, the absence of a patent law throughout the nineteenth century has been identified as one way that Swiss companies 'caught up' in new areas such as the chemicals industry. The patent law finally enacted in 1888—'the most incomplete and selective patent law ever enacted in modern times' (Schiff, 1971, p.93)—was simply designed to serve the vested interests of watch-makers (David and Mach, 2006). Effective intellectual property rights protection appears to reduce the number of competitive sectors in which to innovate, perversely increasing the possibility of duplication of innovation, thereby hindering growth (Horii and Iwaisako, 2005).

Yet much of the policy advice given to developing countries is ahistorical, based from the present on the liberal economic 'regulating state'. The political and capacity underpinnings for this may simply not exist in many developing country contexts where the state has a very different historical role and social fabric. At different economic, social and political levels of development, different strategies and institutions to support them are needed to kick-start and then maintain growth: 'The problems bedevilling latecomers today are not formal legal constraints but informal political pressures exerted by North Atlantic economies in favor of radical market opening. Latecomers lack a vision to guide them in responding to this pressure', especially a politically supported vision grounded in relevant science and technology (Amsden and Hikino, 2000).

5 Beyond political economy without politics

The industrial policy debate has been political economy without the politics. Effective policies requires effective state bureaucracies recruited on merit and motivated by competitive salaries, a transparent internal promotion process and career stability (Rauch and Evans, 2000). The attributes of the political systems that can consistently deliver such capabilities are much less certain (Khan, 1999). Political context is central to successful economic growth of which industrial policy is one element: clear political leadership, vision and enough consensus to maintain long-term development goals. How this is achieved is little understood—except in retrospect. Successful high-growth states have all shared a political imperative to deliver growth, and developed the capacity to deliver this effectively through pressure from a determined leadership, political vision on the necessity of economic growth and a sense of national purpose that shared prosperity underpinned political stability.

Sense of national purpose: Growth happens when the legitimacy of the state depends on its ability to deliver continuing economic development. The politics of economic growth by legitimating contentious policy and motivating individuals and social groups behind a shared vision of long-term development, is the least understood dimension to development. Successful late developers have almost all experienced some political settlement around elites' use of nationalism and the politics of economic growth to ensure social cohesion. State legitimacy matters for economic growth. The most economically successful African states, such as Botswana, are also the continent's most legitimate, so their political leaders do not need to maintain political power at the expense of development. State legitimacy in Africa is estimated to be worth 2.5 per cent annual growth (Englebert, 2002). Economic nationalism has played an important role in economic development in all successful development. Bismarck's development ideology of 'Blood and Iron' was picked up and adopted by Meiji Japan under the slogan *'Fukoku Kyohei'*—'Rich country, Strong military'. In the 1960s nationalism was a strong force in South Korea's slogan 'Defeat communism and achieve unification' and in Taiwan's 'Retake the mainland'.

The primary function of government, to create an inclusive polity, is greatly complicated in societies like Nigeria with significant deep ethnic divisions. Type of regime—democracy or autocratic rule—is not the decisive factor (Przeworski et al., 2000). Economic growth threatens to upset the political settlement on which inter-ethic collaboration may depend. Malaysia's 'Vision 2020' for achieving developed country status depends on a political settlement by which the Chinese and Indian populations that dominate the private sector are politically supported in return for growth funding the majority Malay population's social welfare and economic empowerment. National unity requires attention to equity and social cohesion through shared growth that has purchased political support for the social transformation of rapid industrialisation and economic growth. Providing decent housing for low-income households was, for example, a deliberate strategy for buying political support from growth in Singapore and Hong Kong, creating social inclusion that supported development objectives (Chua, 1997).

In all of East Asia, high-growth countries, inequality fell as incomes rose: 'Labour has been compensated for its decreased political role through wage policies tied to increases in productivity' (Johnson, 1982, p.151). Finland's economic development after its independence from a poor, vulnerable and conflict-prone country to a modern economy with model Nordic democratic institutions was the result of a post-Civil War political consensus around the country's need for policies that delivered both growth and equity, such as land reform and compulsory schooling (Jäntti, 2005). The politics of shared growth was less obvious in other high-growth countries such as Gabon or Botswana, but these are small and non-industrialised economies with a strong political class. By contrast Nigeria's repeated call for a 'national ideology' legitimising the *status quo* is found in 'development' that does not threaten the existing political settlement (Williams, 1977).

Political leadership: to pursue growth requires far-sighted individuals capable of building up the political coalition and administrative competence to deliver on long-term public goods necessary for economic growth: security, infrastructure, a culture of entrepreneurship, strong macroeconomy and international competitiveness. A major ambition for development must be to understand better when and how political leadership pursues sensible growth strategies in political competition (whether in democratic or authoritarian systems). While effective political good leadership of the growth process may depend on happenstance, the political climate that throws up effective leaders is shaped by political competition, transparency and accountability.[12] There is also an increasing phenomenon of 'the emergence of MBA politicians who are focused on improving the productivity of the private sector' (Ndulu et al., 2007, p.179).

Political vision for growth: ideas or ideologies create social cohesion and provide legitimacy for supporting growth. In 1721 the shogun had passed the Law against New Items with the state purpose 'to ensure that absolutely no new types of products should be manufactured' (Ramseyer, 1996, p.132). By the end of the Tokugawa era, however, traditional Confucian hostility to economic growth as the main source of national wealth, power and prestige was gradually abandoned, an ideological transformation embraced by the architects of the Meiji Restoration that made modern capitalism politically feasible in Japan (Sagers, 2006). Similar shifts are needed in many developing countries:

> There are some countries in the world where there are political leaders with sufficient self-confidence and political commitment that they are developing their own vision of how to develop. However, that is not happening in other countries. The main issue in economic growth today is not necessarily that views are changing that much in Washington but to what extent countries are taking their own futures into their own hands.
>
> (Rodrik, 2006, p.4)

6 What is to be done? Japan's expertise on growth and the UK's on governance

Countries often remain firmly stuck in their own historical experience that culturally determines a 'world view' on 'how development happens'. Japan and the UK, ex-colonial powers on different sides of the world with very different experiences of both governance and growth dynamics, with their relative aid budget size and staffing skills, have potential influence and importance in shaping the development agenda. They matter particularly at the moment in the international ambitions for scaling up aid and for improving aid effectiveness, for donor harmonisation, alignment and better genuine collaboration. The World Bank's *Economic Growth in the 1990s: Learning from a Decade of Reform* (2005b) provides an excellent introductory guide for putting political governance at the centre of economic growth dynamics.

Japan and the UK can offer a particularly important complimentary reflection on current ambitions, challenges and opportunities in international development. Modernity may be a Western project, for its two organizational complexes—nation-state and systematic capitalist production—have their roots in the specific characteristics of European history (Giddens, 1990). Japan, as the first non-Western country to succeed in mastering development, has an especially important potential voice and credibility with the developing world. Japan has continued to stress economic growth through technology adaptation and infrastructural development, themes otherwise overlooked by much of the rest of the development community until recently. Influential Japanese economists have been prepared to critique the preoccupation of neoclassical economics in Europe and the USA, with short-run equilibrium—markets as the balance of supply and demand—as only working, like liberal democracy, in the already advanced states, not in the catching-up context of developing countries. The Japanese experience has always made it apparent that late developers need to pay more attention to how the state must actively shape its private sector for international competitiveness (e.g. Murakami, 1996).

DFID is making serious efforts to scale up aid towards the honourable ambition of spending 0.7 per cent of GDP on international development. DFID has emerged as one of the leading agencies in the international development community on the topic of governance. The UK's 2006 White Paper, *Eliminating World Poverty: Making Governance Work for Poor People*, emphasised that 'First and foremost, the fight against poverty cannot be won without good governance. We need to help governments and citizens make politics work for the poor.' But although this otherwise excellent document had a chapter on Governance and a chapter on Growth, it failed adequately to link together these two essential attributes of development. To do that, DFID must answer the question posed by Japan's first *White Paper on Economic Development* [*Kogyo iken*] of 1884:

> Which requirements should be considered as most important in the present efforts of the government in building Japanese industries? It can be neither capital nor laws and regulations because both are dead things in themselves and so totally ineffective. The spirit sets both capital and regulations in motion … So if we assign weights to these three factors with respect to their effectiveness, the spirit should be assigned five parts, laws and regulations four, and capital no more than one part.

Japan is reforming its aid effort, and in 2008 took on the Presidency of the G8 while hosting the fourth Tokyo International Conference on African Development (TICAD IV). Facing fiscal problems and comparatively under-developed civil society interest in international development, it needs international support for its vision and potential to shape the international development agenda. Yet Japan has much to offer. It deserves praise for steadfastly focusing on low-profile objectives of growth through, for example, delivering on the need for proper infrastructure, which only now after many detours has again become fashionable with other major donors. Japan has been traditionally cautious on governance issues,[13] not least (and very differently from the UK) because development is in its own backyard of Asia where the legacy of its militarism of the 1930s and World War II create added sensitivities to 'meddling in internal affairs of other countries'. But Japan has started to become a 'normal state' in international relations. Japan has also begun to see its comparative advantage in international development in Japanese effective post-war democracy in delivering economic growth with comparatively high social equity—the 'good governance' agenda matched its self-interest as well as the common good.

For many years Japanese development philosophy has been emphasising development as a process of long-term transformation in which local context—initial conditions and stages of development—matter. The Japanese development community shares a strong belief, borne out of Japan's historical development process, that the role of the state in economic growth is more than just facilitation of market forces, but is to transform the economy in ways that only government authority and capacity to coordinate disparate individual interest makes possible. It is also practical and focused on real economic challenges of building an adequate infrastructure, developing a country's industrial structure and creating sustainable employment.

The ambition is a collaborative iterative process by which two major development partners, DFID and JICA, can harness their comparative advantages to find shared objectives for improving aid effectiveness around strengthened governance inputs in growth diagnostics and strategies, recognising that limitations in political leadership, strategic vision and sense of national purpose over economic growth are the universal 'binding constraint'. Japan is both an advanced industrialised country and, as an Asian late developer, enjoys close rapport with many developing states. Japan's economic development model still offers contemporary insights on the importance of capital formation and technology policies that contributed to Japan's rapid industrial capitalist growth: self-directed strategies, technological borrowing, taking advantage of shifts in comparative advantage from the product cycle, educational policy, business assistance, financial institutions, transfer of agricultural savings to industry, low wages policy and foreign-exchange rate policies conducive to export expansion (Nafziger, 2005). Japanese offers an understanding of growth more focused on business than applying the generalities of economic theory. A recent evaluation of the World Bank's work on China noted that: 'The terms "global value chain", "brand", "core business", "outsourcing", "research and development capability", "the IT revolution", and "global procurement", are absent from the World Bank's publications on enterprise reform' (Nolan, 2005, p.13).

Japan also offers excellence in strategic planning for development. This has been applied most strikingly in its support since 1995 of Vietnam's transition to a market economy. Japan's development economists and experts together with Vietnamese counterparts jointly developed a practical and comprehensive national growth strategy for macroeconomics, fiscal and monetary policy, industrial policy, and agricultural and rural development. The project has proved immensely valuable both in content and in stimulating economic coordination among key sectors and stakeholders ('growth coalitions'). Like previous East Asian success, it used the discipline of commitment to free trade as a disciplining device for improving performance, and an approach based on self-help rather than aid dependence. This important project is credited with helping Vietnam continue its rapid economic growth through warding off other donor and IFI pressure to a Poverty Reduction Strategy Paper (PRSP) that would otherwise have made Vietnam's budget excessively biased toward pro-poor expenditures at the cost of economic requirements including infrastructure—a point belatedly conceded by other donors' and the World Bank's recent 'rediscovery' of the importance of infrastructure for long-term development (Ishikawa, 2001; Ministry of Foreign Affairs, Japan, 2002).

Japan and the UK are well placed to promote better growth diagnostics that start from the governance challenges, incentives and practical capacity constraints. This starts from the policy debate around the growth components of Poverty Reduction Strategies (PRSs), to inform donor programmes on growth, underpinned by good diagnostics with an emphasis on implementation of recommendations and monitoring progress. Japanese growth expertise is perhaps uniquely placed to address major governance questions: How much of governance form matters to deliver essential governance functions? What institutional arrangements are universal requirements essential for economic growth, and what requires local ownership and context specific policy?[14] Are there stages in economic and political development where new institutional arrangements become critical to maintain growth—e.g. China's new law on property rights in 2007, after nearly three decades of economic growth that defied the mantra of 'secure property rights' as the key to development? This requires bringing politics explicitly into the analysis of the market (and not just into the analysis of the state) as political constructs, defined by formal and informal institutions of rights and obligations, whose legitimacy, and therefore whose contestability, is ultimately determined through political processes. Institutions shape people's political actions given their motivations and perceptions because they influence people's perceptions of their own interests, of the legitimate boundary of politics and of the appropriate standards of behaviour in politics (Chang, 2001). DFID is best placed to complement Japanese growth expertise with insight on the politics of growth as well as the institutional dimension of governance matter: development as building effective political leadership, vision and supporting national consensus on long-term growth tied to social equity.

Japan's experience and approaches to governance with a growth outcome objective should push the international financial institutions and other key players to do more to make theory and policy fit the facts of Asia's success, less choosing facts to fit theory through seeking better evidence-based research on what really works. This requires policy experimentation on what aspects of state leadership, vision, national purpose and technical capabilities can be developed in what local political context and under prevailing WTO global rules, for example, through:

- national strategies for international competitiveness and export orientation;
- promoting economically literate political leadership and paying attention to the political and economic vision and interests of elites, as central to poverty reduction;
- matching capacity to alleviate the negative aspects of growth such as environmental concerns, political and social tensions over the distribution of growth, urbanisation, housing shortages, regional variations in unemployment, as well as a welfare safety-net;
- improving organisational effectiveness of the United Nations Conference on Trade and Development (UNCTAD), the leading international body of expertise in this area but its current impact does not reflect its potential.[15]

An Anglo-Japanese development cooperation with a 'governance for growth' emphasis should actively promote the role of government as providing the political vision for reform to 'catch up', matched by the capacity to implement it effectively to transform societal relationships into those needed for a market economy through policy actions to promote:

- support for governments to develop their leadership, strategic vision, sense of national purpose and technical capacities through active policy experimentation, 'learning by doing' to promote innovation, entrepreneurship and technological adaptation. 'Governance for growth' suggests some key areas for attention in Africa through infrastructure initiatives like the Infrastructure Consortium for Africa and NEPAD Infrastructure Project Preparation Facility; and investment climate policy and initiatives like the Investment Climate Facility and the Africa Enterprise Challenge Fund. Donors need better political governance analysis of political incentives to promote growth (Everest-Phillips, 2007b);
- long-term planning: the wish and capacity to think long-term needs to be taken more seriously—such as by implementation of National Plans of Action produced by countries completing the African Peer Review Mechanism linked to changing expectations; creating political vision beyond the current limitations of most PRSPs; long-term planning is also an important potential coordination process in itself, by which political leadership, officials and the private sector need to agree on the obstacles to growth and practical ways to implement reform; and finding ways to make industrial policy work according to country political realities;
- mitigation of impacts of growth: 'Economic growth is sustainable only when the opportunities and fruits of growth are perceived to be shared equitably by the standards of that society' (Ohno, 2002, p.4);
- developing the inter-disciplinary capacity for economists and governance experts to talk a common language.

Notes

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1 For definition, see World Bank (2005a and Moore and Schmitz (2007).

2 Including the 'ninth' MDG of 'Good Governance' that various countries such as Albania, Azerbaijan and Mongolia have also adopted.

3 For example, China does not have high scores on accelerating resource allocation to growth sectors, prioritising infrastructure for these sectors and making credible support available to investors bringing in advanced technologies (Qian and Weingast 1997).

4 Gujarat has consistently attracted a higher share of investment. West Bengal failed to capitalise on its initial conditions, and Tamil Nadu has a fluctuating performance. Investment per capita in Gujarat was two and half times the all-India average by 1994, while in Tamil Nadu such investment stood at 0.85 of all-India levels, and in West Bengal at 0.47. Local politics in Gujarat developed 'strategic capacities' that have consistently made that state attractive to private capital, while in West Bengal and Tamil Nadu local politics have tended (at least until recently) to have the opposite effect (Sinha, 2005).

5 According to Pinto (2005), political competition possibly decreases the rate of physical capital accumulation and labour mobilisation but increases the rate of human capital accumulation and productivity change.

6 Life expectancy at birth in Korea in 1960 was 53 years. In 2003, it was 77 years. In the same year, life expectancy was 51.6 years in Haiti and 80.5 years in Switzerland. Infant mortality in Korea was 78 per 1,000 live births in 1960 and 5 per 1,000 live births in 2003. In 2003, infant mortality was 76 in Haiti and 4 in Switzerland. The 1960 Korean figures are from Chang (2006), Tables 4.8 (infant mortality) and 4.9 (life expectancy); 2003 figures are from UNDP (2005), Tables 1 (life expectancy) and 10 (infant mortality).

7 Johnson (1982, p.252) also notes the importance of the Ikeda Plan for boosting national self-confidence essential for investor confidence.

8 No conclusive evidence exists that non-democratic regimes are more effective in stimulating growth, and may be less effective at sustaining it.

9 *Japanese Gazette*, Yokohama, 1882.

10 Quoted in Ohno and Ohno (1998, p.7).

11 'The governments of Taiwan, Korea and Japan have not so much picked winners as made them' (Wade, 1990, p.334).

12 Glaeser et al. (2004), besides demolishing the use of 'institutions' to explain growth, demonstrate that economic growth since the 1960s has to a significant extent been a consequence of having effective leadership, rather than constraints on executive authority for institutionalised credible commitment.

13 JICA's 2005 Participatory Development and Good Governance Report of the Aid Study Committee suggested that good governance as the basis for participatory development has five subcategories of goals including building a market environment.

14 Chang (2007a) characterises this as: political democracy; an independent judiciary; a professional bureaucracy, ideally with open and flexible recruitments; a small public-enterprise sector, supervised by a politically independent regulator; a developed stock market with rules that facilitate hostile M&A; a regime of financial regulation that encourages prudence and stability, through things like the politically independent central bank and the Bank for International Settlements (BIS) capital adequacy ratio; a shareholder-oriented corporate governance system; labour market institutions that guarantee flexibility (ch.2, p.4).

15 UNCTAD is attempting to respond to international criticism of its performance and poor reputation: http://www.unctad.org/en/docs/wpd168_En.pdf.

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7 The Japanese approach to growth support in developing countries

Supporting dynamic capacity development*

Izumi Ohno

1 Introduction

Following a decade of the poverty reduction drive, the growth agenda has returned to the center of global development debates. While the first-generation poverty reduction strategies (PRS) in the late 1990s to the early 2000s targeted social sectors, the recent years have seen renewed interest in growth promotion such as private sector development, infrastructure, agricultural and industrial development in both developing countries and the international aid community.

Typical examples of this trend shift are intensified efforts to devise analytical tools such as growth diagnostics (Hausmann et al., 2005) and the *Doing Business* surveys (World Bank and IFC, 2004) by researchers and donor agencies. Various studies on growth strategies have been undertaken, including *The Growth Report* (IBRD and CGD, 2008). Priority of donor assistance has been also changing. The revival of donor support to infrastructure development that sharply declined in the latter half of the 1990s and the promotion of public-private partnerships (PPP) confirm such changes.

It is widely recognized that economic growth is essential for sustainable poverty reduction and that today's successful East Asian economies, including Japan, have adopted growth-oriented development strategies. Based on its own experience as a latecomer country in the past, Japan has for long stressed the importance of sustaining growth so that developing countries could attain self-reliance and overcome aid dependency (MOFA, 2003, 2005).[1] Now, the point of global debates is no longer the choice between growth and poverty reduction, but the content and methodology for formulating and implementing country-specific growth strategies.

From this perspective, it is important to make a deeper analysis of characteristics of donor approaches to growth support. There exist notable differences among donors in how they provide development assistance to developing countries. Differences can be often contrasted as: (i) the structural adjustment approach focusing on macroeconomic stability and

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regulatory reforms, versus the approach that emphasizes the real sector such as industrial structure and labor; (ii) budget support that emphasizes overall policy framework and public financial management, versus project aid focusing on concrete activities with field-orientation. In both (i) and (ii), the Japanese approach tends to emphasize the latter. More recently, the Japan International Cooperation Agency (JICA), an implementing agency of Japan's bilateral Official Development Assistance (ODA), disseminates the concept of the "capacity development" approach[2] that emphasizes ownership, field-orientation, mutual learning, and joint problem solving with partner countries.

There are at least two reasons why the deeper understanding and dissemination of different approaches to growth support are important. First, with the resurgence of the growth agenda, an increasing number of developing countries begin to show interest in the growth support that Japan has offered in East Asia. Not a few African countries have approached the Japanese government, requesting for knowledge sharing and cooperation based on the East Asian development experiences, including (but not limited to) the occasion of the Fourth Tokyo International Conference for African Development (TICAD IV) held in May 2008. Second, in the context of development partnerships, donors are urged to strengthen selectivity of their assistance, based on respective comparative advantage ("division of labor"), in order to avoid duplications and fragmentation of aid (OECD, 2005). It is thus becoming more and more important for Japan to clarify the comparative advantage and complementarity of its growth support, in light of that of other donors.

This chapter intends to respond to such emerging needs in the international aid community. Taking advantage of growth resurgence and rising interest in the East Asian development experiences, Japan should make stepped up efforts to share its approach to growth support with developing countries. This is so especially in countries which are not familiar with the East Asian experiences. The remainder of this chapter is organized into five sections. Section 1 will outline the basic perspectives and characteristics of Japanese growth support. Section 2 will examine major growth studies and analytical tools that have been extensively used by researchers and donors. Section 3 will examine growth support approaches of major donors, such as the World Bank, the United Kingdom (UK), the United States (US), and Germany. Section 4 will analyze how Japanese growth support can be complementary to the Western way and will provide examples in Asia and non-Asian countries.

2 Basic perspectives of Japanese approach to growth support: how does it differ from the Western approach?

According to Yanagihara (1998), there are two contrasting ways of understanding and analyzing economic development. One focuses on the "framework" of an economic system and its management; the other focuses on an economy as the sum total of its "ingredients" or component parts. The "framework" represents rules of the game according to which economic agents make decisions and take action in a given economy. In contrast, the "ingredients" refer to tangible organizational units such as firms, official bureaus, and industrial projects and their aggregations such as industries, sectors, and regions. The ingredients approach conceives the economy as a collection of these components. It takes deep interest in how individual players are doing in the field and the outcome of each game. As general tendency, the "framework" approach is prevalent in Western (especially Anglo-Saxon) donors, while the "ingredients" approach is more common in Japan and East Asia.

In the case of growth support, Japan's "ingredients" approach is characterized by real-sector orientation with four inter-related features: "goal orientation," "field-orientation," "joint work," and "dynamic capacity development" as follows (JICA and GRIPS, 2011):

- *Goal orientation*—this approach pays attention to strengths of a country and considers how to make full use of its economic potential. Particular bottlenecks are identified in this light (such as infrastructure, human resources, technology, specific institutional capacity), and goals and targets are set to remove the bottlenecks. Concrete targets, such as construction of a trunk road from A to B or promotion of certain industry by a certain deadline, are preferred over general improvements in governance or private sector capability. Then plans and actions are created in backward direction from future to present to attain certain goals and targets.
- *Field orientation*—Japanese development officials and experts are more concerned with concrete facts and improvements on the ground than crafting policy frameworks or writing reports. They visit project sites and production sites frequently and establish close contacts with the counterparts of developing countries, in order to formulate and implement desirable and feasible measures viewed from partner countries.
- *Joint work*—development occurs when a developing country learns how to make and execute policies effectively. Japanese officials and experts are conscious of country ownership and work side-by-side with developing country counterparts so that the latter can learn skills and technology through on-the-job training (OJT). Patience is required when the mindset and knowledge of the counterparts are weak, but this is considered inevitable. Japan does not wish to set up a parallel mechanism for implementing aid projects; it instead wants to utilize and strengthen the local mechanism even if it is initially slow and inefficient.
- *Dynamic capacity development*—Japanese cooperation is based on the premise that developing countries will not stay underdeveloped forever. Through policy learning and experience, they are expected to take off

> economically and eventually graduate from aid. Assistance is given for a time to accelerate the day of graduation and not as permanent charity for the poor. Dynamic capacity development aims at improving policy capability through acquiring knowledge and skills by solving specific problems toward achieving concrete goals. This approach helps the developing country gain confidence step by step. It differs from the "good governance" approach that focuses on improving general policy capability with no specific goals.

Certainly, Japan's approach to development assistance shares many commonalities with the Western approach. Nevertheless, as a matter of emphasis, the Western donors tend to focus on the policy and institutional framework, such as market functions, principles of government interventions and budgets and public investment, empowerment and participation, monitoring, administrative efficiency and accountability. Japan is more interested in the real sector, with attention to the abilities and problems of individual firms in the private sector that play a key role in the market economy, such as technologies, human resources, productive elements, demand trends, products and commodities, industrial structures, marketing, logistics efficiency in individual industrial sectors and regions in recipient countries.

3 Review of major growth studies and analytical tools

3.1 Growth diagnostics

Among a number of growth studies and analytical tools, recently growth diagnostics has attracted high attention among development experts. Growth diagnostics is a systematic methodology for undertaking country diagnosis and identifying the most binding constraints to growth (Hausmann et al., 2005). It is often referred to as the "HRV" model after the Harvard professors who pioneered it, Ricardo Hausmann, Dani Rodrik, and Andres Velasco. This model has been pilot-tested by aid agencies including the World Bank and the UK's Department for International Development (DFID) in a number of countries and is increasingly being incorporated in their economic reports. Growth diagnostics attempts to remove a limited number of key constraints to growth specific to each country by using a decision-tree methodology (Figure 7.1). This is a major departure from the traditional approach of directing the same Washington-Consensus-style reforms at all countries, based on a long list of interventions. In this regard, growth diagnostics has made invaluable contributions to today's intellectual debates.

Nevertheless, various arguments are presented on the need to improve the approach adopted by growth diagnostics. First, the diagnosis is driven by economic analyses, with limited attention to the political feasibility of proposed measures. Its prime concern is to identify "what should be done" to initiate

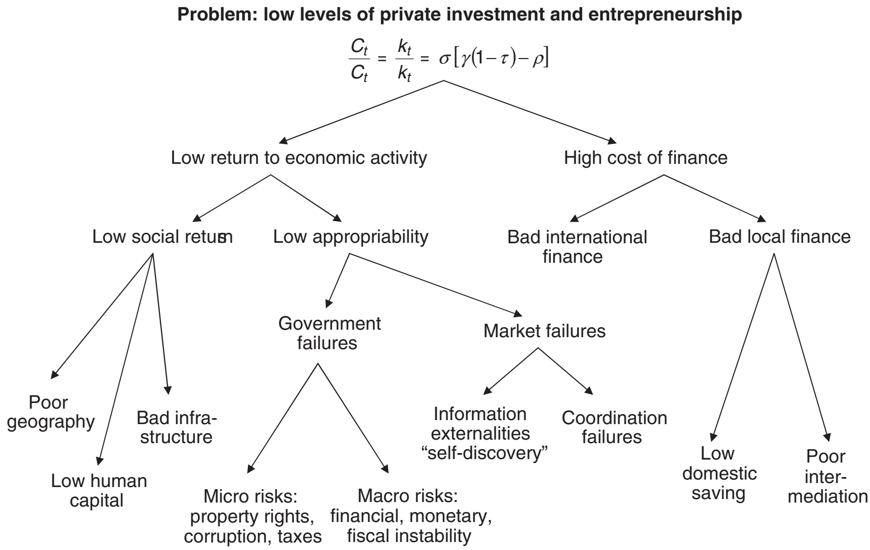

Figure 7.1 HRV model
Source: Hausmann et al. (2005).

growth, rather than "what can be done" given the existing political and institutional constraints. Consequently, growth diagnostics does not give practical guidelines about the formulation of country-specific growth strategies, leaving the task to the self-discovery[3] of individual countries (Felipe and Usui, 2008; Ohno and Ohno, 2012). Second, the structure of problem setting is too narrow, and the decision tree treats the low level of private investment as the key problem. Third, it is neither realistic nor desirable to identify weaknesses of developing countries in terms of international standards and try to remove them. This implies that developing countries should be "average" on all scores (for example, Worldwide Governance Indicators [WBI] and Doing Business Indicators, proposed by the World Bank, see below) before formulating and implementing their growth strategies (Ohno and Ohno, 2012). Fourth, while focusing on short-run constraints, growth diagnostics does not indicate the sequence of measures to be adopted over the long run. Even if one constraint is removed, another is likely to emerge in the complex growth processes. For all these reasons, whether growth diagnostics will become a truly useful instrument for policy makers in developing countries remains to be seen. If not carefully designed, there might be a risk of its becoming an additional donor-driven instrument.

3.2 Doing Business surveys and investment climate assessment

Doing Business surveys and investment climate assessment, initiated by the World Bank, are analytical tools that have been increasingly used for supporting private sector development in developing countries. Doing Business surveys rank economies based on 11 indicators of business regulation that record the time and cost to meet government requirements in starting and operating a business, trading across borders, paying taxes, and closing a business.[4]

The World Bank and the International Finance Corporation (IFC) have published annual reports since 2004 (World Bank and IFC, 2004) and have been tracking regulatory reforms aimed at improving the ease of doing business. *Doing Business 2011* covers 183 countries (the top 3 reformers are Singapore, New Zealand, and Hong Kong (China) with Japan ranking 18th). Doing Business surveys are used for benchmarking to help policy makers assess the regulations in their own countries based on international comparisons and learn from global best practices so that they can prioritize reform measures.

Subsequently, the World Bank published the *World Development Report 2005*: *A Better Investment Climate for Everyone* (hereinafter referred to as *WDR 2005*, World Bank, 2004). The investment climate comprises all the elements of the regulatory business environment, but in addition it includes "location-specific factors that shape the opportunities and incentives for firms to invest productively, create jobs, and expand" (World Bank, 2004, p. 2). These factors include the quality of infrastructure, the overall level of education, rule of law, political stability and security, and functioning financial markets, and so on. Drawing on surveys of over 30,000 firms in 53 developing countries, *WDR 2005* analyzed how and to what extent the government policies and behaviors have affected these location-specific factors by measuring their impacts on costs, risk, and barriers to competition. Policy uncertainties, bribery, regulations and tax administration, courts and justice systems are main concerns of the firms surveyed. Triggered by the *WDR 2005*, the World Bank has started to conduct investment climate assessment in many developing countries, including 22 Sub-Saharan African countries (normally, about 400 sample firms). The results of these surveys are utilized to identify factors that negatively affect private sector development in respective countries.

While investment climate refers to a broader set of enabling factors than the Doing Business indicators, they have a lot in common. Both focus on the general improvement of business environments (level-playing field), giving importance to general frameworks.

3.3 Good governance and the "two-part strategy" for an effective state

Building state capability is a fundamental task for development, and there have been numerous studies on the assessment, measurement, and methodology for state building. Particularly, there have been active debates on the relationship between state capability and industrial policy. While recognizing the need for selective intervention policies implemented by governments in Japan, South Korea, and Taiwan, *The East Asian Miracle* by the World Bank (World Bank, 1993) took a cautious stance,[5] stating that it is difficult to apply these policies in developing countries with poor institutional capacity. It concludes that developing countries should focus on the policies of getting basic conditions right, in combination with export promotion policies. This basic stance of the World Bank has not changed since then.[6]

Mindful of the challenges, the *World Development Report 1997: The State in a Changing World* (World Bank, 1997) has proposed the "two-part strategy" that argues for two steps to a more effective state: (i) matching the state's role to its capability; and (ii) raising state capability by reinvigorating state institutions. This strategy is widely regarded as mainstream thinking at present. Acknowledging that certain industrial policies do not require high levels of institutional capacity, the two-part strategy does not categorically deny the use of industrial policies in developing countries. Neither does it see institutional capacity as something unchangeable. In this sense, the strategy appears to provide flexible guidelines for developing countries. However, its practical implication is that the governments of developing countries with low institutional capacity should focus on getting the fundamentals rights (i.e., the provision of public goods and other intermediate services to correct market failures) without performing high-level interventions. Consequently, the two-part strategy is substantively same as the previous ones, including the arguments presented by *The East Asian Miracle* (World Bank, 1993).

The two-part strategy shares a common perspective with the "good governance" approach in that it aims at the comprehensive and general enhancement of state capability. With increased attention to good governance since the 1990s, the World Bank developed the Worldwide Governance Indicators (WGI) designed to quantify the six dimensions of governance in countries around the world (voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of corruption) and compiled data for cross-national comparison. WGI have been published annually since 1996. WGI serve as useful benchmarks to help understand the relative level of governance of a particular country and institutional reforms required for its development. Nevertheless, these indicators tend to suggest comprehensive reforms that may not be implemented by developing countries with scarce resources, and questions remain as to whether it is realistic to recommend a developing country to adopt an unfocused approach to enhance its general state capability. The critics of the good governance approach note the problem of causality between growth and governance, impossibility—and even non-necessity—of attaining good governance in low-income countries, the need for a smaller or different set of institutional targets to start with, and the absence of empirical evidence that good governance is necessary for growth (Grindle, 2004; Shimomura, 2005; Khan in Chapter 5 of this volume).[7]

4 Approaches to growth support by major donors

4.1 The World Bank

During the first half of the term of the former President Wolfensohn (in office from 1995 to 2005), the World Bank's assistance prioritized the social sector that directly contributed to poverty reduction. During the second half of his term, the Bank resumed its support to infrastructure and private sector development. Nicholas Stern, then Chief Economist (in office from 2000 to 2003), played an instrumental role in this change. Stern declared that the improvement of investment climates and the empowerment of the poor are the two fundamental pillars of the World Bank's activity. Against this background, analytical tools such as Doing Business surveys and investment climate assessment were introduced, which stimulated interest in growth-related research. Moreover, *Economic Growth in the 1990s*: *Learning from a Decade of Reform* (World Bank, 2005) highlights the need to formulate and implement growth strategies beyond the Washington Consensus, based on its critical analysis of the growth experience of developing countries during the 1990s and the reform measures promoted by the World Bank. Strongly influenced by the growth diagnostics approach,[8] it points out the need to formulate and implement growth strategies tailored to the circumstances of individual countries rather than applying uniform policies, as well as the need to identify and remove binding constraints on growth faced by each country. The renewed interest in economic growth is also symbolized by the fact that the World Bank served as the secretariat of the Commission on Growth and Development chaired by Michael Spence, Emeritus Professor at Stanford University (Nobel economics prize winner)[9] and supported the compilation of *The Growth Report* (IBRD and CGD, 2008).

Growth diagnostics, using the HRV tree model, promoted various studies within different units of the World Bank. For example, the Bank's country economic memorandums (CEM) have increasingly incorporated the growth diagnostics approach to support its operations. The Uganda CEM (World Bank, 2007)—produced by the World Bank with the financial support of DFID, the Netherlands, Denmark, and Ireland—stresses the need for a well-prioritized, pro-active growth strategy focusing on removing the most binding constraints on growth. (But, it appears that growth diagnostics is not treated as a standard analytical tool equivalent to Doing Business surveys and investment climate assessment.)

A more recent, notable development, is the concept of new structural economics proposed by Justin Lin (born in Taiwan), former Chief Economist at the World Bank (in office from 2008 to 2012). According to Lin, economic development as a dynamic process requires industrial upgrading and corresponding improvements in "hard" and "soft" infrastructure at each stage. The new structural economics stresses the need to better understand the implications of structural differences at various stages of a country's development—especially in terms of the appropriate institutions and policies, and the constraints and incentives for the private sector in the process of structural change (Lin, 2010, 2011). It does appear that Lin's views seem to give greater emphasis on "ingredients" of the economy. But, it is yet to be seen whether his views will bring change in the World Bank's official position to the role of industrial policies in developing countries.

4.2 The UK

Among bilateral donors, the UK has played a lead role in driving global development debates. Especially, since its establishment in 1997, DFID has successfully elevated poverty reduction to the ultimate goal of development, by actively promoting the Millennium Development Goals (MDGs) and the PRS in the international aid community. But, recently, DFID has started to argue that growth is the most effective way to reduce poverty. At the 2005 Gleneagles G8 Summit, the UK took the initiative in launching the Infrastructure Consortium for Africa with the aim of sharing information and enhancing collaboration in infrastructure support among donors. Its policy shift has become clearer under the leadership of the former Under-secretary of State for DFID, Shriti Vadera (in office during June 2007–January 2008). Subsequently, DFID formulated a series of policy documents, including "Growth and Infrastructure Policy Paper" (DFID, 2007), *Growth: Building Jobs and Prosperity in Developing Countries* (DFID, 2008a), and *Private Sector Development Strategy: Prosperity for All Making Markets Work* (DFID, 2008b). More recently, under the Coalition government that took power in May 2010, DFID has declared that it will put greater emphasis on boosting economic growth and wealth creation, by collaborating more closely with the private sector on development (DFID, 2012).

The first two policy documents (DFID, 2007, 2008a) articulate DFID's commitment to work on reducing poverty through economic growth. They discuss specific measures such as strengthening infrastructure support and private sector development, putting growth and opportunities at the heart of the international development dialogue, and increasing intellectual support in order to achieve sustained growth through the establishment of the International Growth Center (IGC). The private sector development strategy (DFID, 2008b) emphasizes DFID's commitment to making markets function better and with greater fairness[10] and outlines three approaches to deliver it—by working with business for sustainable development, working with the governments and other donors to promote "inclusive market development," and improving research and knowledge management that support private sector development. DFID also collaborated with the World Bank in the preparation of the *WDR 2005*.

The above policy documents take the same perspective as that of the Doing Business surveys and investment climate assessment in that they all aim at the general improvement of business and investment climates and the strengthening of market functions. Growth diagnostics is used in DFID's operations in Malawi, Uganda, and Rwanda etc., although no operational guidelines are established and great variance exists in their contents and formats.

Infrastructure support is another example of DFID's orientation to general frameworks. DFID's infrastructure support is characterized by the active use of multilateral and regional development organizations and the establishment of multi-donor facilities, backed by strong interest in innovative financing and architecture for private-sector financed infrastructure. DFID officials are less involved in individual infrastructure projects, compared with Japanese aid officials, who are interested in the details of individual projects such as their geographical location, technical design, and relationship with regional and industrial development (see Section 4). For example, DFID's support in Africa includes the following menus: (i) policy coordination at the G8 level by the Infrastructure Consortium for Africa; (ii) infrastructure support through the World Bank, European Union (EU), and AfDB, as well as the Southern African Development Community, East African Community, etc.; (iii) establishment of multi-donor facilities aimed at promoting public-private partnerships and developing private sector-financed infrastructure; and (iv) strengthening infrastructure components of bilaterally-funded budget support. Regarding the above (iii), DFID took leadership in forming the Private Infrastructure Development Group (PIDG) within the World Bank in 2002, along with the Netherlands, Switzerland, and Sweden. The PIDG aims to mobilize financial support to reduce the risks involved in private sector infrastructure businesses and develop a comprehensive support program covering the entire business development processes, including the design, planning, construction, and operation stages.

4.3 The US

In the US, there are two main aid organizations: the United States Agency for International Development (USAID), established in 1961; and the Millennium Challenge Corporation (MCC), established in 2004. Both organizations provide grant aid, giving great importance to free market economies and private sector development, human development, good governance, and democracy, which reflect the ideals of the US.

The amount of the US foreign aid, especially aid for economic growth, declined sharply in the 1990s. However, the USAID's latest economic growth strategy, *Securing the Future: A Strategy for Economic Growth* (USAID, 2008), puts clearer and greater emphasis on the need to achieve economic growth and private sector development, to help reduce poverty as well as promote political stability, prosperity, and democratization and reform the society of developing countries from a long-term perspective.[11] Based on this strategy, USAID proposed that the US government pay attention to the following factors to improve firm productivity and competitiveness to stimulate economic growth: (i) stable macroeconomic policies (fiscal, monetary, and exchange policies, etc.) and microeconomic aspects of governance that affect market functions and firm behaviors (business regulation, market functions, property rights and the rule of law, trade policies, etc.); and (ii) improvement in investment climates (infrastructure, finance, and human resources). USAID utilizes the data obtained from Doing Business surveys for analyzing the microeconomic aspects mentioned in the above (i). It also supports the growth diagnostics approach and emphasizes the importance of identifying country-specific binding constraints to faster growth, while applying fundamental economic principles such as the protection of property rights, contract enforcement, market-based competition, appropriate incentives, and financial and debt sustainability.

The MCC provides large-scale grants to developing countries that pass certain eligibility criteria based on their policy performance. More specifically, it selects eligible countries based on the 17 indicators, broadly classified into 3 areas: "Ruling Justly," "Investing in People," and "Economic Freedom." For example, 6 indicators (business start-up, regulatory quality, trade policy, inflation, fiscal policy, and land rights and access) are used to assess the performance of "Economic Freedom" in developing countries, and Doing Business survey data are used for this assessment. The performance of "Ruling Justly" is assessed by 6 indicators (control of corruption, rule of law, voice and accountability, government effectiveness, civil liberties, and political rights), and the WGI data are taken into consideration.

Regarding project implementation, both USAID and MCC establish implementation units independent of the government agencies of the partner country, or outsource project management to consultants and NGOs. This is partly to ensure the transparent and accountable management of funds coming from US taxpayers. This approach differs from the Japanese assistance which emphasizes joint work with the government's counterpart agencies, aiming at their dynamic capacity development through hands-on experience of project implementation.

4.4 Germany

German cooperation for growth promotion is distinctive from the above donors. There are largely shared views among German development officials and experts that the approaches adopted by Doing Business surveys and investment climate assessment are not sufficient to improve firm performance and develop competitive advantages. A joint report by the United Nations Industrial Development Organization (UNIDO) and the German Agency for Technical Cooperation (GTZ), which is now the German Agency for International Cooperation (GIZ), presented a new approach, called the neo-structuralist approach (UNIDO and GTZ, 2008).[12] This report points out the need for not only creating market institutions and frameworks but also taking measures with attention to industrial structures, technologies, labor markets, and human resource development, in order to enhance competitiveness with pro-poor outcomes in globalized and knowledge-intensive markets. The UNIDO/GTZ report was commissioned to the German Development Institute (GDI)—a think tank for German development cooperation, supported by the Federal Ministry for Economic Cooperation and Development (BMZ). GDI plays an important role in growth-related research and has been engaged in research projects on industrial policies in collaboration with BMZ and former GTZ, currently GIZ (Altenburg, 2011).

As shown in Figure 7.2, the neo-structuralist approach does not conflict with the approaches of Doing Business surveys and investment climate assessment. Unlike the latter approaches, however, it emphasizes the need to adopt targeted measures, such as strategic trade policy and selective protection, sectorally targeted human capital initiatives, targeted research and development policies, industrial cluster policies, in addition to overall improvements in business and investment climates.

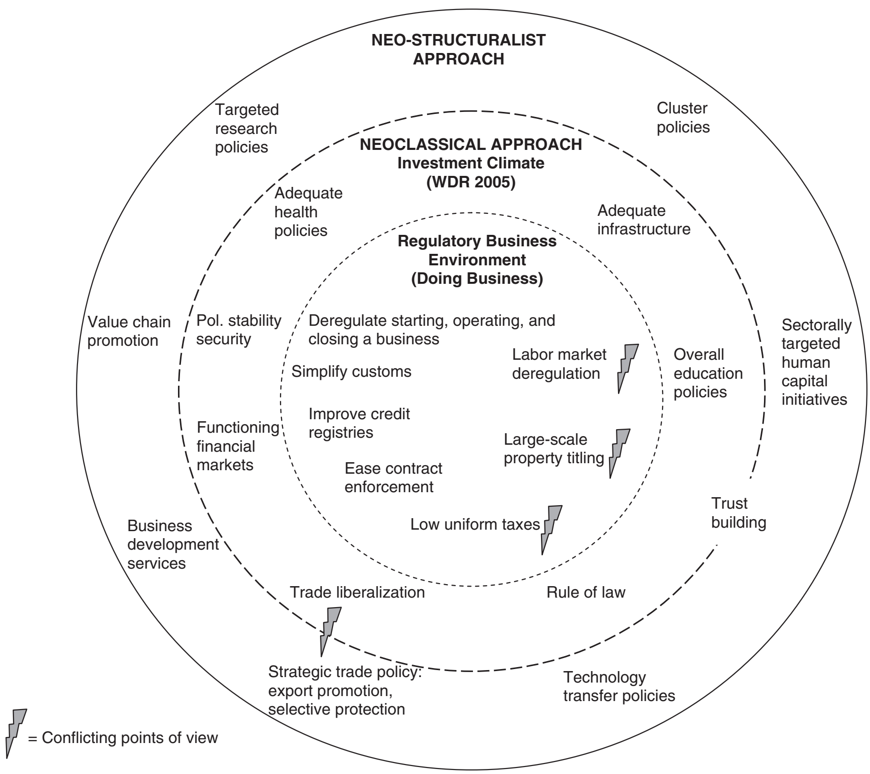

Figure 7.2 Neoclassical and neo-structuralist approaches
Source: UNIDO and GTZ (2008, Figure 1, p.7).

Guided by the BMZ's overall policy, GIZ's growth support gives high priority to: (i) economic policies and private sector development, (ii) technical and vocational education (including linkages with the labor market), and (iii) financial systems. Furthermore, with strong focus on capacity development in providing technical cooperation, GIZ stresses the need to enhance the capacities of various stakeholders, including policy makers, government administrators, business, and firms, in order to bring the benefits of economic growth to the wider segments of the society. Reflecting such perspectives, BMZ's policy and GIZ's cooperation take a multi-level approach to private sector development, which combine macro-level (such as regulatory frameworks and competitive environments), meso-level (such as institutional environment, e.g., chambers of commerce and industrial associations), and micro-level (such as inter-firm linkages and industrial human resources) policies and measures. In this sense, the German approach to growth support has orientation of both frameworks and ingredients.

Regarding infrastructure development, KfW Development Bank (Kreditanstalt für Wiederaufbau Entwicklungsbank) is a key agency for providing financial cooperation. While KfW has recently started providing budget support, project aid is a main instrument for its financial cooperation. As explained earlier, GIZ provides practical technical cooperation under its direct management. In this respect, Germany and Japan share commonalities in their approaches to growth support.

5 Japan's growth support approach: examples and complementarity with the Western approach

5.1 Concept of dynamic capacity development

As stated before, goal orientation, field-orientation, joint work, and dynamic capacity development are four inter-related features of the Japanese "ingredients" approach. Among them, dynamic capacity development takes place in the process of designing and implementing goal-oriented growth strategies and measures. It aims to improve ability through selective, hands-on effort by setting clear goals and making focused efforts to enhance the unique strengths of the country. Instead of comparing countries across the board to rank them or find faults with individual countries relative to global norms, the dynamic capacity development approach is to identify the future potential unique to each country. Limited resources are poured into this area to realize that potential rather than scattered across many unrelated programs. Concrete action plans are prepared to make full use of their growth potentials, such as promoting specific industries and regions/areas, and developing road and telecommunication networks based on a time-bound plan.

Then how can the dynamic capacity development approach be complementary to the Western development thinking? To what extent can it be useful for developing countries which are not familiar with the East Asian way?

Development is both a political process and an economic process, and policy formulation is inseparable from political and institutional reforms. "What should be done" (desirability question) should not be equated with "what can be done" (feasibility question). The optimal solution from an economic rationale may not be necessarily implementable in a developing country that faces various political and institutional constraints. Even if growth diagnostics (or the HRV model) identifies key binding constraints to growth for each country, the recommendations will not be useful if they conflict with political reality. This observation applies to the Doing Business approach and the good governance approach as well. Not all feasible policies are desirable and not all desirable policies are feasible. While it is very important to understand the ranking of respective countries compared with international standards and clarify challenges to be addressed, it is also vital to assist developing countries under various constraints in identifying feasible prescriptions and the sequence of actions and formulating and implementing growth strategies.

Under the dynamic capacity development approach, field-orientation and joint work aim at facilitating the joint formulation of goals and policies through interactions with government leaders and policy makers over an extended period. Backed by the understanding of country-specific context from field-based perspectives, these approaches should help establish concrete goals and policy measures that are both desirable ("what should be done") and feasible ("what can be done") for each country.[13] Such approaches should facilitate the self-discovery process of developing countries, while respecting their ownership. This suggests the complementarity between Japanese and Western approaches.

Table 7.1 provides comparison of Japan's growth support approach to those of major Western donors, based on the analyses of the previous sections.

5.2 Examples of Japan's growth support

Although there are many examples, we would like to give attention to two types of Japanese cooperation, which embody the dynamic capacity development approach and other key features of Japan's growth support. The first type is policy dialogue, which is intellectual cooperation between a developing country and an advanced one, held regularly over a few to several years with open and evolving agenda. Policy dialogue differs from technical assistance with narrowly prescribed terms of reference or with standardized policy matrix. If strong ownership and commitment exist on the side of partner countries, it should serve as a useful instrument for helping improving their policy capability through hands-on advice. Japan has conducted policy dialogue with many developing countries in various modalities regarding purpose, scale, participants, duration, and frequency (Table 7.2). It usually starts with a national leader of a developing country

Table 7.1 Comparison of donor approaches to growth support

	Approaches to growth support	*Remarks*
World Bank	• Doing Business approach: ranking countries by using international standards as benchmarks; supporting the overall improvement of investment climates (WDR05) • Good Governance approach: supporting the overall improvement of institutional capacity without focus • Two-part strategy: matching the state's role to its capability (WDR97); skeptical about the possibility of developing countries with low levels of institutional capacity implementing industrial policies	Framework approach; leading global development debates
UK	• Doing Business approach and Good Governance approach • Strong interest in designing the financial architecture to mobilize resources for infrastructure development and promote public-private partnerships; provide infrastructure funding as part of budget support	Framework approach; excels in strategic planning and dissemination
US	• Doing Business approach and Good Governance approach (although may provide support for value chain development of priority industries specified by partner governments)	Framework approach
Germany	• Neo-structuralist approach: combining the Doing Business approach with ingredients approach for industrial capability building; emphasize the need to pay attention to industrial structures and human resources which support the market economy • Multi-level approach: combining macro-level, meso-level, and micro-level measures • Support infrastructure development primarily through projects; emphasize the interest of individual firms as well as the institutional architecture for public-private partnership	Combination of the framework and ingredients approaches
Japan	• Combine the Doing Business approach with ingredients approach for industrial capability building; emphasize the need to pay attention to industrial structures and human resources which support the market economy • Take pragmatic approach to help formulate prescription, based on goal-orientation, field-orientation, joint work, and dynamic capacity development • Emphasize the specific context of infrastructure development projects, such as geographical location, technical design, and links with regional development	Ingredient approach

Source: Elaborated by the author.

Note: Analysis of this table is largely drawn from the literature review. Since various initiatives are implemented on the ground in response to the needs of partner countries, it is possible that in reality, differences among donors may not be as clear-cut as shown in the table.

Table 7.2 Japan: policy dialogue with developing countries (selected list)

Country	*Period*	*Head/key players*	*Purpose and content*
Argentina	1985–1987 1994–1996 (follow up)	Saburo Okita (former foreign minister) etc., JICA	Comprehensive study on agriculture and livestock farming, industry, transport, and export promotion
Thailand	1999	Shiro Mizutani (former MITI official), JICA	Study on the master plan for SME promotion policy
Vietnam	1995–2001	Shigeru Ishikawa (professor) etc., JICA	Large-scale joint study on macroeconomy, industry, agriculture, enterprise reform, crisis management, etc.
Indonesia	2000	Shujiro Urata (professor), JICA	Policy recommendation for SME promotion
Myanmar	1999–2002	Konosuke Odaka (professor) etc., JICA	Study on agriculture, rural development, industry, trade, finance, ITC, etc.
Mongolia	1998–2001	Hiroshi Ueno and Hideo Hashimoto (ex-World Bank economist and professor), JICA	Study on the support for economic transition and development
Indonesia	2002–2004	Takashi Shiraishi and Shinji Asanuma (professors) and six professors, JICA	Policy support for macroeconomic management, financial sector reform, SME promotion, private investment promotion, democratization, decentralization, and human resource development
Laos	2000–2005	Yonosuke Hara (professor) etc., JICA	Study on macroeconomy, finance, state enterprise, FDI, and poverty reduction, etc.
Vietnam	2003–current	Japanese embassy, JICA, JETRO, JBIC	Bilateral joint initiative to improve business environment and strengthen competitiveness through two-year monitoring cycle of action plans
Ethiopia	2009	GRIPS Development Forum (Kenichi Ohno, Izumi Ohno), Japanese embassy, JICA	Kaizen, basic metals and engineering, productivity movement, policy procedure and organization, etc.

Source: Author's research.

Abbreviations: MITI (Ministry of International Trade and Industry), SME (small and medium enterprises), JICA (Japan International Cooperation Agency), JETRO (Japan External Trade Organization), JBIC (Japan Bank for International Cooperation), GRIPS (National Graduate Institute for Policy Studies).

Note: This table lists policy dialogues that are large-scale or worthy of special attention. Besides these, Japan offers policy advice through dispatching advisors to heads of state or ministers, expert dispatches, drafting reports on development strategy, training courses and site visits, conferences and seminars, etc. of various scale and duration.

requesting Japan to discuss development strategy generally and/or teach and transfer the experiences of East Asian development. Examples of policy dialogues in Vietnam and Ethiopia are presented below ([1] and [2]).

Western donors and international organizations also conduct policy dialogue, but their topics tend to be less industrial and more towards macroeconomic, legal, social, or governance aspects. When industrial subjects are discussed, they are usually cross-sectoral issues such as ICT, globalization, and enterprise reform rather than sector-specific targeting or planning. Japan's policy dialogue is unique in the sense that it aims directly at strengthening the state's role and capacity in industrialization rather than reducing the scope of government intervention. Korea also offers the Knowledge Sharing Program (KSP) to developing countries, and industrial development is one of the topics supported by KSP (Chapter 10).[14]

The second type is the support to infrastructure development, backed by real-sector concern. A large part of Japanese ODA regularly goes to building large-scale infrastructure, especially in the transport and power sectors. When such infrastructure is built, it is customary that supporting programs that take advantage of that infrastructure or complement it are also provided for effectiveness and synergy. This includes the formulation of master plans for regional or industrial development, operations and maintenance programs, human resource development, safety and environment programs, local SME development, the "one village one product" program, and the installation of one-stop border posts. In other words, the support to infrastructure development is backed by real-sector concern.

Unlike DFID, Japanese aid agencies tend to work on concrete issues, such as the type and location of infrastructure to be built, industrial potential of the targeted areas and measures for attracting industries, and technological design of individual infrastructure projects. Although projects are implemented by consultants and contractors, aid officials closely follow the project cycle, including the planning of infrastructure projects, the formulation of master plans and feasibility studies, the decision on project funding, and supervision and implementation monitoring. In this connection, due attention is paid to the geographical aspects of infrastructure development, such as development corridors (regional development linked with core infrastructure), the combination of infrastructure and FDI attraction (industrial parks, special economic zones, etc.). Examples of Thailand's Eastern Seaboard Development and El Salvador's port development combined with regional development are shown below ([3] and [4]).

(1) Vietnam—joint policy formulation through open-ended dialogues ("Ishikawa Project")

The "Ishikawa" Project, formally *The Study on the Economic Development Policy in the Transition toward a Market-Oriented Economy in the Socialist*

Republic of Vietnam, was the first large-scale bilateral research project for Vietnam after diplomatic relations with the West were restored in the early 1990s. This project was supported by JICA, as part of Japan's bilateral technical cooperation and conducted by a research team led by Shigeru Ishikawa, emeritus professor at Hitotsubashi University, a renowned development economist with deep knowledge of China's economic transformation. The project started in April 1995 based on an agreement by top political leaders of Japan and Vietnam and was implemented over 6 years in 3.5 phases. A key feature of the Ishikawa Project was joint work based on a "think together" approach with the Vietnamese experts and policy makers. The Japanese and Vietnamese experts formed a joint research team and analyzed the problems associated with Vietnam's transition to a market economy, often involving the experts of international organizations. Furthermore, Prof. Ishikawa built a trustful relationship with former Communist Party General Secretary Do Muoi. There were no policy conditionalities or policy matrices, and Prof. Ishikawa attached high importance to frank exchange of opinions with the spirit of mutual respect. Based on the shared understanding of the problems, the Japanese experts provided recommendations for the formulation of sustainable economic development plans by the Vietnamese government (Kobayashi, 2008). Priority topics were agriculture and rural development, industrial and trade policies, fiscal and financial policies, and state-owned enterprise reforms, which suggest strong interest in the real sector.

The Ishikawa Project provided a model for JICA's subsequent intellectual cooperation, such as the Indonesia Economic Policy Support Project (2002–2004) and the Laos Economic Policy Support Project (2000–2005). Similar intellectual support, though smaller in scale, has also been implemented in recent years in Africa, such as Japan–Ethiopia industrial policy dialogue (see [2]).

(2) Ethiopia—joint policy formulation, accompanied by concrete industrial projects (Japan–Ethiopia industrial policy dialogue)

The Japan–Ethiopia industrial policy dialogue is an intellectual cooperation project, launched upon a request from H.E. the late Mr. Meles Zenawi, former Prime Minister of Ethiopia, who had strong interest in the experiences of East Asian industrial development. What triggered Prime Minister Meles' request was a report compiled by the GRIPS Development Forum (2008a), which highlights JICA's *kaizen* (quality improvement guidance at the production floor)[15] project in Tunisia in comparison with EU assistance for firms to acquire ISO certificate (Chapter 8 of this volume). Both projects aimed at strengthening Tunisia's industrial competitiveness through quality improvement. But, the JICA project took an order-made approach, providing firm-specific diagnosis and guidance to 28 model firms, while the EU project took a ready-made approach based on international standards like ISO. Subsequently, he requested the Japanese government to provide intellectual support to Ethiopia's industrial development strategy from East Asian perspectives, through policy dialogue and technical cooperation of *kaizen* project. A two-year project for industrial policy dialogue (2009–2011) started, supported by JICA, where a group of researchers of the National Graduate Institute for Policy Studies (GRIPS) have been engaged in policy dialogue on industrial development, and a team of Japanese consultants has been working on *kaizen* project (JICA and GRIPS, 2011). The JICA–GRIPS team visited Ethiopia every three months and conducted industrial policy dialogue, mainly through 3 channels: (i) direct dialogues with Prime Minister; (ii) meetings and discussions with senior policy makers such as the Senior Economic Advisor to the Prime Minister, and the Ministers and the State Ministers of the relevant ministries (High Level Forum); and (iii) meetings, discussions, and collaborative work with policy makers and practitioners in charge. The JICA–GRIPS team also met with various stakeholders including business, academia, and donor agencies.

Ethiopia stands out from other countries in Africa because its Industrial Development Strategy (formulated in 2002) has clear policy orientation and the government has been taking promotional measures for selective, priority industries. The Ethiopian government is keen to benefit from the past experiences of East Asian industrial development, not only the content, but also "specific" and "action-oriented" formulation of policies and its organizational arrangements. Through the joint work and open dialogue process, this bilateral industrial policy dialogue aims to nurture mutual understanding on the progress and bottlenecks of Ethiopian industrial development, as well as exploration of a future course of action to be taken. Topics discussed during 2009–2011 included the next five-year development plan (especially, industrial development), the methods for drafting industrial master plans and action plans, organizational aspects of industrial policy formulation, basic metal and engineering industries, and the concept and practice of *kaizen*, and so on. Concrete industrial projects and studies were proposed and agreed upon as a result of policy dialogue at high levels. Such process has facilitated the identification of JICA's prospective projects in Ethiopia, as well.

(3) Thailand—regional development around core infrastructure (Eastern Seaboard Development)

In East Asia, there are many core infrastructure projects accompanied by satellite programs, supported by Japanese ODA. A typical example is the Eastern Seaboard Development Plan in Thailand, to which Japan provided concentrated assistance during the 1980s, including ODA loans for 16 major infrastructure projects and related technical cooperation (ports, roads, railways, water resources, environment, industrial zones, and investment promotion, etc.). The Eastern Seaboard Development Plan is Thailand's first forward-looking, strategic initiative aimed to fuel a robust economic takeoff. It was regarded as the highest priority at the time of the Fifth (1982–1986) and Sixth (1987–1991) National Economic and Social Development Plans. Two major objectives of development in this area were to: (i) strengthen international competitiveness by building an industrial base suitable for accelerating industrialization; and (ii) systematically expand economic activities out towards regional areas while generating employment outside of Bangkok so as to mitigate concentration levels, and other strains of urbanization, in Bangkok. This represents a goal-oriented approach, such as promoting specific regions/areas, developing infrastructure networks based on a time-bound plan. The results of impact evaluation confirm that the Eastern Seaboard Development in Thailand contributed to attracting private investment and industrial development (JBIC, 2001).

Other examples in Asia include: the development of the Hanoi–Haiphong transport corridor along National Highway No.5 in conjunction with Haiphong Port improvement, FDI attraction, and traffic safety programs in Vietnam; and the development of Sihanoukville Port and power and telecommunication networks combined with the construction of a special economic zone and FDI marketing in Cambodia. With concrete goals and action plans, such approach has effectively contributed to dynamic capacity development of respective countries. At even a larger scale, the development of the Greater Mekong Region encompassing six countries (China, Thailand, Vietnam, Laos, Cambodia, and Myanmar) is promoted under the leadership of Japan and the Asian Development Bank where the East–West and the North–South corridors serve as the core infrastructure.

(4) El Salvador—regional development with core infrastructure, combined with policy dialogue[16]

This is a non-Asian example of regional development with core infrastructure, which has been implemented through policy dialogue. It took a goal-oriented approach, boosting the country's strength rather than working generally on its weaknesses.

In El Salvador, Japan supports the development of La Union Port situated in the Eastern Region of this small country. By international standards, the quality of El Salvador's transport infrastructure—seaports, airports, and the road network—is above average and even considered the best in Central America. For this reason, infrastructure was not identified as the "binding constraint" in the growth diagnostics conducted for this country by Hausmann and Rodrik (2003). However, the government of El Salvador hoped to upgrade the existing port to augment the country's position as the regional transport hub. This could also contribute to the development of the Eastern Region which was the poorest region of this country. The Japanese government assisted the drafting of the Master Plan for the Development of the Eastern Region (*The Study on Economic Development, focusing on the Eastern Region, of the Republic of El Salvador*), provided an ODA loan to expand La Union Port as the core infrastructure, and aligned other aid programs to it. For example, an old bridge on the Honduras border was rebuilt, digital map technology was introduced, and the development planning of La Union City was conducted. In addition, Japan provided training for port workers and implemented social sector programs such as education, clean water, and rural electrification as well as productive sector programs for SME promotion, aquaculture, agriculture, irrigation, and livestock.

It is interesting to note that the US, through MCC, also supports regional development around core infrastructure development in El Salvador and that there are differences between JICA and MCC approaches. For example, the MCC selects countries that satisfy 17 eligibility criteria in the areas of governance, politics, economics, and human development for its cooperation and then concludes compacts with the selected countries. In the case of El Salvador, a 5-year compact was agreed which consists of various projects. The MCC implements projects through an implementation unit independent of existing government organizations of the partner country. Japan has implemented various projects which are agreed through policy dialogues with the Salvadoran government. Although each project has a fixed period of cooperation, there is long-term commitment to bilateral cooperation in the eastern region. These projects are undertaken by the government and counterpart organizations of the partner country, with Japanese experts working side by side to support their initiatives.

6 Conclusion

There exist notable differences among donors in their approaches and perspectives regarding growth support. Japan (and East Asia) emphasizes the real sector, such as individual industries and industrial structures, and pays attention to "ingredients" of the economy. In contrast, Western donors and organizations show great interest in overall policy and regulatory "frameworks." Such differences can be observed among Doing Business, good governance, growth diagnostics approaches, and what we call the dynamic capacity development approach. The dynamic capacity development approach, practiced by Japan and East Asia, is characterized by real-sector pragmatism, goal orientation, and aspiration for building the country's unique strength rather than improving governance scores generally vis-à-vis the global standard. By focusing on hands-on endeavor to achieve concrete objectives, this approach is sharply distinct from the dominant development thinking of Western donors which emphasize an early adoption of policies and institutions that copy international best practices. Nevertheless, it should be noted that such differences should not be strictly applied because some donors (e.g., Germany) have similar real-sector, or ingredient, approaches and emphasize capacity development.

The Western approach and the Japanese approach are complementary and not incompatible with each other. It is obvious that both general frameworks and concrete ingredients are necessary for successful development. Given the fact that the donors with framework orientation excel in communicating their thoughts and methodology and are leading global development debates, there exists ample scope and need for Japan to provide the information on the characteristics of its growth support. This is also desirable in light of supplying balanced information to developing countries.

Notes

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1 *The Official Development Assistance (ODA) White Paper 2003* (by the Ministry of Foreign Affairs) emphasizes the importance of growth and infrastructure in reducing poverty, and presents Japan's arguments at the DAC Network on Poverty Reduction with special reference to a study on the contribution of large-scale infrastructure to economic growth and poverty reduction in Vietnam (pp. 92–7). *The ODA White Paper 2005* also discusses infrastructure studies undertaken by Japan jointly with international organizations (pp. 18–21).

2 For studies that analyzed JICA's capacity development approach, see *Capacity Development and JICA's Activitie*s (February 2003) and *Capacity Development (CD)* (March 2006). Moreover, the JICA Research Institute is conducting research on capacity development based on case studies.

3 Hausmann and Rodrik (2003) argue that self-discovery includes: (i) the discovery of innovative investment by private corporations; and (ii) the discovery of appropriate support measures for pioneer companies with such entrepreneurship (support not provided to their followers) by governments.

4 For the methodology, see the website of the World Bank (http://www.doingbusiness.org/features/Highlights2010.aspx).

5 *The East Asian Miracle* groups policy alternatives for developing countries into two categories, i.e., (i) policies of getting the basic conditions right; and (ii) selective intervention policies, and recognizes the usefulness of the latter policies based on the experience of Japan, South Korea, and Taiwan. However, it concludes that since a quite high-level governance capacity is required for selective intervention to succeed, developing countries should refrain from the (ii) and focus on the (i) policies in combination with export promotion policies, as South East Asian countries did.

6 See Deverajan and Uy (2009) "Is it worthwhile to support industrial policy?" Section 3 (6) for their presentation at the Workshop on Industrial Policy in

Developing Countries, Bonn (November 18–19, 2009 organized by the German Development Institute).

7 For example, see Grindle's argument about "good enough governance," Khan's argument about "'growth-enhancing' governance capability," or Shimomura's argument about "strategic governance" and "endogenous governance."

8 How the growth diagnostics affected *World Bank 2005* and the subsequent growth studies conducted by the World Bank is described in "Growth Paths: Country Specificity in Practices: Concept Note for Growth Diagnostic Studies" (downloadable from the website of the World Bank at http://siteresources.worldbank.org/INTPREMNET/Resources/489836-1123682017954/GrowthPaths_conceptnote.pdf).

9 The Commission on Growth and Development was a scholarly commission organized by members, including high government officials, researchers, and representatives of private sectors (some of whom were from developing countries). It was established in April 2006 and issued its final report in June 2008 (the World Bank served as its secretariat).

10 This is similar to the concept of M4P ("Making Market Systems Work Better for the Poor") presented by DFID in 2005.

11 The former Bush administration formulated *National Security Strategies* (2002 and 2006) and regarded economic development as an important pillar associated with diplomacy and defense (3Ds: Defense, Diplomacy, and Development). The 2008 economic growth strategy was formulated by USAID in order to reconfirm the importance of economic growth support by the US in its national security strategy. More recently, the Obama administration formulated a new *National Security Strategy* in May 2010, and announced the Presidential Policy Directive of Global Development Policy in September 2010. This Presidential Directive elevates broad-based growth as a top priority because this is the only sustainable way to accelerate development and eradicate poverty.

12 *Creating an Enabling Environment for Private Sector Development in Sub-Saharan Africa* is downloadable from the following website: http://www.businessenvironment.org/dyn/be/docs/160/Altenburg.pdf. From January 2011, GTZ (German Agency for Technical Cooperation) became GIZ (German Agency for International Cooperation), by integrating two other organizations, i.e., InWent (training) and DED (experts dispatch).

13 According to Nonaka and Konno (2003), this is related to the type of knowledge unique to Japan and the East. Knowledge is created in a continuous, self-transcending process through which one freely transcends the boundary of the old self into a new self by acquiring a new context, and between self and other.

14 Korea's KSP has two main pillars of bilateral policy dialogue sessions and construction of policy modules (information kits on particular policy measures). There are two channels of conducting KSP: (i) the Ministry of Strategy and Finance (supported by the Economic Development Cooperation Fund of the Exim-Bank, and the Korean Development Institute) and (ii) Ministry of Foreign Affairs and Trade (supported by the Korean International Cooperation Agency).

15 *Kaizen*, in Japanese management, means "continuous improvement" of productivity and quality without additional cost, in a participatory process and a bottom-up approach.

16 For more detailed case study, please see Hosono (2010).

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8 The quality and productivity improvement project in Tunisia

A comparison of Japanese and EU approaches

Tsuyoshi Kikuchi

1 Introduction

As challenges of development are diverse, aid organizations must properly recognize the need for diversity in methods and approaches in responding to them. Each aid organization has fields, methods, and approaches in which it excels. Equally, each aid organization has areas in which it has little knowledge or experience. Ideally, superior methods and approaches of different aid organizations should be brought together to deal with any development problem of low-income countries. Collective aid efforts based on comparative advantages of donors can produce great synergic effects.

This chapter examines the complementary relationship between Japan and the European Union (EU) using a Japan International Cooperation Agency (JICA) project, "The Study on the Master Plan for Quality and Productivity Improvement in Tunisia,"[1] as an example.

There are three ways by which different aid organizations can work together towards solutions for the same development issues in developing countries:

(i) Unified multilateral assistance conducted jointly by a number of aid organizations through explicit consultations, where each aid organization contributes to the project using the method or approach in which it excels.
(ii) A combination of assistance programs formed through an explicit consultation among aid organizations, with each organization employing the method or approach in which it excels.
(iii) Separate assistance programs where each organization independently mobilizes a method or approach to offer the kind of assistance other aid organizations are not providing.

The case described in this chapter falls under the third category. The EU had been providing assistance to Tunisia for quality improvement in manufacturing as part of its efforts to strengthen the international competitiveness of Tunisian industries. Subsequently, JICA conducted a preliminary study to determine what kind of cooperation was feasible and what Tunisia

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expected of Japan for strengthening international competitiveness. It found that that the EU was helping Tunisian companies to acquire International Standard Organization (ISO) certification to improve the quality of their business management. Although the acquisition of ISO certification installs a quality management system and strengthens document management in the company, it does not automatically lead to improved quality management or production technology. The acquisition of ISO certification simply means that one advantageous condition for international business is now in place. This fact was taken into consideration when the JICA Project Formulation Mission formulated the new project.

Consultations between JICA and Tunisia led to the agreement that JICA would dispatch a consultant team to improve the quality of production management and products for the purpose of enhancing the international competitiveness of Tunisian companies. As the field study of the JICA consultant team progressed, it became clear that the JICA project would positively affect Tunisian companies preparing to acquire ISO certification. Even more, those that had already acquired ISO certification would also benefit as the project would provide additional conditions for the strengthening of international competitiveness through the actual improvement of product quality and productivity. Thus, it was reaffirmed that the JICA project and the EU project in progress were mutually complementary, as had been hoped in the preliminary study. Details of this complementarity will be the main focus of the sections to follow.

2 Outline of the JICA project

2.1 Background

In 1995, Tunisia signed a partnership agreement with the EU which stipulated that tariff barriers with the EU would be abolished by 2008. In the same year, Tunisia introduced Programme de Mise à Niveau (program for upgrading) in anticipation of a future inflow of high quality and inexpensive products from the EU as a result of this agreement. In 2005, recognizing that the active promotion of broad-based productivity improvement and quality management was essential for the strengthening of international competitiveness, the National Quality Project Management Unit (UGPQ) was established under the Ministry of Industry, Energy, and SMEs.

Actually, the UGPQ was established as a temporary organization for implementing the above-mentioned EU aid project. It aimed at providing guidance for Tunisian companies to adopt quality management and productivity improvement approaches with EU guidance. The goals were set to help 600 companies by 2010, and 1,300 companies by the end of the project, to acquire ISO and other internationally recognized standards. However, the UGPQ lacked profound knowledge and experience regarding quality and productivity improvement activities, and its organizational capacity to expand such activities nationwide was not fully developed.

Against this background, the Government of Tunisia requested the Government of Japan to provide assistance for the formulation of a comprehensive master plan containing recommendations for required policies and institutions as well as action plans that would guide the UGPQ to expand quality and productivity improvement activities.

2.2 Objectives

The objectives of the JICA project included survey and analysis, the implementation of a pilot project, and, based on the results of these, the formulation of a master plan prescribing policies, implementation mechanisms, and action plans for quality and productivity improvement. The targeted industries were electrical/electronics and food processing, two sectors that were highly important in Tunisia. During the implementation process of the pilot project, various advisory services were to be provided for selected model companies to improve quality and productivity. At the same time, effectiveness of the quality and productivity improvement manuals compiled in advance would also be examined.

2.3 Content and methodology

This project on the Study on the Master Plan for Quality and Productivity Improvement in Tunisia lasted for two years from August 2006 to July 2008 and had three phases. The main activities and duration of each phase are described below.

PHASE I: A fact-finding survey on private companies focusing on quality and productivity improvement (August to November 2006).
PHASE II: Implementation of a pilot project for quality and productivity improvement (December 2006 to October 2007).
PHASE III: Formulation of a master plan for quality and productivity improvement (October 2007 to July 2008).

In Phase I, the following issues were surveyed from the viewpoint of quality and productivity improvement, and remaining issues were also identified:

(i) present conditions and problems of Tunisian industries in general;
(ii) present conditions and problems of the electrical/electronic and food processing sectors;
(iii) present conditions and problems of institutions and organizations which assist industries and enterprises;
(iv) status of policies, measures, and the legal framework;
(v) assistance by other donors;

In regard to (v) in particular, possibilities of duplication, complementarity, and synergy effects with the JICA project were studied.

In Phase II, a pilot project was implemented. In accordance with the implementation plan which was formulated in advance, criteria for selecting model companies were determined, and 15 producers were selected as model companies from each of the two sectors, electrical/electronic and food processing, with a total of 30 model companies. At the same time, manuals for quality and productivity improvement were drafted for each of the 2 sectors. These were the preparatory stage for the full-scale implementation of the pilot project.

The actual implementation of the pilot project included guidance on quality and productivity improvement technology for the model companies and the use of the prepared manuals. In addition, guidance was also provided for the Tunisian counterparts, by means of On-the-Job Training (OJT), on how to assist companies (i.e., training the trainers). The most important point was the development of quality and productivity improvement methods and approaches that suited the industrial climate and the social and cultural conditions of Tunisia, as well as the reality of Tunisian companies, through adjustments of Japanese technology and production systems. This also means the fostering of local capacity to modify technology introduced from outside to create appropriate technology. The manuals prepared in advance were also modified.

In Phase III, a master plan, which was the final outcome of the project, was drafted. The Government of Tunisia hoped to improve quality and productivity in all industries as well as all regions of the country. For this reason, a master plan for the national dissemination of quality and productivity improvement technology, covering all industrial sectors and regions and including diffusion mechanisms and action plans, was compiled taking into consideration the results of the pilot project conducted over the electrical/electronic and food processing sectors. In this process, as many stakeholders as possible were mobilized in exchanging information and opinions. After that, the JICA consultant team and local counterparts prepared the draft.

This project can be described as a bottom-up approach to aid, as it formulated a master plan by incorporating the results of the fact-finding study and the pilot project conducted at the level of the factory floor.

The project can also be summarized from the viewpoint of the transfer of technology. The transfer of technology consists of three main stages: (i) learning the relevant technology; (ii) modifying the learned technology to suit the reality of a particular region or country; and (iii) spreading the modified technology to the entire region or country. In short, they can be referred to as the "learning stage," the "modifying stage," and the "dissemination stage," respectively. Our project involved the "learning stage," the "modification stage," and a preparatory step for the "dissemination stage" (formulation of a master plan for dissemination). The actual implementation of the "dissemination stage" was left to the Tunisian side.

To repeat, the scope of the JICA project covered the formulation of a master plan and action plans, compilation of manuals, training of human resources and trainers for the implementation of the master plan, and dissemination of its impact. The final stage, dissemination, called for the actual implementation of the master plan, including action plans, as proposed by the JICA project. This required as pre-conditions the government approval of this master plan and subsequent establishment of necessary systems, organizations, and budgetary resources. These preparatory measures would have to be undertaken by the Tunisian side.

The appendix diagram compares the three stages of technology transfer and the three phases of the JICA project under consideration.

2.4 Considerations for the implementation of the JICA project

The following points have been taken into careful consideration for the implementation of the JICA project.

(1) Conformity with development policies and development programs of Tunisia

It is essential for the JICA project to conform to Tunisian development policies, development programs, and industrial policies, and so forth. The JICA project was initiated in August 2006, during the last year of the 10th Five-Year National Socio-economic Development Plan (2002–2006). It had been decided that the project content would conform to the policies indicated by the 10th Five-Year Plan on the grounds that the next Five-Year Plan (2007–2011) had not yet been announced and that a major change of the policies would be unlikely in the near future. The policy goals in the 10th Five-Year Plan included the construction of economic infrastructure, improvement of the financial system, the strengthening of international competitiveness, the improvement of productivity in the private sector, and the narrowing of economic gaps among different regions of the country. Among these, the JICA project would directly contribute to the strengthening of international competitiveness and the improvement of productivity in the private sector. It would also have a positive effect on the narrowing of regional economic gaps as companies located in remote areas were also selected as model companies for the pilot project.

Since 1995, the Government of Tunisia had been implementing the Mise à Niveau program as one of the key industrial policies. This program aimed at strengthening the international competitiveness of Tunisian companies through quality improvement. The objectives of the JICA project were in line with this. There was no doubt that it would further promote international competitiveness, which was one of Tunisia's most important policy issues.

(2) Conformity with Japan's aid policy

Japan's aid policy toward Tunisia was specified in the Country Assistance Program for Tunisia of the Japanese Ministry of Foreign Affairs. It listed the leveling-up of industry, the development and management of water resources, and environment as three major areas of policy priority. As for assistance toward the leveling up of industry, it was stated that, while overall improvement of international competitiveness was desirable, Japanese support should focus on economic infrastructure with an emphasis on in the transportation sector and the information and communication sector; production and quality management; productivity improvement; fostering of SMEs; development of technological capability; and vocational training, taking into consideration the sectors and areas in which Japan exceled.[2] The JICA project could be classified broadly as assistance to raise the level of industry in general, with specific contributions to production and quality management, productivity improvement, and fostering of SMEs, as stipulated in the Country Assistance Program.

(3) Respect for country ownership

The success of intended technology transfer depends critically on the capacity and willingness of project partners on the Tunisian side. These are the key determinants of technology absorption during the implementation and the sustainability of the project after its completion. Accordingly, the JICA project adopted the principle of encouraging the willingness and involvement of the Tunisian partners, respecting their ownership, and reducing the role of JICA consultants as the project proceeded.

(4) Utilization of Japanese know-how in quality and productivity improvement

The ODA Charter of Japan calls for the "utilization of Japan's experience and expertise." Japan has developed a number of methods and approaches for improving the quality and productivity of industry. For example, the Five S's (5S), Quality Control (QC) circle, Total Quality Control and Total Quality Management (TQC/TQM), kaizen, and Toyota's production system (just-in-time system and *kanban* system) have attracted much attention not only in Western countries but also in developing countries. In Tunisia, knowledge of these production techniques is shared widely by business people and academics of business administration.[3] However, their lack of practical guidance means that they are unable to fully apply such knowledge to actual production processes. Japanese cooperation is expected to fill this gap, and such expectation was the background for initiating the present JICA project as explained above.

Methods and approaches developed in Japan have their roots in the culture and industrial climate of Japan, as well as in the way of thinking and the value system of the Japanese people. It is important not to force them blindly on Tunisian government officials and managers of the model companies. In other words, the culture of Tunisia, as well as the way of thinking and sense of values of the Tunisian people, must be respected.

(5) *Avoidance of aid duplication and emphasis on complementarity and the synergy effect*

Frequent consultation and information exchange should be arranged with other donors operating in the same field (industrial promotion and private sector development) in Tunisia to not only avoid duplication but also generate positive complementarity and synergy effects.

3 Comparison with the EU project

Our survey of industry-related projects of other donors in Tunisia found that the Industrial Modernization Project (PMI) assisted by the EU had the closest objectives to those of the JICA project. The two projects are compared below.

Both projects supported the Mise à Niveau program implemented by the Government of Tunisia, with the aim of contributing to the strengthening of international competitiveness of Tunisian industries. The JICA project formulated a master plan for quality and productivity improvement, while the EU project promoted the "industrial modernization program." The main activities of the JICA project were (i) implementation of a pilot project; (ii) compilation of manuals; and (iii) formulation of a master plan. For the EU project, activities include (i) assistance for business creation; (ii) assistance for quality improvement; and (iii) business guidance.

The EU's assistance for quality improvement specifically meant assisting Tunisian companies to acquire ISO certification. Meanwhile, the JICA project envisaged improvement of quality and productivity on the factory floor. The EU project transferred internationally uniform standards applicable for all companies in areas such as business management and document preparation. In contrast, the JICA project adopted different techniques and approaches for different problems encountered by individual companies. A senior manager of the EU project described this difference as "prêt-à-porter" (or ready-made) versus "just-fit" (or order-made). Another difference between the two projects was that the majority of JICA consultants had experience in directing production processes while this was not the case with the consultants of the EU project.[4] A Tunisian official who was well acquainted with the JICA project noted that such differences between projects were highly welcome as the source of a positive synergy effect.[5] Table 8.1 summarizes these differences.

At the time of the commencement of the pilot project, the number of model companies that had already acquired ISO certification was 17 out of 30. Eight companies were in the process of acquiring such certification or hoping to acquire it in the near future. Five companies had no intention of acquiring ISO certification.

Even among model companies with ISO certification, many had the problem of disorderly placement of raw materials, intermediate inputs and finished products, as well as an extremely inefficient layout of the factory floor.

Table 8.1 Comparison between the JICA project and the EU project

	JICA project	*EU project*
National program to be aligned	Programme de Mise à Niveau (1995)	Programme de Mise à Niveau (1995)
Overall goal	Strengthening international competitiveness of Tunisian industries	Strengthening international competitiveness of Tunisian industries
Immediate purpose of project	Formulation of a master plan for quality and productivity improvement	Implementation of Industrial Modernization Program (PMI)
Main activities	1. Implementation of quality and productivity improvement of pilot project (guidance for model companies) 2. Compilation of dissemination manuals 3. Formulation of a master plan (including action plans and dissemination mechanisms)	1. Assistance for business creation 2. Assistance for quality improvement 3. Business guidance (The text in the next two items refer to the second activity only)
Nature of assistance in quality improvement	Quality and production improvement on the factory floors of model companies (including training of counterparts)	Assisting acquisition of ISO and other international certifications
Characteristics of assistance in quality improvement	1. Different approach for each company 2. Order-made 3. Instructors have practical experience in production 4. While ISO certification is not the main purpose, the project can prepare conditions for obtaining ISO and contribute to actual improvement after ISO certification 5. Bottom-up approach from factory-level results at model companies to master plan drafting	1. Common approach for all companies (applying international standards) 2. Ready-made 3. Instructors do not need practical experience in production 4. Installation of quality and document management systems may not automatically improve the quality of production management and production technology 5. Top-down approach based on international standard like ISO

With the implementation of the pilot project, quality and productivity at such factories improved through the introduction of the 5S and kaizen for plant layout. Other model companies newly acquired ISO certification as a result of positive assessment of guidance received under the JICA project. These experiences at several model companies clearly proved complementarity between assistance for the acquisition of ISO certification under the EU project and assistance for production floor improvement under the JICA project.

4 Feasibility of the transfer of Japanese technology

Even if a number of aid organizations try to formulate projects with the intention of complementarity, it is not certain whether the recipient country will accept the particular sectors which these aid organizations choose or the methods and approaches which they mobilize. While the JICA project in question was not formulated with an explicit consultation with other donors such as the EU, JICA still hoped for complementarity with other donors operating in Tunisia. For Japanese consultants employed by JICA, however, the greatest concern at the initial stages of this project was whether or not the quality and productivity improvement techniques and approaches developed in Japan were suitable for and transferable to Tunisia, a country with culture, industrial climate, way of thinking, and sense of values which are very different from those of Japan.

Fortunately, with the progress of the pilot project, it became clear that Japanese techniques and approaches for quality and productivity improvement were acceptable to Tunisian model companies selected for the pilot project to a greater degree than originally anticipated. Let me cite some concrete examples.

First, the 5S technique,[6] which is supposed to be uniquely Japanese, was accepted by a large number of model companies and produced positive outcomes. One model company went so far as to produce a 5S manual in Arabic for its employees after hearing about the 5S from JICA consultants.

Second, another model company installed suggestion boxes in different locations in the plant, encouraging employees to submit comments and opinions. By so doing the management hoped to receive more ideas from them. This is one example of the bottom-up approach for business management stimulated by the pilot project.

Third, one model company had a training program of multi-skilled workers even before the initiation of the JICA project. The intention of this training, however, was to ensure that one worker could quickly replace another if the latter was absent or went into retirement, rather than improving quality and productivity. Nevertheless, the existence of such practice pointed to the possibility of workers who could operate more than one machine and supervise multiple processes in the future. Emphasis on multi-skilled workers is a distinct feature of the Toyota production system in particular and the production method of Japanese manufacturing companies in general.[7]

Fourth, at many of the model companies, application of kaizen to the plant layout quickly yielded positive results. The reshuffling of existing equipment can improve quality and productivity without spending much money. This is another example of how Japan can teach good practice. Among 15 model companies in the electrical/electronic sector, more than half introduced this approach without difficulty, achieving both quality and productivity improvement. One company reduced the defect rate from 20 percent to 3 percent even before completing the kaizen process. Two companies raised productivity by more than 50 percent.

Fifth, one model company producing electrical parts organized QC circles with a high hope of improving product quality. The QC circle is a mechanism where factory or shop workers form small groups to continuously improve and manage quality, whether it is the quality of a product, service, or a task (Japan Industrial Management Association, 2005). Since such bottom-up activities are originally developed by Japanese companies, it was not certain at the beginning of the JICA project whether they would be accepted by Tunisian companies, which were more used to a top-down approach to business management. Although this model company did not show tangible results by the end of the pilot project period, the company management became fully aware of the importance of QC circles and the entire company began to make effort to improve quality.

While it is too early to conclude, from a limited number of observations, that Japanese techniques and approaches are generally acceptable to people with a different culture and sense of values, it can at least be said that there is a possibility of such transfer under certain conditions.

This supposition is supported by the facts that overseas plants of Japanese companies often use Japanese production systems and that there have been cases of JICA projects that aimed to transfer the basic components of Japanese production systems to developing countries. Below, two cases are examined more closely; one regarding a private company, Toyota, and the other involving an ODA project implemented in Singapore.

The Toyota production system can be described as the most representative Japanese production system. Let Taiichi Ohno (1912–1990), the founder of this system, explain it in his own words (Kadota, 2006, p. vii):

> The technique we call the Toyota production system is the result of our endeavours to catch up with the automobile industry in advanced Western countries in post-war Japan when there was no fund or equipment. The most important goals for us were productivity improvement and cost reduction. To achieve these goals, we emphasised the idea of eliminating all kinds of wasteful movements in the plant. Our approach was to discover all causes of various types of muda (waste) in production activities one by one and to establish solutions through the trial and error process. Such techniques and ideas as kanban (index cards), heijunka (production smoothing) and jidoka (automation with human intelligence) were developed as a means of just-in-time manufacturing through trial and error on the factory floor. In short, the Toyota production system originates from practical work at Toyota's plants and is strongly characterised by its emphasis on practical effects, practical work and practice rather than theoretical analysis.

Is the Toyota production system acceptable to countries other than Japan? Ohno continues:

> We do have reservations regarding whether or not just-in-time manufacturing can be applied to foreign countries where the business climate, labour-management relations and other social systems differ from those in Japan. However, it is our firm belief that the ultimate goals of companies and their employees differ little from country to country.
>
> (Kadota, 2006 p. viii)

Thus his position was mixed as to the universal applicability of the Toyota production system. It has been 17 years since Ohno passed away, and the reality today is that this system is employed at Toyota plants worldwide, even though some modifications have been necessary in some countries.

Toyota's manufacturing plants around the world aim at the production of automobiles of globally uniform quality.[8] For this reason, the company invites the employees of plants abroad to Japan for training while dispatching an elite team to each overseas plant to ensure the application of the Toyota production system through intensive education and training. With the expansion of production, training teams in overseas plants where the Toyota production system has been firmly established are now dispatched to other countries in view of the limited availability of elite teams at the headquarters.[9]

The following incident, narrated by Takahiro Fujimoto of Tokyo University, shows how foreign workers were prepared for the Toyota production system. In 1983, Toyota founded New United Motor Manufacturing Inc. (NUMMI) in Fremont, California as a joint venture with General Motors.

> Toyota sent newly recruited employees at NUMMI to Takaoka Plant in Japan for training to facilitate their understanding of not only Toyota's history and corporate management principles but also the basic ideas of production, QC activities and teamwork concepts, prior to the introduction of the Toyota production system on the factory floor. Instead of North America, this training took place at a site where the Toyota production system was practiced on a daily basis. The employees of Takaoka Plant warmly welcomed their American colleagues from NUMMI and taught them the basics of the Toyota production system through practice. This training took place from June 1984 to February 1985, and as many as 257 NUMMI employees went through it. NUMMI subsequently became a model company for Japan-US joint ventures and Toyota gained confidence that its own production system had *universal applicability*. Toyota has extended this experience to many other countries to sustain its prosperous business.
>
> (Fujimoto, 2007, pp. 530–31. Italics mine)

Needless to say, Toyota does not intend to introduce its unique production system without alteration to its overseas plants at any cost, nor does it believe that such unchanged replication is possible. Toyota's Guiding Principles clearly indicate this. One principle says that the company shall "respect the culture and customs of every nation and contribute to economic and social development through corporate activities in the communities." This pledge was originally made in January 1992 and revised in July 1997. Toyota has consistently practiced it (Mito, 2003).

Let us now look at another case involving an ODA project, "Productivity Improvement Project in Singapore," which transferred Japanese productivity improvement technologies and approaches. From 1983, JICA provided assistance to Singapore under a similar theme to that of the current JICA project in Tunisia. While the project was implemented for a period of as long as seven years, the first two years were spent in ironing out the two countries' different approaches to aid, and finalizing its direction, in view of the fact that this was the first JICA project of this type.[10] Adjustments were necessary because (i) the Japanese team had at first attempted to transfer Japanese productivity improvement technology and approaches without modification, despite the fact that Singapore, although a fellow Asian country, was different from Japan in terms of culture, beliefs, and the way of thinking, and (ii) there was a communication gap between Japanese experts and their counterparts. Both sides subsequently regretted what had happened and held a series of meetings to mend broken relationships and restore mutual trust.

In the end, the project was successfully implemented. The original Japanese techniques and approaches were modified to respect the social background and the way of thinking of the Singaporean counterparts so they would be accepted by the latter. Through this experience, it was also verified that the basic components of Japanese techniques and approaches were transferable to a foreign country. Table 8.2 compares business approaches in Japan and Singapore as conceived by a former team leader of the JICA project in Singapore. His observations are also applicable, with few changes, to the present case of Tunisia. Tunisians and Singaporeans share many common characteristics. For example, they are both result-oriented and seek quick results. They also prefer the top-down approach to decision-making and fixed work assignments with little flexibility.

5 Conclusions

Japan has rich experience in industrial promotion. On the factory floor, there are many production management techniques and approaches that have been developed in Japan and attract much attention from the rest of the world. Particularly prominent are quality improvement and productivity improvement techniques and approaches as described in this chapter. Although most of them have emerged from Japan's culture and industrial climate, as well as the way of thinking and sense of values of the Japanese people, it has been shown in many cases that a large part of them, or at least their basic components, can be applied and transferred to foreign soil with

Table 8.2 Differences between Japanese and Singaporean business management

	Japan	*Singapore*
Result- vs. process-oriented	Process-oriented: – Results are obtained from processes and efforts – Try first, results come later – Appreciation of efforts made	Result-oriented: – Results are the first priority – seeking a system which appears to lead to good results – Processes and efforts are not appreciated unless results are achieved
Decision-making	Bottom-up: – Decisions come from middle level – Everyone wants to participate in decision-making to a certain extent	Top-down: – Decisions come from the top – Leader-follower relationship – Commitment is important
Work assignment	Flexible: – Broad and unclear job description – Group responsibility – Assignment adjusted to ability – Multi-functional assignment	Fixed: – Duties and responsibilities are clearly defined in job description – Individual responsibility – Fulfillment of job requirements – Single job assignment
Planning function	Planning and operational functions shared even at the operator level	Clear distinction between the planning function and the operational function

Source: Fukuda (2007).

a different culture and sense of values. Toyota even has confidence that its production system is universally applicable.

In terms of experience in industrial promotion and technology that supports it, Japan has the upper hand over other donor countries. At the same time, there are sectors and technologies where Japan is less experienced. The combination of comparative advantages of individual aid organizations, in terms of sectors, techniques, and approaches, is desirable and should produce complementarity and the synergy effect in solving specific development problems of developing countries. In this way, available resources of the donor community can be effectively utilized and shared.

While Japan boasts many techniques and approaches that can be used on the factory floor, former suzerain countries have rich experience and information that is relevant to the creation of good environment for industrial promotion such as the development of legal, taxation, and accounting systems. This is because such systems which were installed during the colonial rule often remain in former colonies. In view of this reality, complementary cooperation is conceivable where former suzerain countries are in charge of developing the soft infrastructure such as legal, taxation, and accounting systems, while Japan is responsible for production management and guidance on the factory floor.

There are no doubt ways for donor organizations from different countries to contribute their specific strengths to develop approaches towards finding solutions. In Japan, business management is primarily bottom-up, while that in Europe and the US is top-down. As far as in-house kaizen activities are concerned, the Japanese approach is that of steady implementation on a daily basis even if the progress is small, while European and American companies excel in the break-through approach. Liker (2004) remarks that "because Western firms tend to focus on break-through innovation and are weak in terms of continual small improvements, this has been the focus of the teaching of kaizen to Western firms" (Liker, 2004, p. 26). Also, Dertouzos et al. (1989) note that

> from the long-term perspective, technological progress is based on the two engines of gradual improvement and sudden breakthroughs. To strike an appropriate balance between the two poses a constant challenge. Lewis Branscomb points out that Japanese companies have been combining the two approaches fairly efficiently. Both approaches have their own strengths and weaknesses, and the establishment of a team consisting of people who excel in different fields will achieve the sought-after complementary relationship.

In this chapter, a Tunisian case was discussed to show the possibility of complementarity in development effort involving multiple aid organizations. Such complementarity should be further considered in future studies. To produce complementarity and synergy effects, key points that must be identified include: (i) the forms of aid provided by donor countries and organizations; (ii) sectors and approaches where aid organizations enjoy comparative advantages; (iii) existing systems and structures of aid recipients (governments or counterpart organizations) which can accept and adjust foreign aid; and (iv) the mechanism for involving local consultants who are active recipients of technology and skills and potent instruments for their dissemination.

As stated at the outset, problems faced by developing countries are becoming increasingly diverse and complicated. Research into the issues mentioned above is essential not only for improving aid quality and outcomes but also for the optimal distribution of aid resources. The rapid progress of globalization and market liberalization, which have a great impact on developing countries, makes it even more urgent to undertake such studies.

Appendix

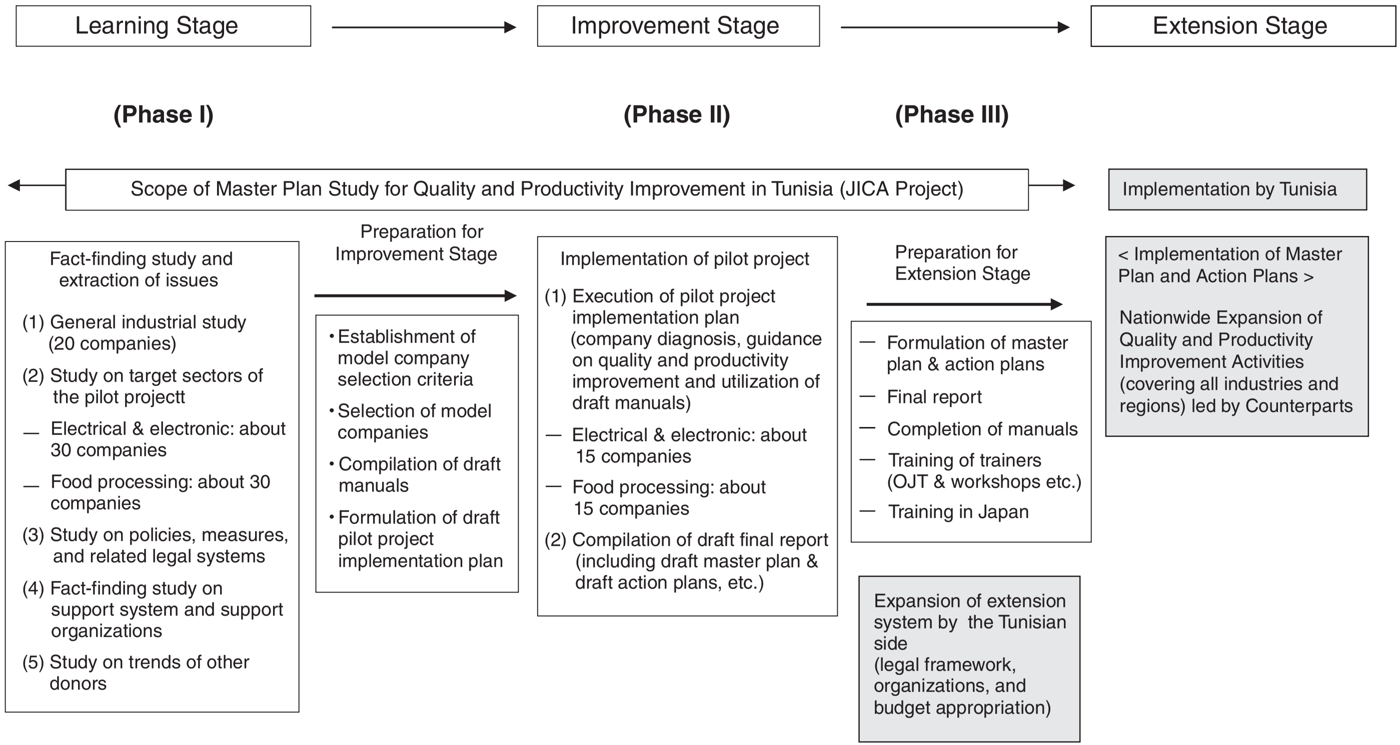

Figure 8.A Three stages, content, and method of transfer of technology in the JICA project

Note: Works in white boxes are carried out under the JICA project, while works in gray boxes are to be carried out under the Tunisian initiative.

Notes

1 This was a two-year project started in August 2006, which was in progress at the time of initial writing of this chapter. Some of the information in this chapter is unpublished and quoted here with the permission of JICA.
2 See the website of the Ministry of Foreign Affairs (www.mofa.go.jp/mofaj/gaiko/oda/index.html).
3 A master's degree program in the Faculty of Business Administration of the University of Tunis offers a course on Total Quality Management.
4 One of the JICA consultants used to be a general director of a factory in the Asian region with long experience in guiding local staff toward quality and productivity improvement. The presence of such a person allows transmission of experience and knowledge from one developing country to another (South–South cooperation).
5 Observation by an official of the Ministry of Industry, Energy, and SMEs at the time of formulation of the JICA project.
6 The 5S technique, consisting of *Seiri, Seiton, Seiso, Seiketsu*, and *Shitsuke*, is a very Japanese method for improving quality and productivity on the factory floor. These five slogans can be variously translated. One example is Sort, Set in Order, Shine, Standardize, and Sustain, which maintains the initial letter of S but deviates from the Japanese meaning. A more literal translation would be remove unnecessary things, arrange tools and parts for easy view, keep the work place clean, maintain personal hygiene, and behave with discipline (eds.: see also footnote 7 of Chapter 1).
7 Professor Fujimoto of the University of Tokyo proposes ODA projects for training multi-skilled workers (Fujimoto, 2007). This is an important proposal in light of the fact that Japanese ODA programs for technology transfer have produced mainly single-skill workers in the past. Workers trained only in one skill by vocational or technical schools in developing countries are often unable to find suitable jobs. The training of multi-skilled workers will not only expand the scope of job search but also increase the possibility of such workers establishing new companies of their own.
8 Toyota's overseas manufacturing locations include the US, Canada, France, the UK, Turkey, Thailand, India, Australia, and South Africa.
9 *Toyo Keizai Weekly*, Sep. 22, 2007.
10 Prior to this, JICA had conducted a development study, "Factory Modernization Program in the People's Republic of China," in 1981, two years before the Singapore Project began. The purpose of this study was to prepare a proposal for improvement of production technology in state-owned factories.

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9 Strategic action initiatives for economic development

Trade and investment promotion in Zambia

*Dato' J. Jegathesan and Masayoshi Ono**

1 Introduction

This chapter outlines the technical assistance of the Japan International Cooperation Agency (JICA), which supported economic development in Zambia through the creation of an enabling environment for promoting trade and investment. This technical assistance, called the Strategic Action Initiative for Economic Development (SAIED) Programme, or alternatively, the Triangle of Hope (TOH) concept, paid special attention to how best successful development experiences in East Asia (in this case, Malaysia) could be utilised in the present development challenges faced in Africa (in this case, Zambia) under the South–South Cooperation framework. The chapter also endeavours to show a concrete example of how Dato' J. Jegathesan, as a Malaysian expert with close to 30 years' hands-on experience in helping the development of Malaysia, has collaborated with Zambian officials and the private sector in an attempt to help create an ideal investment environment, both administrative and physical, for private sector investment, and, subsequently, to realise country-led trade and investment promotion initiatives through intensive face-to-face dialogues.

For years, many developed nations have been pouring development funds into Africa through outright grants and low-interest loans. Despite the billions of dollars being poured into Africa, however, the continent has yet to achieve any significant economic success, unlike the series of economic miracles among Asian nations. Many African nations that were 'richer' than their Asian counterparts in terms of per capita income when they became independent in the 1950s and 1960s—almost at the same time as some Asian nations did—are now much poorer. Many have even gone backwards in virtually every aspect of national development.

Since the first Tokyo International Conference on African Development (TICAD I) in 1993, the Japanese government has led international discussions on African development by advocating the importance of ownership of Africa and partnership with the international community. As the former

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Japanese Prime Minister, Junichiro Koizumi, announced at the G8 Summit in 2005, Japan's key ODA strategies for Africa under TICAD include 'comprehensive support to promote trade and investment' and 'strengthening of Asia-Africa cooperation to share Asia's experiences'.[1] It is emphasised that Asia's post-WW2 experiences in economic development can be valuable assets for Japan's assistance to African development. For this reason, the Japanese government has adopted an approach to development assistance to Africa to take into account the factors that made development possible in Asia. The Asian success model that created the region's dynamic growth was, and is, seen as a programme where the private sector becomes the engine of growth. This model holds that governments must not engage in business, but should create an economic environment that encourages private sector dynamism.

JICA looked at Malaysia's experience of moving from Least Developed Country (LDC) status to becoming an economic success story and decided to utilise Malaysians' technical expertise and experiences to support economic development in Africa. The organisation approached Dato' J. Jegathesan, the former Deputy Director General of the Malaysian Industrial Development Authority (MIDA), to assist in these efforts. MIDA has been widely acknowledged as having played a central role in the creation of the Malaysian economic miracle.

From the end of November 2004 to early December of that year, the JICA Malaysia Office and the government of Malaysia (specifically, the Economic Planning Unit of the Prime Minister's Office) sent a joint mission to several countries in Africa—Kenya, Zambia, Zimbabwe and South Africa—to study possibilities of new cooperation activities in Africa under the framework of South–South Cooperation.[2] Prior to this joint mission, the JICA Malaysia Office and Dato' J. Jegathesan, as the JICA consultant, held a series of discussions on criteria for selecting countries to create successful models of economic development in Africa. Geo-political characteristics were particularly taken into account, and it was proposed to establish (i) a model for landlocked countries, (ii) a model for nations with a coast and a relatively large population and (iii) a model for island nations.

During the mission to Zambia, the concept of the project was presented to the Minister for Finance and National Planning, Ng'andu Magande. Subsequently, it was welcomed by the President of the Republic of Zambia, Levy Patrick Mwanawasa. During the visit of the President of Zambia to Japan in January 2005, the President formally requested technical assistance for trade and investment promotion from JICA. Consequently, JICA dispatched a mission in March 2005 and agreed to assist the government of Zambia in implementing a series of events for business, trade and investment promotion. During these events, the concept of the Triangle of Hope (or TOH, which will be discussed in Section 3) was presented to various stakeholders in Zambia, including the President. Implementation of the concept in the form of technical assistance through the Strategic Action

Initiative for Economic Development (SAIED) Programme received the President's approval.

Zambia is landlocked with the nearest port over 2,000 km away from the Zambian provinces of Lusaka and Copperbelt. With the country's economy depending heavily on mining and agriculture, it is vulnerable to changes in the international market and natural disasters such as drought. While the improvement in GDP growth rate at an average of 4.8 per cent between 2000 and 2006[3] provided a positive macroeconomic picture, other factors and indicators such as high inflation rates, at an average of 19.5 per cent between 2000 and 2006,[4] and high interest rates, at an average of 38.3 per cent between 2000 and 2005,[5] were constraints to the diversification of economic activities, including the development of value-added industries. JICA's assistance with the technical expertise of Dato' J. Jegathesan, with his experience in Malaysian economic development, aimed at creating a conducive environment to promote and diversify investment and industries.

2 Malaysia's experiences in industrialisation

Malaysia successfully industrialised its economy in the 1970s and 1980s, going from producing mainly raw materials such as rubber, palm oil and tin to concentrating on manufacturing activities. Further transformation is ongoing under the challenges of globalisation. The diversity of its population has been a central issue in Malaysia's development; the nation's population consists of Malays and indigenous minority tribes (Bumiputra) (about 50 per cent), Chinese (about 40 per cent) and Indians (about 10 per cent).

During the British colonial administration, the Indians and Chinese were brought into Malaysia from the late eighteenth century to the nineteenth century from southern India and southern China as rubber plantation workers and tin mine workers. After acquiring its independence in 1957, Malaysia experienced a racial riot in May 1969. Several negative socio-economic factors led to the riot. Critical among these factors were high unemployment rates, identification of economic activities with race and imbalance of wealth distribution among the major races—rich Chinese, middle-class Indians and poor Malays despite Malays being the majority population.

Thus, the reduction and eradication of poverty among all Malaysians and balanced economic wealth creation became the major strategies of the government of Malaysia. Creating and strengthening national unity became an overarching goal of the government.

In order to improve the well-being of its people irrespective of race, the government of Malaysia introduced new policy frameworks and strategies in steps since 1970. These consisted of the New Economic Policy 1970–1990, the National Development Policy 1991–2000 and Vision 2020. The economic policies were also translated into more detail as the Outline Perspective Plans and the five-year cycles of the Malaysia Plan, while specific sectoral plans, such as industrial master plans and national agricultural policies, have also been formulated and periodically revised.

Prior to the introduction of the New Economic Policy, the government's economic policies had been focused on accelerating the growth of the economy through investment in infrastructure and agriculture, without much attention to the equitable creation of jobs and distribution of wealth among all races. Such purely 'growth-oriented' policies risked further dividing Malaysians by race, or between the 'haves' of one race and the 'have nots' of another. Thus, it was of paramount importance that the government take a strong and active role in economic and business activities while working very closely with the private sector to create job opportunities and wealth for all Malaysians.

To make such a role possible, an institutional framework was firmly established within the government machinery with strong leadership of politicians, headed by the Prime Minister, and public service with the central government planning body, especially the Economic Planning Unit (EPU) of the Prime Minister's Office. The EPU was created in 1961, and in the same year, the National Development Planning Committee (NDPC) was established, headed by the Chief Secretary to the Government with heads of ministries as its members, to oversee the formulation and review of all plans prepared by the ministers. The EPU acted as the secretariat. The National Planning Council (NPC) was also established as the highest decision-making body on various public policies. NPC membership was composed of the ministers for key ministries, such as the Ministry of Finance and the Ministry of International Trade and Industries. Such economic policy planning has been carried out in close partnership with the private sector.

The government of Malaysia also adopted the Malaysia Incorporated concept as the core policy in 1983 to provide a framework for mutual cooperation between the public and private sectors. With the growing private sector becoming an integral part of Malaysia's economic success, the government launched the Malaysian Business Council with the Prime Minister as its chairman and its members drawn from the government and the private sector. The council formed several committees to deal with specific issues such as infrastructure, monetary and financial issues, human resources development and, most importantly, trade and investment.

The government learned from its hard experiences in the changing global economic environment. It implemented various policies, undertook development projects and established a comprehensive institutional framework, thus creating a conducive environment for massive inflows of foreign direct investment (FDI) and mobilisation of domestic savings to boost its economy. By 1980, the government had managed to transform the country from a raw material producer to the world's largest producer of electronic semi-conductors and the third-largest exporter of room air-conditioners, with the creation of over 150,000 jobs within these sectors alone. Malaysia experienced rapid economic growth from 1970 to 2000 at an average of 6.6 per cent. The real GDP more than tripled from RM (Malaysian ringgit) 21.4

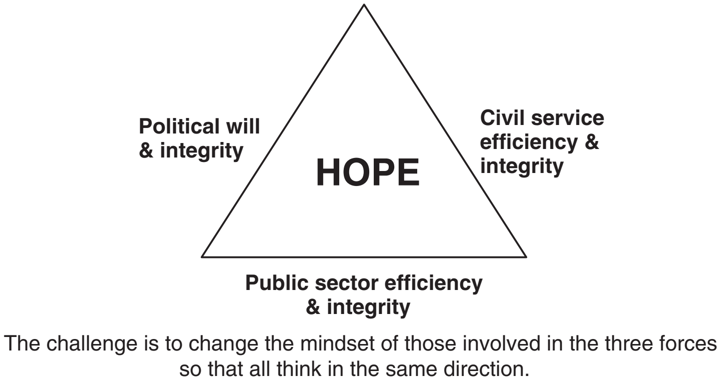

Figure 9.1 Conceptual framework of Triangle of Hope

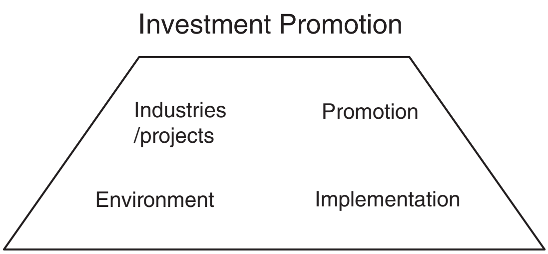

Figure 9.2 The Quadrant Strategy

billion in 1970 to RM 79.1 billion (in 1978 prices) in 1990,[6] and almost tripled again, reaching RM 209.3 billion (in 1987 prices) in 2000.[7] The incidence of poverty declined from 49.3 per cent in 1970 to 7.5 per cent in 1999.

3 The essence of the SAIED Programme and the concept of TOH

The SAIED Programme implemented in Zambia was built on Malaysia's experiences in industrialisation in the 1970s and 1980s, as explained above. The essence of this programme can be represented by the Triangle of Hope (TOH, Figure 9.1) and a Quadrant Strategy (Figure 9.2). The TOH concept was originally a small part of the programme, but the name TOH caught on and has become the commonly used name for the SAIED Programme.

3.1 Triangle of Hope

The TOH is a concept designed to open the eyes of the leadership of developing nations to the three forces that must work together for the economic success of any nation. This concept stresses that the poor of any nation—be it the US, UK, Germany, Japan, Malaysia or Zambia—literally pray to God that these three forces work together, and only if this happens can one expect jobs and wealth to be created. These three forces are (i) political will and integrity, (ii) civil service efficiency and integrity and (iii) private sector dynamism and integrity. In Malaysia, all three forces shared the same vision and strategies, and together implemented various development plans.

The first force, political will and integrity, refers to the need for government leaders, cabinet members, politicians and parliamentarians to be selflessly dedicated to national development and be incorruptible. They should have the same vision for the future of their nation and see themselves as 'gifted by God' to serve their nation and its people selflessly. The second force, civil service efficiency and integrity, refers to the need for civil servants to understand that they are servants of the people, and not civil masters. They should be dedicated, incorruptible and totally apolitical, serving the government without fear or favour. The third force, private sector dynamism and integrity, refers to the need for a corporate private sector that is dynamic and aware of the problems of the nation. Instead of waiting for handouts from the government, people in the private sector must be prepared to work with the government to achieve national prosperity. They must realise that only if the ordinary people are happy and prosperous can they, too, succeed.

As can be seen in Figure 9.1, integrity, or good governance within the government and private sectors, is a common element. If even one of these three forces does not work to its full potential, the nation will not succeed. Of course, in any nation, however badly governed and however much in discord, there will be a trickle of investments by companies hoping to reap the profits of high-risk activities, such as mining and supplying to armed groups. For such a trickle of investments to come in, no great macro and microeconomic efforts may be necessary. To convert that trickle into a wave, creating thousands of jobs and ensuring that wealth reaches the unemployed and the less advantaged, requires concerted strategies and for that, the TOH must manifest its full potential. To do this requires changing the mindset of all levels of leadership, to move from 'business as usual' to an awareness of the need for dynamic change and a strong commitment to growth and development.

3.2 Quadrant Strategy

Once the TOH concept is understood, the Quadrant Strategy becomes the vehicle to move from concepts and principles to creating jobs and wealth.

The term 'quadrant' is used because four steps must be taken. The first step in this process is to create an attractive environment for general and specific sectors. Second, identify projects and/or industries that have comparative and competitive advantages. Third, promote the national image to attract investment. Finally, implement the approved projects as speedily as possible to provide jobs and wealth within the country.

The investment environment created by Malaysia during its rapid economic development can, in hindsight, be described by the following formula:

E + C4 + O = P

where **P** = profits for companies and prosperity for the nation; **E** = an environment in which every investor will observe the 'Ten Commandments' for an investment decision; **C4** = (i) cost of doing business; (ii) convenience provided at all stages; (iii) capability of infrastructure and government; and (iv) concessions (incentives, etc.); and **O** = opportunities. The Ten Commandments referred to above are:

1. political stability;
2. economic strength and fundamentals;
3. attitude of welcome from highest minister to most junior civil servant;
4. government policies concerning (a) equity, (b) employment of expatriates, (c) exchange control and (d) rule of law (ownership of assets, etc.);
5. infrastructure—land, electricity, water, etc.
6. labour (trainability, education, work ethics, harmony, productivity);
7. banking and finance;
8. government bureaucracy—friend and ally or hostile obstacles;
9. local business environment;
10. quality of life.

Figure 9.2 illustrates the Quadrant Strategy. The details regarding each of the four quadrants are as follows.

First, the creation of an investment environment conducive to rapid economic development will motivate the movement of foreign and domestic investments into the productive sectors. This will be at two levels: (i) the administrative environment, requiring the reduction of red tape and the establishment and improvement of transparency, rule of law, speed of approvals, etc., and (ii) the physical environment, involving for instance industrial parks that offer infrastructure for problem-free economic and business activities.

Second, the identification of priority economic and/or business sectors that offer the best competitive advantage to the nation is critical. Many developing nations seek to copy the success of other nations and want to jump onto a business bandwagon that has succeeded elsewhere. This mistake has caused many developing nations to waste scarce and valuable resources with little success. The need to investigate what will work for the specific country is critical.

Third, the implementation of well-planned strategies for investment promotion is important to maximise success and minimise expenses. The moment it is known that a country is interested in FDI, advice will flood into the country from the media industry and public relations consultants to convince the country to launch massive public relations programmes in developed nations, and to take out expensive advertisements in magazines and newspapers. Developing nations with no experience reaching out to foreign investors are forced to use valuable and scarce resources on these programmes, which more often than not bring very few tangible benefits. The key to investment promotion is to understand that it is not an *activity*; it is not so much about a president or minister leading a delegation of local businessmen—mostly hangers on—to an FDI exporting nation. Rather, investment promotion is a *process* which starts with the first two quadrants (Investment environment and Priority industries/sectors) of the Quadrant Strategy so that the nation has something positive to sell.

Fourth, a great challenge is to ensure that approved projects are speedily implemented so that they offer jobs and create wealth for the nation. Ministers in developing countries often proudly announce, 'We approved 300 projects last year!' When the same ministers are asked how many projects have been implemented, they cannot produce any details. This is a major problem in many developing nations, including those in Africa. Very few seem to be interested in the 'hard work' involved in ensuring speedy implementation of every project approved. The central government may say they have speedily approved all projects that are within their responsibility. However, that is not enough: as far as the investor is concerned, the government is one monolithic structure. Whether the bureaucratic delay is at the central, state, municipal, city or departmental level, it is still seen as government delay. As long as the project is unable to take off, government inertia drains the private sector and deprives the nation of employment and wealth creation benefits.

3.3 Lessons for Africa based on Malaysia's experiences

It is a common view of policy-makers in Africa and advisers from donors that comparative advantage is an important and essential factor for a country's economic development. However, comparative advantage is not the key. It is competitive advantage that is the most essential element for development. In simple terms, comparative advantage depends on factors like a country's natural resources and location, so the country has no choice in the matter, while competitive advantage must be fostered by man to make full use of comparative advantage.

For competitive advantage to develop, there is a need for maximum cooperation, efficiency and incorruptibility among the forces that initially make up a TOH. Malaysia successfully created competitive advantage with strong leadership under the principles of the TOH concept, and also created a conductive environment for rapid flow of FDI into the country through the implementation of the Quadrant Strategy. FDI flow was facilitated by the

Investment Promotion Agency as the key implementing agency, while all government departments and the private sector worked together to realise the growth of the economy and equitable distribution of wealth to achieve the common goal of the nation.

The economic growth of any nation can be translated into the three waves of economic development. The process of economic development in Malaysia was no different. The first wave is agricultural and commodity development. This wave is rather slow, but continuous development should be ongoing, with improvement of productivity and cost efficiency of the factors of production. The second wave is industrial development based on competitive advantage against other countries, which can only be created when the principles of the TOH concept are fully realised. The third wave is a service and/or knowledge-based drive, where human resources with knowledge create huge amounts of economic growth. These three waves were carefully analysed within the context of the JICA programme in Zambia and will equally apply to any country in Africa. Taking this process into account enabled the SAIED Programme to be effectively designed and implemented.

4 Implementation of the SAIED Programme and TOH in Zambia

4.1 The Zambian economy

Zambia is a typical landlocked country with a population of 11.8 million (2006 estimates). The country is sparsely populated by more than 70 ethnic groups. Eight countries border Zambia, namely, Angola, Botswana, Malawi, Mozambique, Namibia, Tanzania, Democratic Republic of Congo and Zimbabwe. Zambia's shortest route to the sea is via Zimbabwe to Beira in Mozambique.

In the late 1960s, Zambia was the world's third largest copper mining country, after the US and the former Soviet Union. It was said at the time of independence in 1964 that the country could be the richest nation in Africa thanks to its abundant copper reserves. However, world copper prices collapsed in 1975 with devastating effects on the country's economy, and the government lost control of the economy due to financial mismanagement. Thus, various policy reviews urged the government of Zambia to diversify its economic structures, including into tourism and agriculture, and tighten its fiscal policy and government expenditures. However, the mining sector still remains a major hub of economic activity, which accounted for 12.0 per cent of total GDP with US$3,084 million worth of export in 2006, while agriculture accounted for 22.6 per cent of total GDP (US$10.1 billion) in that year. Only 3.2 per cent of GDP comes from the manufacturing sector. The annual GDP growth rate was 5.8 per cent in 2006.

With successful implementation of a fiscal policy and the recent booming increase in the world copper price, inflation in Zambia fell to single digits in 2006, at 8.2 per cent per annum at the end of the year, for the first time in 30 years. Under the attempt to diversify its economic activities, the country also saw commercial agriculture in maize, tobacco, cotton and coffee as potential areas for viable economic growth. However, the majority of ordinary Zambians still experienced chronic livelihood insecurity compounded by frequent droughts.

During the implementation of the Fourth National Development Plan (1989–1993),[8] the government abandoned its intervention in the economy in 1991 and left it completely up to the market, assuming that the market would be fully functional to bring active economic growth. However, the results were mixed because no effective mechanism had been put in place to develop infrastructure and human resources, and because neither proper development planning nor management systems had been established to support the potential of a liberalised market economy.

Learning from these results, the government reviewed its position in 2002 and began to play a complementary role in the market economy with a strong policy coordination and implementation mechanism, accompanied by a proper public investment programme.

Zambia completed the Heavily Indebted Poor Countries (HIPC) Initiative process in 2005 and received significant debt relief under the Multilateral Debt Relief Initiative (MDRI). It received 100 per cent cancellation of debt stock owed to the International Monetary Fund (IMF), the World Bank and the African Development Bank. As a result, with a favourable international market price of copper export, the balance of payments significantly improved to over US$100 million in 2007.

However, despite positive trends within economic activities represented by the mining and agricultural industries, Zambia ranks low in the UNDP's 2006 Human Development Index, at 165 out of 177 countries. Infant mortality rates are among the worst in Sub-Saharan Africa. With one in five mothers being HIV positive, Zambia has one of the world's highest rates of HIV infection. The infection kills around 80,000 people each year. More than half of hospital beds throughout the country are occupied by people with HIV/AIDS and related illnesses. Apart from AIDS, the main causes of death are malaria, at 50,000 each year, tuberculosis, diarrhoea, pneumonia and other preventable infections.

The Fifth National Development Plan (FNDP) 2006–2010, which was also accepted as the second Poverty Reduction Strategy (PRS) by the IMF and the World Bank, was implemented with the long-term national vision under Vision 2030 with the aim of making Zambia a prosperous middle-income country. The theme of the FNDP was 'broad-based wealth and job creation thorough citizenry participation and technological advancement' with economic and social sub-themes. The focus of the FNDP was to create an environment which encouraged private sector growth, including agriculture and rural development, through macroeconomic stability, investment in infrastructure such as roads, hospitals and schools, human resource development and public sector accountability. Within the framework of the FNDP, the government of Zambia emphasises the importance of the promotion of commerce and trade, as well as the manufacturing sector, where the private sector is expected to play the most important role as the engine of growth.

The Private Sector Development (PSD) Programme was launched in 2004 with the support of various international and bilateral development assistance agencies. PSD was implemented to accelerate private sector-led economic growth with the aim of increasing the share of the manufacturing sector in total GDP from 11 per cent at the start to 15 per cent by 2010. The FNDP also aimed at identifying appropriate trade expansion measures for export promotion.

In order to achieve the objective of further promotion of rapid industrial development for both domestic and regional markets as well as exports, the government, as per the recommendations of SAIED/TOH, adopted the concept of Multi-facility Economic Zone (MFEZ), which covered aspects of domestic trade, investment and exports. The MFEZ, which combined the best advantages of an industrial park and an export processing zone and free trade zone, was to be operated and coordinated through the Zambia Development Agency (ZDA), a new agency created for this purpose.

4.2 Adaptation of the TOH and the Quadrant Strategy by the government of Zambia

During the visits of the JICA mission to Zambia in 2004 and 2005, mentioned earlier, the Minister for Finance and National Planning expressed his interest in the concept of TOH presented by JICA. Subsequently, when a cabinet briefing was given on the SAIED Programme (TOH and the Quadrant Strategy), the President, in a display of unprecedented political will, gave full support to the JICA proposal.

This strong political will and support from the highest person in the government of Zambia was critical to initiate the implementation of the SAIED Programme. As explained earlier, the Malaysian experience indicates that political will is an essential element of the TOH concept. The policy framework for the implementation of SAIED/TOH was also in place within FNDP, as mentioned earlier. The President subsequently appointed the members of the TOH Steering Committee, which is chaired by the economic adviser to the President and co-chaired by the Resident Representative of the JICA Zambia Office, and another adviser to the President.

In an attempt to fulfil three of the four quadrants (Investment Environment, Priority Industries/Sectors and Implementation), the following 12 task forces were formed under the President's direct authorisation. Each has 3 government members and 2 from the private sector and the option to co-opt others. It should be noted that other than the JICA Malaysian consultant these committees did not have any other expatriate advisers or consultants.

This concept perhaps differed from many other donor-supported projects where there are often a number of short- to long-term foreign consultants and advisers for every sector who tend to carry out the work that is supposed to be performed by local members.

The 12 task forces were as follows:

1. agriculture and agro-based industry;
2. cotton and cotton-based projects;
3. education;
4. medical and health;
5. information and communication technology (ICT);
6. tourism;
7. banking and insurance;
8. mining;
9. small and medium enterprise development;
10. air cargo hub and inland ports;
11. Multi-Facility Economic Zones (as substitute for Free Trade Zones);
12. streamlining government machinery.

Direct appointment of about 70 task force members by the President himself gave members strong commitment to and ownership of the SAIED Programme. The areas to be covered by the 12 task forces were identified by taking into account the economic situation of Zambia. The country already had a growing agriculture and commodity sector and this should be further developed (the first wave). However, due to its landlocked nature and high costs of local manufacture due to transport and other factors, Zambia did not have the competitive advantage for many industrial products, as compared to its coastal neighbours (needed for the second wave). Even so, the country could move into the third wave by value addition of local natural resources and undertaking limited import substitution where viable. Thus it was proposed that Zambia should leapfrog itself into the third wave and use skills and knowledge as its competitive edge. Under the SAIED (TOH) strategy, these 3 waves are planned to drive Zambia's economic efforts for jobs and wealth creation.

Dato' J. Jegathesan, one of the present authors, as the consultant responsible for putting this initiative into action, and for meeting JICA's and the government of Zambia's expectations, undertook the challenge of creating the terms of reference for all the task forces, except for the mining task force. Each task force was presented with ideas as to what kind of policies, measures and incentives would be needed to create dynamic private sector growth. They were invited to study the propositions presented, and were asked to assess the propositions and accept, amend or reject them. Finally, the task forces presented viable and sustainable strategies, whereupon both government officials and the private sector took ownership for ensuring implementation. Each task force was individually briefed on all aspects of the terms of reference, the recommendations, etc. It was emphasised to all that once the task forces accepted any recommendation that had been offered, the Malaysian consultant would disclaim all ownership of the idea and that these would be the task forces' ideas alone.

The task forces were given three months by the President to produce action plans for each theme. While there was a general assumption that the work by local people alone might not manifest such speedy results, all the task forces managed to complete their action plans and submit their reports to the President within the allotted time. During their initial stage of work, the committees were provided with appropriate advice and guidance. Dato' J. Jegathesan as the consultant responsible for the proper direction of all the task forces conducted a mid-term review of their work halfway through their three-month assignment. The strong political will of the President, which was demonstrated by the direct appointment of the task force members, also brought strong will and commitment by members of the task forces, who were from both public and private sectors. This government leadership, civil service commitment and pro-active private sector participation were the critical ingredients of the TOH strategy, as had been emphasised from the early stages of the SAIED Programme.

4.3 Project identification

For the period between 2005 and 2006, much work was done laying the groundwork for an ideal economic environment, and many recommendations made to the Cabinet were approved and put in place during 2007 and 2008.

Investment promotion (the third of the four quadrants) only started in 2007. The first target nation was Malaysia, and in March 2007, a Malaysian business delegation was organised with the support of the Malaysian Industrial Development Authority (MIDA) and the Malaysian South-South Association (MASSA). Thus, for the first time, a Malaysian business investment delegation (18 members in all) proceeded to Zambia. Two projects were agreed to be implemented as a result of this mission. One was a mobile phone assembly and manufacturing operation to make Zambia the hub for Africa, and the other was a private vocational and technical college.

In April 2007, the SAIED Programme turned its attention to India. A Zambian investment promotion initiative was launched in India (Chennai, Bangalore, Coimbatore and Mumbai). A number of Indian companies, which had no prior knowledge of or interest in Zambia, committed to visit Zambia in 2008. As a result of these initiatives, consultants from an Indian hospital group visited Zambia in May 2007 and the group committed to the government of Zambia to set up a super-specialty medical centre in Zambia, with only the government's ability to provide for a suitable building delaying or accelerating the implementation of this project. The first Asian Business, Investment and Trade Conference (ABITC) was held in Zambia in January 2008. This event catered to business people from any part of Asia, but with specific focus on a business delegation from India and Malaysia with very specific projects in mind.

The key question was: What types of sectors should be promoted as viable, considering Zambia's high cost of transportation and landlocked position? The various task forces, dealing with economic and business sectors, identified the following areas as priorities for Zambia.

1 *Education*: Thousands of Zambians and those in neighbouring nations go to Europe and the US, etc. for their college and university education, simply because facilities are inadequate in their own countries. Under the TOH strategy, the government agreed that Zambia should have the vision to become a regional centre of educational excellence.
2 *Medical and dental*: Despite the presence of excellent foreign-trained doctors (many of whom have gone abroad to serve in developed nations due to lack of facilities in Zambia), Zambia does not have enough sophisticated medical facilities. Thus, Zambians go abroad for MRI, angiogram, angioplasty and many other sophisticated medical tests and procedures. Under the TOH strategy, the government agreed that Zambia should have the vision to become a regional centre of medical excellence.
3 *ICT*: With its excellent English speaking population, high unemployment and increasing e-linkages with the world, Zambia can become the next ICT growth centre initially for call centres, and, subsequently, for other more sophisticated offshore operations. The high cost of imported electronic items provides opportunities for domestic assembly of electronic equipment. The high cost of use of internet facilities (internet cafés, etc.) gives opportunities for the establishment of facilities that will bring down the cost of ICT usage.
4 *Electrical household items*: Landlocked Zambia must import bulky household electrical items through neighbouring ports. This cost of transport problem creates an opportunity for semi-knocked-down (SKD) and completely-knocked-down (CKD) imports of components for local assembly and eventual manufacture. Items such as refrigerators, washing machines, fans, computers and microwave ovens could be candidates for such opportunities.
5 *Cotton products*: Zambia is a producer of cotton, but 90 per cent of it is exported in raw form (lint). The TOH strategy gave the Zambian government a vision to make Zambia a centre of excellence for the growing of cotton, and also the processing of cotton into highest value cotton products, thus minimising the cost factor in transportation. The government decided to develop a strategy to promote clusters of cotton-related companies. Land would also be made available for companies wishing to grow cotton.
6 *Agriculture and agro-based industries*: Zambia's economy is based on agriculture. With its high altitude and favourable agronomic environment,

Zambia could become a major producer of high-quality, organic agricultural products. This sector is another priority, so land and support, including incentives, were to be offered to companies that set up commercial agricultural production. Support would also be offered for the processing of these products into finished or semi-finished products. The government also prepared to offer land to those who wanted to grow trees, and this would be encouraged with incentives.

7 *Mining*: Zambia is a major producer of copper and gemstones. Opportunities exist for forward integration of these minerals into higher value products before export. This is another priority economic sector.

8 *Tourism*: The relative lack of 4- and 5-star hotels in Lusaka has caused a shortage of hotel rooms and a prevalence of high room rates. Livingston, the site of the Great Victoria Falls, is in dire need of good hotels, so the government is prepared to offer land for hotels in this area that could one day become a great tourist destination. The government would promote the establishment of hotels and provide support and incentives. There is also potential for the manufacture of items the hotels will need, such as furnishings, linen, detergents and toiletries.

9 *Energy*: Zambia imports all the energy it uses. Any project that could help reduce the imports of energy would be encouraged and given incentives and support. For example, energy from biomass that could help bring power to rural areas or convert urban waste to energy would be welcome.

4.4 Development of Multi-facility Economic Zones (MFEZ)

As one of the key areas of development under the SAIED Programme, JICA assisted the government of Zambia with technical advice in the development of a MFEZ. This advice was based on the Malaysian experience, which involved the establishment of various economic zones (industrial parks, free trade zones, etc.). A new concept was developed that combined the advantages of a sophisticated industrial park and an export processing and free trade zone, while minimising disadvantages.

The government of Zambia would utilise experts from the Kulim High Tech Park (KHTP) in Malaysia, which was developed with Japanese technical assistance 15 years ago, as well as from Japan (JICA), to develop a master plan and conduct a feasibility study for the establishment of an MFEZ in the outskirts of the capital of Lusaka. Financing from development financing institutions would follow to realise the MFEZ.

5 Challenges ahead

Priority areas identified by the 12 task forces were approved by the Cabinet and translated into action plans, which were to be implemented by the relevant government ministries, departments and institutions. Implementation was monitored by the Triangle of Hope (TOH) Steering Committee. The Steering Committee evaluated the performance of the respective ministries and government agencies in light of whether or not the benchmarks set in the action plans were achieved.

The task forces compiled quarterly monitoring reports with performance indicators, and discussed whether any specific measures need to be taken to expedite the implementation of the Strategic Action Initiative for Economic Development (SAIED) Programme. The civil servants must now undertake the challenge to show the same spirit and commitment as that of the President and key ministers by implementing the action plans in an effective manner.

It can thus be seen that the SAIED Programme is not a one-shot, short-term affair, where a study is done, a report presented, and then, whether it is feasible—whether it can be implemented—is left to the government of Zambia. This JICA initiative is a sustained programme of actions, where the government of Japan, through JICA, works with the Zambian government and even the private sector with the objective of creating visible outputs to contribute to economic growth with job creation through domestic and FDI promotion. It is a further challenge for the government of Zambia to maintain the momentum of opportunities to create continuing competitive advantages for Zambia.

Notes

* Dato' J. Jegathesan was engaged in the JICA-sponsored technical assistance project explained in this chapter as Senior Investment Adviser with the project period from July 2006 to March 2009. He is also Adviser to the JICA Malaysia Office on promotion of South–South Cooperation. Masayoshi Ono worked at the JICA Malaysia Office for South–South/Asia–Africa Cooperation. The views expressed by the authors do not necessarily reflect the views of JICA.

1 'Japan's Policy for African Development: Prime Minister Koizumi's Message to Africa in the context of the G8 Summit' (6 July, 2005). Retrieved from http://www.mofa.go.jp/region/africa/policy.pdf.

2 The United Nations Development Programme (UNDP), which is actively promoting South–South Cooperation, defines the term as 'a means of promoting effective development by learning and sharing best practices and technology among developing countries'. JICA's task force on South–South Cooperation has used the UNDP definition as a base from which to construct its own definition: 'Mutual cooperation aimed at fostering self-sustaining development, involving deepening relations among developing countries while conducting technical and economic cooperation' (see http://www.jica.go.jp/english/about/policy/south/policy.html).

3 Calculated by the authors using data from IMF's World Economic Outlook Database, October 2007.

4 Ibid.

5 Calculated from the figures available from the Bank of Zambia (http://www.boz.zm/snapshot.htm).

6 Government of Malaysia, Third Outline Perspective Plan, 1991–2000.

7 Government of Malaysia, Eighth Malaysia Plan, 2001–2005.
8 After the Fourth National Development Plan (1989–1993), it was not until the formulation of the first Poverty Reduction Strategy Paper (2002–2004) and the Transitional National Development Plan (2002–2005) that the government resumed national development planning.

10 Modeling and sharing Korean development expertise for African growth*

Won-Gyu Hwang

1 Introduction

Throughout the twentieth century, Africa was stigmatized with all the negative symbols of underdevelopment, such as poverty, ill health, corruption, conflicts, and disorder. As its underdevelopment continued in spite of a massive transfer of aid starting from the 1960s, the Western world has shown signs of fatigue since the mid-1980s. Ironically, since the mid-1990s, the African economy has started to revive amid the Western negligence. With the dawn of the new millennium, Africa was in general on the vigorous rise toward development.

One of the most aspiring yet difficult tasks for African leaders is to find an appropriate model of development fitting to their countries. Due to their long history of colonization and humiliation, most African countries lack self-confidence in development. Frustration and embarrassment prevail throughout the continent. They could hardly find a single success model of development from neighboring countries on the same continent. Only when they look out, could they find a few exemplary cases in East Asia, notably Korea. Since the story of Korea's economic development is an epitome of all hardship and adversity with which many developing countries share, it could therefore easily draw attention and sympathy from the developing world, thereby attracting a great deal of academic interest in the Korean economic development model.

As is well known, Korea has evolved from a subsistence economy to one of the industrial powers in the last half-century. Korea's economic development has shown not only the speedy growth of magnitude, but also exhibited qualitative attributes in terms of income distribution and industrial structure.

The remarkable story of Korea's economic development has inspired many practitioners and scholars around the world. It must be one of most dramatic turnarounds from the basket case to the best practice of economic development during the second half of the twentieth century. Quite a few studies have been carried out to find the relevance of Korean experiences to other developing economies, and the endeavor is still underway.

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With the accession to the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and Development (OECD) in 2010, Korea was listed as the first nation to transform its status from the recipient to the donor. The fact has become a catalyst for reflecting Korea's development model for other countries. Considering its relatively small financial resource for aid as the latest donor, sharing Korea's development experiences, not money itself, became one of the most requested needs from the Least Developing Countries (LDCs). Nonetheless, there have been few mechanisms to meet the demand effectively. In addition, one should encounter numerous barriers to make an effective delivery of Korea's knowledge in development to other developing countries. Achieving success at home is one thing, and replicating it in other countries is another.

This chapter was therefore prepared to answer the following questions: Is Korea's success a model to be emulated for LDCs? What is the essence of Korean economic development and industrial development strategy? Can the Korean development model be duplicated? How can it be delivered effectively? And what should be taken into account in the field of development consultation?

2 Attributes of Korean development as a model

It would not be an exaggeration to say that economics is a science of searching for the right policies to improve people's standard of living. Generations of intellectual efforts have been devoted to find the right models to maximize the growth rate of a country, and delivery of such efforts continues under the rubric of growth and/or development theory. Once, a focus was laid on socialist economics when they showed remarkable transformation and growth immediately after the revolution. The prevalence of the communist movement before and after WWII can be well expounded with the significant performance of communist blocs notably at the initial stage of revolution. In the 1960s and the 1970s, a considerable effort was made in search of a right development model for newly independent countries of Asia and Africa. One time, the dependency theory was considered an alternative development model for countries in the Third World, and an effective tool ensuring the "economic emancipation" from neo-liberalism (Frank, 1964). However, academic fever on the theory once popular in development circle in the 1960s gradually languished due to its omnipresent criticism without providing pragmatic alternatives.

Then the intellectual community started to pay attention to the East Asian development model as the growth speed was remarkably fast with industrial sophistication. The Japanese model of government–industry collaboration was considered the origin of the East Asian development model. By that time, however, the success story of Japanese development had already become the epic of past generations when the policy setting was much different. The experiences of East Asian latecomers, or the Asian Newly Industrializing

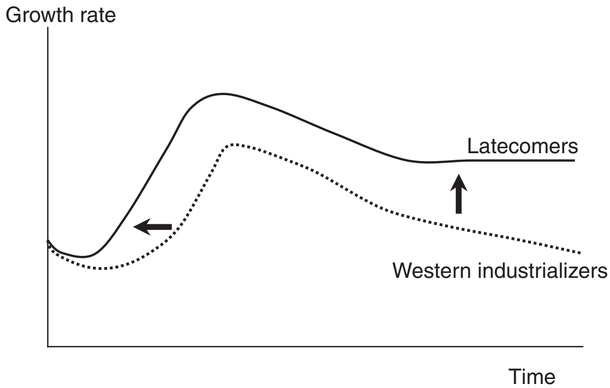

Figure 10.1 Trajectory of growth path for catching-up

Countries (ANICs) such as Hong Kong, Singapore, Taiwan, and South Korea rose up as the best-practice development model containing different aspects from the Japanese model and more relevant to the evolving international economic environment of the twentieth century. Out of the ANICs model, however, the case of Singapore and Hong Kong seems to have limited applicability to other developing countries as they are small entrepot economies. In this sense, South Korea together with Taiwan offers a more relevant model of East Asian development for most developing countries.

To be called a right development model for other countries, it should encompass three attributes: speedy and sustainable economic growth, quality of structural transformation, and applicability to other countries.[1] First, an economic model should suggest ways to speed up growth in a desirable direction. A model should enable latecomers to avoid mistakes as well as to find shortcuts to development. In this context, the economic circle has once indulged in the concept of turnpike theory to suggest the shortest path to development (McKenzie, 1976; Takahashi, 2010). The assumption to realize convergence or catching-up by developing countries necessitates a higher growth rate than advanced countries for a sufficiently long period of time. In this sense, the focus of catching-up theory is twofold: how to shorten the period of take-off; and how to sustain the higher growth rate than that of European countries in the late nineteenth century and the early twentieth century.

As illustrated in Figure 10.1, latecomers speed up and take off more quickly than Western industrializers (developed countries), which means the growth curve shifts to the left. In history, it took nearly 150 years for the Western European countries to reach maturity while it is 40 years for the case of Korea. Sustainability is illustrated as the upper layer curve implying higher growth rate of latecomers than advanced countries named as “Western industrializers” in the diagram.

Table 10.1 Economic statistics of selected countries in 2010

	Population (million)	*GNI (US$ billion)*		*GNI per capita (US$)*		*Exports (US$ billion)*
		nominal	*PPP*	*nominal*	*PPP*	
Ghana	24	30	39	1,240	1,600	8
Philippines	94	192	368	2,050	3,930	51
Turkey	76	719	1,104	9,500	14,580	121
Brazil	195	1,830	2,129	9,390	10,920	202
Korea	49	972	1,418	19,890	29,010	425

Sources: CIA (2012) and World Bank (2012).

2.1 Quantum leap in growth

Korea has made outstanding development in terms of income per capita. It is quite clear when the growth path of income per capita is compared with other countries. Table 10.1 shows a comparison among the countries having different initial conditions of economic development in the early 1960s which is the eve of Korea's economic movement. The countries chosen are: Ghana, having nearly equivalent income per capita with Korea, the Philippines with 2.5 times, Turkey with 3 times, and Brazil having 5 times higher income than Korea in the early 1960s. The table also illustrates various economic statistics in 2010.

Even comparing with other high performers in different continents, Korea's growth record looks distinctive. There are only seven countries in the world achieving GNI per capita higher than US$20,000 with a population of more than 50 million, and Korea became the seventh member of the so-called "20–50 Club" in 2012.

There are many literatures calling East Asian development a miracle.[2] It is true that East Asian economies led by Japan and more recently backed by China made unprecedented growth in a relatively short period of time. During 1965–1999, East Asia on average marked an annual growth rate of 5.6 percent, while the global average was 1.6 percent. The figure is far ahead of those in any part of the world. As a result, income per capita rose rapidly and people's living standards improved dramatically. Even among East Asian economies, Korea is outstanding, as shown in Table 10.2. It was an East Asian basket case in the 1950s, suffering from division of land, civil war, and recurrent famine. However, the nation has made a remarkable shift from the typical subsistence economy to one of the industrial powers of the world.

2.2 Structural transformation: from subsistence to knowledge-based economy

Few countries have been capable of transforming their industrial structure so dramatically as Korea in the last 50 years. Table 10.3 describes the

Table 10.2 Growth of GNI per capita in major Asian countries
Unit: current US$

Country	*1965*	*2007*	*Change (%)*
Korea	130	19,690	15,046%
Taiwan	204	15,078	7,291%
Singapore	540	32,470	5,913%
Hong Kong	710	31,610	4,352%
Japan	890	37,670	4,133%
Thailand	130	3,400	2,515%
China	100	2,360	2,260%
Indonesia	70	1,650	2,257%
Malaysia	330	6,540	1,882%
India	110	950	764%

Sources: World Bank, Taiwan Government (Recited from Schuman, 2009).

Table 10.3 Production structure of Korean economy
Unit: %

Year	*Agriculture, fishery, and mining*	*Manufacturing*			*Services*
		Total	*o/w Light*	*o/w Heavy*	
1953	48.4	9.0	78.9	21.1	42.6
1960	38.9	13.8	76.6	23.4	47.3
1970	28.7	21.3	60.8	39.2	50.0
1980	16.7	28.6	45.6	54.4	54.7
1990	9.3	28.9	32.6	67.4	61.8
2000	5.3	29.4	20.7	79.3	65.3
2009	3.0	27.8	14.7	85.3	69.2

Source: Bank of Korea, National Accounts.

evolution of he production structure of the Korean economy from the 1950s to the 2000s. Korean industrial transformation can be aptly called a metamorphosis from a subsistence economy to one of the industrial powers of the world. When the truce agreement of the Korean War was signed in 1953, Korea exhibited a typical feature of underdeveloped subsistence economy, relying predominantly on the primary sector. The primary sector accounted for 48.4 percent of GDP, while the proportion of manufacturing was merely 9.0 percent. Though a majority of people were engaged in agriculture, the country then was far from self-sufficient in food. The country had to rely on food subsidy from the United States under the PL480 scheme. The

Table 10.4 Share of top 10 export items in Korea
Unit: %

Rank	*1961*		*1970*		*1980*	
1	Iron ore	13.0	Textile	40.8	Garments	16.0
2	Tungsten	12.6	Plywood	11.0	Steel products	5.4
3	Raw yarn	6.7	Wigs	10.8	Footwear	5.2
4	Coal	5.8	Iron ore	5.9	Ships	3.6
5	Cuttlefish	5.6	Electronics	3.5	Audio equipment	3.4
6	Live fish	4.5	Confectionery	2.3	Synthetic fibers	3.2
7	Graphite	4.2	Footwear	2.1	Rubber products	2.9
8	Plywood	3.3	Tobaccos	1.6	Wood items	2.8
9	Rice	3.3	Iron products	1.5	Video equipment	2.6
10	Swine bristle	3.0	Metal products	1.5	Semiconductors	2.5
Total		62.0		81.1		47.6
Rank	*1990*		*2000*		*2010*	
1	Garments	11.7	Semiconductors	15.1	Semiconductors	11.1
2	Semiconductors	7.0	Computers	8.5	Ships	10.1
3	Footwear	6.6	Automobiles	7.7	Mobile phones	8.1
4	Video equipment	5.6	Petroleum products	5.3	Petroleum products	6.9
5	Ships	4.4	Ships	4.9	Automobwiles	6.8
6	Computers	3.9	Mobile phones	4.6	Display products	6.4
7	Audio equip.	3.8	Synthetic resin	2.9	Automobile parts	4.1
8	Steel products	3.8	Steel products	2.8	Plastic products	3.5
9	Synthetic fiber	3.6	Garments	2.7	Chemical prod.	3.1
10	Automobiles	3.0	Video equipment	2.1	Domestic appliances	2.9
Total		53.4		56.6		62.8

Source: Statistical database of the Korea International Trade Association (www.kita.net).

manufacturing sector was not only minuscule, but also far from modern. Virtually all manufacturing goods were imported or distributed by the international donor community.

Korea's industrial transformation is reflected well in its export items. As shown in Table 10.4, export volume before industrialization was marginal and items were predominantly resource-based such as rice, tungsten, dry fishes, and timber, all of which were leading export items at the time. However, Korea's exports became more and more sophisticated with improvements in technology, and its volume swelled drastically to become the ninth country surpassing its trade volume over US$1 trillion in 2011.

At the dawn of the twenty-first century, Korea became one of the industrial powers of the world, producing high-technology electronic products such as semiconductors. In addition, Korea entered into a full-fledged knowledge economy while leading the world in production of shipbuilding, semiconductors, electronic display panels, mobile phones, etc.

2.3 Rapid growth with equity

The quality of Korean economic development is attributed not only to the speed of growth and industrial transformation, but also to income distribution. International comparative studies illustrated that the Korean economy expanded in parallel with income equality in the course of economic development. According to the World Bank's research on the *East Asian Miracle* (1993), Korea has exhibited one of the most desirable patterns of development, rapid growth with redistribution during the period of 1965–1989.

Korea's income inequality remained relatively stable throughout the 1990s and 2000s. Its Gini coefficient at 0.315 ranks 20th out of 34 OECD member countries, and is much more favorable than most emerging countries (OECD, 2010). In addition, Korea could achieve democracy later on and it is recently ranked on top in Asia in the Democracy Index Survey conducted by the Economist Intelligence Unit.[3]

3 The relevance and applicability of the Korean development model to Africa

This section deals with whether Korea can be a relevant model for African countries which are earnestly seeking the right model of development. Finding the most relevant economic development model for African countries can start from an authoritative research report recently published by the World Bank. *The Growth Report* identified only 13 economies which have recorded more than 7 percent growth annually for more than a quarter century since 1950 (Commission on Growth and Development, 2008). It is plausible that African countries can find their own models of development among those 13 countries. However, the countries listed in Table 10.5 are quite heterogeneous in terms of population size and land area. On one side, there lies China with a population over 1.3 billion and land size near to 10 million square kilometers. At the other end, there is a small island-state in the Mediterranean called Malta with a population of less than half a million.

In the same manner, all 54 countries in Africa are diverse in their size of area, population, and resource endowment. Therefore, each country can find a more relevant model which fits better than others considering their own setting. Nonetheless, finding the fittest to the average African country may be a meaningful intellectual work. Thirteen countries can be categorized into four groups. Type I countries in the above table are either too big, or too wealthy to emulate for most African countries. Countries belonging

Table 10.5 13 model countries with sustainable growth rates

Type	*Country*	*Population (2011, thousand)*	*Land area (sq. km)*	*GNI per capita (2010, nominal, US$)*
Type I	China	1,347,350	9,596,960	4,270
	Brazil	192,376	8,511,965	9,390
	Indonesia	237,641	1,919,440	2,500
	Japan	127,610	377,835	41,850
Type II	Thailand	65,500	514,000	4,150
	Korea	50,000	98,480	19,890
	Malaysia	29,000	329,750	18,300
	Taiwan	23,245	35,980	19,130
Type III	Botswana	2,038	600,370	6,790
	Oman	2,773	212,460	18,260
Type IV	Hong Kong	7,104	1,092	32,780
	Singapore	5,183	693	40,070
	Malta	418	316	19,130
	African country on average	19,700	570,218	1,548

Sources: World Bank, African Development Bank.

to Type III and Type IV are either resource-dependent on a single item[4] or too small, which are not generally available for most African countries. In this sense, countries in Type II should be more relevant for most African countries to emulate. Among countries in Type II, Thailand and Malaysia might look closer to the African prototype in terms of land size and population. However, Korea together with Taiwan should provide a better quality precedent in its remarkable growth with equality. If we take into account the initial condition of a shattered economy which is commonplace in Africa, Korea offers an incomparably relevant model for African countries.

There is no doubt that Korea's economic performance is distinctive in quality as well as in quantity. The question is however whether Korea's development model is specifically relevant to Africa's efforts toward development in the twenty-first century, and whether it is applicable to African countries. If so, how can it be replicated more precisely to which country in Africa? The current section shall be devoted to delving out which factors of Korea could become a role model for African development, and narrowing down specifically to apply the Korean model to a particular small country in Africa—Rwanda.

3.1 Factors coinciding with the Korean development model to Africa

The process and pragmatism of Korea's experiences offer ample insights, but do not necessarily provide specific guidance for countries with very different policy environment, such as culture, governance system, resource endowment, policy process, and implementation capacities.

There are yet many Korea factors that can be emulated by other developing countries, in particular by African countries. Most of all, Korea is a paragon example of compressed economic development that has accomplished economic development within a generation (Amsden, 1992). Its rapid shift from subsistence to an industrialized economy is the most aspiring goal pursued by many African countries which desperately covet the realization of tangible changes within a generation. That is to say, Korea can be a beacon of hope for most African countries.

Second, Korea's development is more distinctive since it has succeeded in spite of its inclement circumstances against development. The country was divided, and then war-torn. The quasi-war status of military confrontation still continues, which necessitates a perennial heavy burden on defense spending. The country is small in size and resource-poor, but populous. In addition, the nation has to import all petroleum at the highest costs in the world, since its import transportation route is the farthest from production sites which are mostly in the Middle East. It is Korea's ingenuity and manipulation of overcoming unfavorable conditions that fascinates other developing countries.[5] In a sense, the Korean development model is versatile to be applied to many low income countries trapped in all difficult conditions.

Third, Korea is like a development laboratory. Characterized with its compressed development, the country has undergone not only brilliant successes, but also bitter failures in pursuit of diverse policies. Few countries in the world have actually experimented such drastic (or innovative, to some extent) ideas into policy. Therefore, policy experiences of Korean economic development offer invaluable lessons for latecomers either to replicate or to avoid. One of the laudable aspects of Korean economic development is the concerted efforts, desirable interaction, and smooth transition of initiatives between private and public sector, which is extremely important yet one of the most difficult subjects for many developing countries.

Fourth, Korean development is not a story kept in a library. It is a living example. Most Korean people enjoying an affluent life nowadays have actually experienced a predicative livelihood at one time during their lives. Therefore, Korean people have some hands-on experiences, thus Korean economists have some acumen in economic development that can be hardly emulated by people in the West. Though Korean policymakers might not be as fluent and prolix as Western economists in delineating policy options in foreign languages, many have acute sense and intuition in taking necessary and adequate actions based on their actual experiences in development. Economic development is something beyond the realm of academic knowledge.

Fifth, in terms of development cooperation resources, Korea may not have ample resources when compared with leading industrialized countries. However, there is a room for Korea to increase its endowment as the economy grows and the country is determined to comply with the OECD recommendation of Official Development Assistance (ODA) contribution. In addition, another important yet hardly-known resource is available in Korea—philanthropic resources mainly from the Christian community. Among Christian organizations in the world, Korean protestant churches are probably the best-organized ones, thus one of the most resourceful congregations. For example, at a certain national priority area of philanthropic activities, the amount the Christian community supports already exceeds several times the official support. If well mobilized, the resources can be channeled effectively into African countries.

3.2 Fitting the Korean development model to Rwanda

No matter how excellent the end-result of economic development is, it is hard to replicate a development model without considering social and economic relevance. However, the Korean development model can be easily applied to many African countries, especially those which share commonalities with Korean experiences. Among 54 African countries, it is hard to deny Rwanda is close to a basket case in development. Nonetheless, there exists an applicability of Korea's development model to Rwanda.[6] Between Rwanda and Korea, there are a lot of similarities in both economic and non-economic factors affecting development. Table 10.6 illustrates non-economic commonalities in both countries. These are mostly geo-demographic factors.

As shown above, the socio-economic circumstances faced by Korea in the early 1960s are not that different from those of Rwanda in the early 2000s. Nonetheless, there are many differences in internal and external environment between the two. Some were of course more favorable to Korea, but in general, Rwanda appears to possess more favorable factors than Korea in the 1960s.

Less favorable factors for Rwanda compared to Korea include global trade regime, neighborhood externalities, and the role of government. First, the global trade environment in the twenty-first century under the World Trade Organization (WTO) regime makes external trade more competitive than in the 1960s when Korea had benefitted from the Most Favored Nations (MFNs) scheme under the General Agreement on Tariff and Trade (GATT). Second, Korea could make use of positive neighborhood spillover from externalities, including the most innovative economies in the world such as Japan. Korea's industrial development owed much to the Japanese operation of international division of labor either as offshore producers or as vendors of components. A considerable number of Korean companies participated in the vertical production structure of Japanese companies during the development stage. On the other hand, it is difficult for Rwanda to expect positive outcomes as its surrounding neighbors have been suffering from underdevelopment. Third, the Korean government in the 1960s and the 1970s could play a leading role in development. As illustrated by

Table 10.6 13 non-economic commonalities in Rwanda and Korea

Factors	*Common attributes*	*Rwanda*	*Korea*
Land	Small & mountainous (Portion of mountains)	26,000 sq km (80%)	99,720 sq km (70%)
Population	Densely populated (Density per sq km)	11.7 million (450)	49 million (491)
Geography	Remote and costly transportation	Land-locked	At the edge of Eurasian continent
Conflicts	Disasters and destruction	Eviction and genocide	Division and civil war
Religion	Christianity	90% of total population	27%, but solidly organized
Leadership	Educational and political background	Paul Kagame (Uganda and Military)	Park Chung-Hee (Japan and Military)
Milestone	Truce and development	1994 and 2003	1950 and 1962

the nickname "*Korea Incorporation*," the Korean government intervened deeply in major investment decisions, resource allocation, and planning. The Korean government's proactive efforts were appraised as the typical role model of a developmental state. However, though the Rwandan government is determined to play a pivotal role in development, its commitment in the twenty-first century is relatively more limited than that of Korea in the 1960s. Under the WTO regime prohibiting command of an explicit industrial policy, the role of the Rwandan government stays as a facilitator or an advocator at most.

There are many factors which are more favorable to Rwanda than those of Korea's initial stage. First, though both countries have little arable land, Rwanda is endowed with more fertile and more diverse flora than Korea. Mild weather and appropriate precipitation allow multiple cropping in Rwanda, which is not available in Korea. Second, Rwanda can make use of opportunities of being a latecomer in the wake of rapid technological transformation. Rwanda in the age of the information society, unlike Korea's status in the post-industrial era, does not necessarily follow the footpath of early industrialized countries. In the economic turnpike theorem, latecomers can take on the route of a jump-start development under a certain condition, and Rwanda can be wisely poised to climb on the bandwagon of new technology. Third, Korea's regional position in its development stage was subsidiary to Japan. Throughout the period of the Cold War, Korea was located at the Far Eastern edge of the capitalist camp. All international trade flow aimed at crossing the Pacific Ocean, which necessitated the most expensive transportation route. However, though Rwanda is landlocked, it can be a regional business hub commanding the natural monopoly market in the deep inside of East Africa. Fourth, Rwanda could spend a smaller portion of its national budget on defense, which is not imaginable for Korea under the persistent threat from North Korea. Fifth, the Rwandan tradition of a multilingual society can be a great asset in the age of a global village, while Korea's mono-lingual culture poses immense challenges in the era of globalization.

Comparing the favorable and unfavorable conditions Rwanda faces, it can be estimated that Rwanda has potential to replicate what Korea has explored in the path of rapid development. Nonetheless, similarity at the starting point may not guarantee the possibility of replication. Each country has its unique socio-historic nexus and requires indigenous pursuit of development policy. What is given to each nation is how to judiciously mobilize and manage resources toward development. In this perspective, Rwanda has been making efforts in emulating East Asian success, and the country can and deserves to succeed as Korea did a generation ago.

For the purpose of sharing a concrete example, the section below describes the author's experiences in policy consultation for the government of the Republic of Rwanda in 2006–2009. Though subjective, the story provides some insights in replicating an economic model for other countries. In this case, endeavor was laid on seeking applicability of the Korean development model to Rwanda.

3.3 The author's experience as policy advisor in Rwanda

By no means is the Republic of Rwanda in a favorable condition for economic development. It gained independence from Belgium in 1962. However, independence was another start of long-lasting hardship internally as well as externally. The country was artificially split into two nations as Rwanda and Burundi, leaving many racial compatriots in the eastern provinces of the Democratic Republic of Congo. Upon independence, racial conflicts intensified between Hutu and Tutsi, and exploded in 1994, resulting in the outbreak of the so-called Rwandan genocide. Nearly one million people were sacrificed within a few months starting April 1994.

Then a new government came to power under the support and recognition of the international community. The military leader Paul Kagame showed percipient leadership in resuscitating the shattered nation, stabilizing and moving the society into development. The country which would have been the basket case of Africa's low income countries is nowadays a lauded economy adopting one of the most business-friendly policies in Africa. Its policy stance has been rewarded with its rapid and stable growth rate since 2003.

When Rwanda reached a point in concentrating economic growth in the early 2000s, a group of intellectuals within the government started to look at the performance of East Asian economic growth, and wished to emulate their strategies, notably those of South Korea. To name a couple, they included Dr. Donald Kaberuka, the incumbent President of the African Development Bank and the former Rwandan Minister of Finance and Economic Planning, and Dr. David Himbara, the former strategic advisor to the President. Influenced by their advice, President Kagame himself showed a keen interest in learning from the experiences of Korea. There was communication between the two countries to invite a Korean industrial economist to Rwanda through the Korea International Cooperation Agency (KOICA) office in Tanzania. However, no Koreans volunteered for the job although the KOICA searched for a candidate for three years. Then a devoted development economist, the author of this chapter, volunteered to work at the Rwandan Ministry of Commerce and Industry (MINICOM) in 2006. While working at the Ministry, he did more than what was described in the Letter of Contract, contacting many key decision-makers of the nation. Eventually, he was invited by President Kagame to give a lecture on economic development. Impressed by the magnificent performance of Korea and sympathizing with Korea's adversity and struggle in development efforts, the President ordered the author to be invited again at the cost of the Rwandan government. Since then, he has made a perennial visit to the Office of the President, and submitted several policy reports on development planning and macroeconomic management. Then he was ordered by the President to travel all around the nation to give lectures to major decision-makers and opinion leaders. His lecture tour included the Cabinet Ministers meeting, joint conference of the Senate and Parliament, military leaders meeting, all provincial offices including the capital city, business leaders associations, and the National University of Rwanda.

The author emphasized Rwanda's positioning as the inland business hub in East Africa and underlined the importance of promoting the manufacturing sector at home. He again recommended looking at East Asian countries as Rwanda's model, including Singapore and Korea. His suggestion of making the nation the African business hub while combining the attributes of success of Singapore and Korea led the President himself to make an official visit to those two countries for the first time in Rwandan history in 2008. The Singapore government recognized and responded to Rwanda's consultation request, whereas the Korean government did not embrace this opportunity unfortunately.

Nevertheless, the author's consultation reports were highly valued by the Rwandan government as a guideline for government restructuring in favor of mainstreaming macroeconomic management at the Office of the President. Moreover, these reports contributed to enhancing the country's policy capacity, leading to the creation of a policy analysis unit at the Office of the President and a research institution called the Institute of Policy Analysis and Research (IPAR). The reports again emphasized the government to pursue new perspectives in looking "4-wards": forward-looking, outward-looking, eastward-looking, and downward-looking.

Later, the government invited a few Singaporean experts to work at some public agencies, and that effort led to a successful reconstruction of State-Owned Enterprises (SOEs). The newly created institution called the Rwanda Development Board (RDB) incorporates all SOEs in the nation under one roof. This is a Rwandan version of Temasek, a holding company of major SOEs in Singapore. As a revolutionary way to realize maximum efficiency, Joe Ritchie, an American businessman, was appointed as the founding CEO of the organization.

The author's efforts left a legacy in relations between the two countries. First, Rwanda opened a diplomatic mission in Seoul in 2009, and the KOICA in return opened its office in Kigali, the capital city. Then tens of Korean volunteers and senior technical advisors were dispatched, and several projects were launched including the computation center cum library at the National University of Rwanda, and a renovation project of a vocational training institute. In response to Rwanda's amicable approach to Korea, the Korean government designated Rwanda as one of eight African strategic partner countries of Korea's development cooperation. In 2011, Korea dispatched a preparatory task force team to open an embassy in Rwanda. The Rwandan government responded quickly with H.E. Paul Kagame's attendance at the OECD Fourth High Level Forum on Aid Effectiveness, which took place in Busan in November–December 2011.

Rwanda still aspires to maintain friendly and coaching relations with East Asian countries. In recent days, China has played the greatest role in investment in major projects in Rwanda. However, though Rwanda is much in need, what Rwanda earnestly wants from its East Asian friends is not money, but wisdom in development.

4 Korean mechanism of sharing development expertise

Korea is often referred to as a sole paragon example in which a recipient country of development assistance transformed to a donor country within a generation. Since the Republic of Korea became a full-fledged member of the OEDC Development Assistance Committee in 2009, the Korean government has announced a promotion of better development assistance in both quantity and quality. In particular, Korea pledged to increase the proportion of ODA to GNI in coming years.

4.1 Overview of Korea's ODA

Korea's development cooperation started even when it still relied on ODA from advanced countries. Korea as early as the 1960s began contributing to international development by providing technical training under the financial auspices from multilateral agencies, which expanded substantially in the 1980s, offering a wider range of training, seminars, etc.[7] (Lumsdaine and

James, 2007). The International Development Exchange Program (IDEP), the first technical cooperation program financed purely by the Korean government, was launched at the Korea Development Institute (KDI) in 1982 as a form of Technical Cooperation among Developing Countries (TCDC). Then the concessionary loan facility, named the Economic Development Cooperation Fund (EDCF), was established in 1987, followed by the creation of the KOICA in 1991 to allocate grants-in-aid.

As Table 10.7 shows, the scale of Korea's ODA until the late 1990s remained small. It was only after 2000 when the volume leaped by a great amount, and in 2010 the total amount surpassed US$1,000 million, increasing nearly five-fold from 2000. Compared to other OECD—DAC member countries, Korea is still a small donor. In 2010, its ODA/GNI ratio ranked the lowest with 0.12 percent, whereas Portugal allocated 0.29 percent of GNI to ODA and Italy was the second lowest with 0.15 percent. In terms of volume, Korea was the sixth lowest donor. However, as part of its endeavor to eradicate poverty, Korea continuously expands its contribution to the international community as promised at the time of acceding to the DAC.

In terms of the types of ODA, Korea allocates a bigger amount of bilateral aid and concessional loans than grant and multilateral aid. This may be attributable to Korea's positive experience as a recipient country that achieved economic growth from concessional loans, believing in fiscal discipline of the recipient country (OECD, 2008). However, Korea is to follow the DAC's Recommendation on Terms and Conditions of Aid which recommends the member countries to raise the overall grant element to 86 percent (OECD, 2008). Though its portion as well as amount looks relatively stringent, the growth speed is salient, increasing ODA to GNI from 0.12 percent in 2010 to 0.15 percent in 2012 and 0.25 percent in 2015.

4.2 Legal framework and organizational structure of Korean ODA

Korea's ODA is under the framework of the Basic Law on International Development Cooperation, which was enacted in January 2010, soon after its membership to OECD-DAC. The Basic Law was enacted following the recommendation of OECD-DAC in 2008. This Law encompasses the fundamental values, objectives, and direction of Korea's development cooperation. The goals are comprised of the following: to alleviate poverty, empower women and children's rights, and achieve gender equality, sustainable development, and a humanitarian approach to bring world peace and prosperity. The operational principles include universal ideals such as following the UN Charter, and support and cooperation with partner countries for their sustainable development.

At the policy and implementation level, Korea has a dual structure, as illustrated in Figure 10.2. The Ministry of Foreign Affairs and Trade

Table 10.7 Korea's ODA disbursements
Unit: US$ million

Year	*1990–1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*
ODA (Total)	89.4	116.0	159.2	185.6	182.7	317.5	212.1	264.7
Bilateral aid	41.8	71.5	123.3	111.3	124.7	131.4	131.2	171.5
- Grant	26.1	50.1	53.4	54.8	37.2	39.0	47.8	53.0
- Concessional loan	15.7	21.4	69.9	56.6	87.5	92.4	83.4	118.6
Multilateral aid	47.6	44.5	35.9	74.3	58.0	186.1	80.9	93.1
ODA/GNI (%)	0.02	0.02	0.03	0.04	0.06	0.08	0.05	0.06

Year	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*
ODA (Total)	278.8	365.9	423.3	952.3	455.3	699.1	802.3	816.0	1168
Bilateral aid	206.8	245.2	330.8	463.3	376.1	490.5	539.2	581.1	891
- Grant	66.7	145.5	212.1	318.0	259.0	361.3	368.7	367	567
- Concessional loan	140.1	99.7	118.7	145.3	117.1	132.2	170.6	214.1	324
Multilateral aid	72.0	120.7	92.6	289.0	79.2	205.6	263.1	234.9	277
ODA/GNI (%)	0.06	0.06	0.06	0.10	0.05	0.07	0.09	0.10	0.12

Sources: Ministry of Foreign Affairs and Trade, Korea Eximbank, EDCF Database, and OECD International Development Statistics Database.

Note: Data for 1990–1994 are average. All data are net disbursement based.

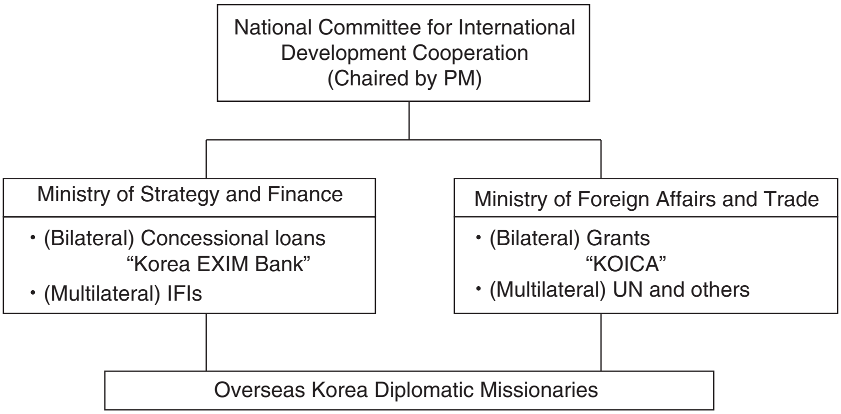

Figure 10.2 ODA architecture of Korea
Source: http://www.odakorea.go.kr/.

(MOFAT) is in charge of grants and technical cooperation policy, which is implemented by the KOICA. As for concessional loans, this is managed by the Ministry of Strategy and Finance (MOSF), which is carried out by the Korea Export-Import Bank's Economic Development and Co-operation Fund (EDCF). Every five years, MOSF and MOFAT prepare and submit the Basic Action Plan subject to approval of the National Committee for International Development Cooperation (NCIDC). The dual structure has incessantly raised the issue of aid ineffectiveness, namely lack of coordination and fragmentation (OECD, 2008). The Korean government has been advised to tackle this two-pillar system and create a single entity that overlooks all policies, strategies, objectives, and activities.

In order to alleviate the shortcomings of the fragmented structure, the NCIDC chaired by the Prime Minister is to be in charge of policy-making of medium- and long-term strategy and coordination of Korea's ODA. It is the single overarching authority that oversees all ODA activities including the development policy, post evaluation, ODA volume, and operational plan. The NCIDC is also expected to improve efficiency and transparency of Korea's ODA while complementing Korea's decentralized system.

4.3 ODA resource allocation

Korea's ODA resource allocation in recent years is described in Table 10.8. As for the geographical feature, a significant sum of Korea's ODA is disbursed to Asia and Lower Middle Income Countries (LMICs) which is in clear contrast to other DAC member countries who focus more on Africa and LDCs. The OECD recommended Korea to shift its focus to the poverty-stricken countries in Africa, but Asia has always been the largest recipient, owing to Korea's

Table 10.8 Korea's ODA allocation by region, income group, and sector
Unit: US$ million

	2001	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*
Region									
Africa	4.38	5.63	18.98	28.11	39.14	47.83	70.17	104.06	95.01
SSA	1.44	2.59	15.21	22.02	33.41	38.85	52.56	86.3	74.7
Asia	124.47	161.77	192.46	258.82	374.95	227.59	299.99	281.37	313.45
Middle East	1.39	5.87	42.18	81.08	177.74	71.79	70.66	30.54	21.37
Income Group									
LDCs	8.35	45.74	56.88	86.05	114.92	92.11	120.97	144.24	161.17
OLICs	60.94	25.16	26.91	49.24	45.99	36.11	37.24	68.51	76.45
LMICs	64.86	91.84	138.69	164.24	267.18	193.38	250.91	207.82	204.17
UMICs	26.24	33.44	7.85	9.23	9.22	9.73	21.76	28.15	38.83
Sector									
Economic infrastructure	74.44	71.6	108.85	113.12	138.12	170.95	402.86	544.52	876.64
Social infrastructure	56.38	160.26	136.91	314.32	398.25	403.09	410.5	696.0	402.37
Production	5.24	7.17	38.27	18.8	50.25	33.5	128.99	77.44	57.12

Source: OECD International Development Statistics Database.

Note: SSA (Sub-Saharan Africa), LDCs (Least Developed Countries), OLICs (Other Low Income Countries), LMICs (Lower Middle Income Countries), UMICs (Upper Middle Income Countries). Sector allocation is commitment based.

geographical position and its unique development experiences (OECD, 2008). Korea also directs much of its foreign direct investment to Southeast Asia as well. This implies Korea's attempt to link ODA to its national economic interests (Choi, 2011) as well as to promote regional integration and to export Korea's own development experience while displaying its attempt to meet the international norms and standards as the newest DAC member (Stallings, 2010). Sector-wise, a large amount of ODA is concentrated on the economic sector. While disbursement to social infrastructure sector is stable, aid to economic sector rose rapidly by more than two-fold from 2007 to 2009.

4.4 Priority areas of Korean ODA

Recently, the Korean government reaffirmed the significance of selection and focus. In the Roadmap for Korea's ODA, which represents the direction of Korea's ODA policy, Korea is to follow the recommendation of OECD-DAC on selection and focus and to reform its aid strategy so that prioritization of the KOICA and the EDCF are coherent. It also aims to reduce priority partner countries to 26 based on income level, region, and capacity (PMO, 2010). At the same time, it will lessen one-shot events or short-term projects and boost budget on education and training as well as emergency relief (MOSF, 2011).

In terms of prioritization of sector, Korea is to focus on eight sectors in which it has abundant experience and which are demanded by partner countries: economy, health, human resources, ICT, agriculture, rural development, environment, and industry and energy. Both the KOICA and the EDCF will cooperate in developing contents and transferring their know-how along with consultation from related ministries (PMO, 2010). The Korean government will also mainstream cross-cutting issues including green growth, gender equality, and human rights in all eight priority sectors (PMO, 2010).

Prioritization is necessary when taking into consideration Korea's limited ODA resources and its comparatively small budget. Furthermore, since Korea's policy capacity is relatively weaker than that of implementation, it should establish mid- and long-term combined strategy for an efficient management of ODA budget (MOSF, 2011).

4.5 Dissemination of Korea's development experiences

With its unprecedented achievement in economic development, Korea attracts a great deal of attention from many developing countries including those in Africa. Despite the magnitude of Korea's ODA budget remaining smaller in comparison to other OECD-DAC members, Korea has strength in having unrivalled experiences and knowledge in economic development to share with other developing countries.

Korea's involvement in policy consultation started in the mid-1980s when the Malaysian government pursued the Look East Policy under the initiative of Prime Minister Dr. Mahatir. The Malaysia Industrial Development Agency (MIDA) commissioned the United Nations Industrial Development Organization (UNIDO) to draft the First Malaysian Industrial Development Plan earmarking Korean experts to be integral members of the project team. The KDI dispatched five Korean industrial economists for three years (1984–1987). When Korea revived successfully from the aftermath of the East Asian economic crisis in the late 1990s, demand for development consultation surged, mainly through the overseas arms of the KOICA. In this stage, individual consultants were dispatched to work at government agencies in developing countries under the financial support of the KOICA. Due to shortages in development cooperation resources, big projects were hardly available with an exception of the Vietnamese project. In 1994 immediately after the restoration of diplomatic relations, the Vietnamese government requested to build an economic think tank, the Vietnam Development Institute (VDI, later renamed as the Development Strategy Institute or DSI) as a Vietnamese version of the KDI. The multi-million dollar project financed by the KOICA was carried out in laying the corner stone of building Vietnam's premier policy research institution.

Upon incremental requests from developing countries, the Korean government devised the Knowledge Sharing Program (KSP) to deliver Korea's development experiences systematically. The earlier version of the KSP had been proposed and managed by the World Bank in collaboration with the Korean government under the name of the Knowledge Partnership (KP) since the early 2000s. The KSP is an important intellectual mode of Korea's ODA with the objective of systemization of Korea's development experiences and provision of assistance to ameliorate poverty and achieve sustainable development tailored to each partner country while mainstreaming growth in development strategy. It is a demand-driven comprehensive consultation program launched in 2004 by the MOSF and implemented by the KDI. It is also specific and result-oriented and KSP supports detailed policy formation and institutional capacity building with the aim to produce tangible outcomes. Until 2011, KSP has carried out research and consultations in more than 25 countries in over 200 topics. Consultation for the Dominican Republic on export development (2008–2010) and a 3-year strategic partnership project with the Vietnamese government (2009–2011) are notable examples of the KSP. The KSP is putting efforts in systemization and modularization of Korea's development policy and expertise in 100 best practices in order to offer as a Standard Operating Procedure (SOP) in development cooperation.

The KOICA is also very active in offering development consultation, especially in Africa. It organizes Korean senior experts as policy advisors at various agencies in developing countries, and supports multi-sector consultation upon request from the recipient countries. Some of the notable examples are: Algerian development planning (2007–2008), Rwanda industrial development consultation at the Office of the President (2008–2009), and the Democratic Republic of Congo development planning at the Office of the President (2011). A similar scale policy consultation project is underway in Ethiopia (2012).

5 Concluding remarks: two contrasting views in policy transfer

No other continent in recent history has experienced more hardship and frustration than Africa. In spite of its reputation as the cradle of human settlement and brilliant cultures, Africa as a whole underwent the process of colonization and exploitation from the late nineteenth century. The continent was fragmented by European imperial powers when they engaged in a major territorial scramble and occupied most of the continent. As a result, up until now the African economy has been characterized with typical symptoms of backwardness and underdevelopment.

In spite of all adversities mentioned above, there is no doubt that the twenty-first century should be the era of Africa. Already most countries in Africa since the late 1990s have started to move forward. The average economic growth rate of Africa during the first decade in the twenty-first century reached the level in the 1960s when a great deal of dynamism erupted in the aftermath of independence. During the period of 2000–2008, the average growth rate in Africa was 5.4 percent. The global economic crisis that started in 2008 weakened the growth of the majority of African countries' economies in 2009. However, the economic slowdown was not as drastic as other continents, as statistics suggested only a 2.5 percent decline for 2009.[8] Although there remain many uncertainties, the African economy seems to have recovered its lost resilience since 2000. Poverty still remains rife, but most African states have benefitted from a more stable political environment in recent years to start catching up with the developed world. In this context, at the start of the twenty-first century, the time has begun for African countries to accelerate development.

Korea is well known as an economic wonder of the second half of the twentieth century. Therefore, it is hard to deny that the Korean experiences must have many aspects that can be replicated by other developing countries. In this last section, however, it is tested whether a country's development expertise, no matter how excellent it is, can be transferred to another country while suggesting two contrasting views on policy applicability. This chapter is not meant to answer the question, but leave propositions in the hands of readers of the book.

(1) Can we replicate the Korean development model in Africa?

At first glance, this appears not to be problematic. In fact, applying a model indigenous in a country to another country might not be that easy. Furthermore, replicating tacit knowledge and experiences of a country must be extremely equivocal. As has been the experience of Korea, many best practices advised by international organizations as successful precedents in developed countries, more often than not, have not been working very well in Korea. Even some policy recommendations undeniably turned out to be inimical to the economy.[9] A nation's policy can be easily distorted by different policies with diverse interests and strategies. Using an analogy of medicine as an example, policy transplantation in a nation often incurs rejection symptoms. Therefore, it is appropriate to say that there is no development panacea that can cure all obstacles of economic growth. In this sense, a policy recommendation by foreign consultants should remain extremely temperate, and refrain from overriding local expert opinions at ease. It is insightful to think of the False-Paradigm model which attributes the status of underdevelopment in developing countries to faulty and inappropriate advice provided by international advisors from developed countries and multinational donor agencies.[10] Along the line, Francis Fukuyama has suggested a useful concept in transferring institutional capacity from one country to another. He classified factors according to the degree of transferability, then argued: while organizational design and management are relatively easy to transfer, cultural factors are hard to copy.

(2) It is generally accepted that there is no royal road in development

Each country has its own indigenous culture, history, and natural setting, thus requires a unique solution that fits into its own policy environment. A success model grounded in the local conditions of a country may not be applicable universally to other countries. Nonetheless, scholars have attempted to find common factors in economic development. One of the recent studies of this effort was released by the special Commission on Growth and Development under the title of the *Growth Report* (Commission on Growth and Development, 2008). The report identified 5 common factors to high growth performers of 13 economies which have recorded more than 7 percent economic growth rate per annum for more than a quarter century since 1950. The 5 features are: leadership and governance, macroeconomic stability, future orientation, market allocation, and openness.

Interestingly, the framework drafted by the Commission is to a great extent coincident with the success factors of the Korean development model. In one way, it reflects the quality of Korean development as a paragon for other developing countries. On the other hand, it signifies at the same time that Korea's development model is not unique at all.[11] There are a number of best practices which have made the best use of existing technology and setting. Examples include Great Britain in the eighteenth century, Germany in the nineteenth century, Japan in the early twentieth century, and East Asia including Korea in the second half of the twentieth century. Something that has worked in one country can be a valuable treatment for other countries in spite of different time periods and settings. Nonetheless, each developing country should revise the best practices scrupulously to fit into its own culture and system. History teaches us what development ought to be. Policy contents differed, but the leadership exerted was more or less identical in many countries.[12] That is why development belongs not only to the realm of sciences, but also to that of arts.

Notes

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1 Kuznets (1988) has argued that any economic development model must have the following attributes: a significantly above average growth rate, the existence of a country whose performance conform to the model, an explanatory power of rapid growth, and being a reasonably replicable one.

2 One of most notable examples is the publication by the World Bank (1993).

3 http://graphics.eiu.com/PDF/Democracy_Index_2010_web.pdf/.

4 Botswana depends on a single item—diamond mining—which accounts for more than one-third of GDP, 70–80 percent of export earnings, and about half of the government's revenue (CIA World Factbook, http://www.cia.org). Oman also depends heavily on the petroleum sector. Crude oil has accounted for over 30 percent of GDP since 1980. Revenues from the sector have grown to represent roughly two-fifths of GDP in recent years (Encyclopedia Britannica, http://www.britannica.com).

5 For instance, Korea could build one of the greatest and most efficient steel mills in the world without having raw materials at home. Again, Korea re-exports petroleum products to the world including the Middle Eastern countries after refining the imported materials. In fact, petroleum products in recent years are one of the greatest export items in Korea, the volume of which is comparable to electronics.

6 The selection of Rwanda is based on the author's personal experiences of working for the government as an economic advisor in 2006–2009 at the Office of the President and at the Ministry of Commerce and Industry.

7 One of most popular subjects of technical cooperation Korea then offered was the "Saemaul Movement," a nationwide operation of integrated rural community development strategy.

8 *African Statistical Yearbook 2010*, jointly published by the African Development Bank, UN/ECA, and African Union Commission.

9 One of most well-known examples of this kind is the IMF's policy recommendation of high interest rates in the aftermath of the East Asian foreign exchange crisis in 1997. The IMF imposed the option against skepticism over the conditionality raised by many local economists. It then resulted in a widespread unemployment which further aggravated the economic situation.

10 Todaro and Smith (2011).

11 In economics circle, four elements are generally regarded as the most influential factors in Korean economic development, such as high investment rates, labor market competition, export orientation, and a strong interventionist government (Kuznets, 1994).

12 East Asian success stories in Colin Bradford (1986) characterise that it is not the dominance of market forces, free enterprise, and internal liberalization that determines the success of economic development. Rather, embodiment of effective and highly interactive relationships between the public and the private

sectors characterized by shared goals and commitments are crucial in the development strategy and economic policy of government. It is the degree of consistency. A coherent development strategy was not only formulated but followed by both the government and the private sector in providing an unusual degree of common direction to national energies in these cases.

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11 The relationship between aid and economic growth

What aid strategy should the Government of Uganda promote?

Lawrence Kiiza[*]

1 Introduction

Attempts to correlate increases in aid with economic growth have persisted in research and policy circles for over five decades to justify foreign assistance from rich to poor countries. While the vast majority of studies find no causal connection between them, some argue that there is a correlation between aid and growth for certain countries having strong policies and institutions. It is this argument that has the greatest significance for Uganda's aid infrastructure in today's socio-economic climate. Uganda has come a long way from the aid-dependent post-civil war economy of the late 1980s, where aid levels once reached 30 per cent of GDP (Roberts and Fagernas, 2004). Pertinent questions have to be raised that take into account the improved level of economic development and institutional capacity of Uganda. Now that Uganda is on a sustained economic growth path with relatively sound fiscal, monetary and trade policies, will increasing aid flows have an important impact on growth? Or, is there a point of diminishing returns? Should different types of aid be mobilised to respond to the changing socio-economic climate in Uganda? These are the kinds of questions that the Government of Uganda should be considering in its aid negotiations with development partners.

This chapter will not attempt to directly address the question on diminishing returns from aid, given the complexities in this debate,[1] nor will it examine the wider macroeconomic impact of aid on growth through money supply and exchange rate appreciation (Mugume, 2007). Instead, the main aim will be to assess the possible growth impact of two contrasting bilateral donors based on the composition of their aid, in the context of Uganda's Poverty Eradication Action Plan (PEAP).[2] Section 2 will revisit the evolution of the literature on aid and economic growth, highlighting the ongoing perceptions and misconceptions related to this debate in the context of Uganda. Section 3 will draw on the findings of the literature and test the applicability of the findings through case study analyses of the UK and Japan. The UK is characterised by a sustained approach to General Budget Support

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and institution-based project support, whereas Japan is characterised by project support largely channelled through technical cooperation and tied aid (aid linked to the purchase of goods and consultant services from the source country) in the areas of investment and productivity enhancement. The chapter concludes that despite the UK's adherence to the aid effectiveness agenda as outlined by the Paris Declaration of 2005, Japanese support, which diverges from this agenda, is more targeted towards stimulating short-term economic growth based on the ethos of the East Asian model of development.

Regarding the methodology, case studies were conducted to highlight the magnitude of research in this field. For Uganda country statistics, specific primary and secondary sources are utilised from the Ministry of Finance, Planning and Economic Development (MFPED) and the Uganda Bureau of Statistics (UBOS). The aid data for the UK and Japan are based on official data that form part of the external resource envelope for the Medium Term Expenditure Framework (MTEF) process. In addition, primary evidence was obtained through direct missions by the respective development partners and through individual interviews.

A few caveats should be noted regarding the analysis in this chapter. First, given the multiplicity of the variables in question, simplifications have been unavoidable when assessing linkages between aid flows and growth effects. The complex arrangements of aid flows have been interpreted as one-dimensional, blurring distinctions between the macro and micro impacts that aid has on the economy, although the distinctions have been made where possible. Second, individual project interventions have not been scrutinised for their specific impact on economic growth through consumption, savings or export growth, but instead classified into growth- or non-growth-enhancing areas based on donor investment. This is because the problem of assigning causality of economic growth in a specific geographical area to an individual aid intervention is complex due to the multiple interventions across Uganda, implying the existence of a macro bias in the analysis. Third, the issues of inequality and sustainability have not been addressed, largely because of the inconclusive debates surrounding predominantly growth-led strategies and the non-economic factors that can impact these issues.[3] Finally, it has to be stressed that while the focus of this chapter is economic growth as opposed to other areas of a comprehensive development framework, there is no intention to suggest that growth has priority over other areas such as human development or the promotion of democracy.

2 Literature review

For over five decades a continual game of 'ping-pong' has taken place in forums for research and policy in an attempt to find a tangible link between increased levels of aid and economic growth. The below summarises the main contemporary debates, focusing on Uganda where possible. In sum, the link remains tenuous, although researchers have started to explore different angles that have important ramifications for Uganda's present economic and institutional climate.

Paradigm 1: An aid-financed 'big push'

The 'big push' argument holds that a large inflow of aggregate aid in social and productive sectors will result in growth across all sectors of society. This is originated from the Jeffrey Sachs school of thought and is based on the theory of a 'poverty trap' and consistent low productivity, which prevent poor countries from growing. The big push argument has caught the interest of policy groups and governments and has taken shape through initiatives such as the United Nations Millennium Project, which advocates high concentrations of aid to specific geographical areas, and the International Finance Facility, which proposes the frontloading of aid from rich countries to meet the Millennium Development Goals (MDGs) and the Gleneagles G8 pledge to double aid to Africa by 2015. The rationale is quite simple, specifically that the poorest sections of society are too poor to save for the future and are therefore prone to becoming trapped into low or negative growth rates. Large increases in aid through multiple organisations such as NGOs, government and the private sector would finance a big push in public investment and increase Africa's underlying productivity through human, agricultural and industrial development to lift people out of this trap (Sachs, 2005). The big push approach is characterised by a holistic approach to improving the lives of the poor, utilising various forms of foreign aid and delivering a plethora of projects and programmes to enable the attainment of intended goals.

The big push argument is compelling, especially in countries where governments have failed to invest in needed public investment and private alternatives have not been ready to invest sufficiently. On a macro scale, historical aid trends to Sub-Saharan Africa have totalled US$2.3 trillion over the past five decades, and yet the growth outcomes expected with this 'big push' have failed to come about. Data for 22 African countries from 1970 to 1994 show that US$324 billion was spent on public investment, US$187 billion of which was provided by donors, yet growth rates during this period failed to take off as the big push theory predicted (Easterly, 2006). Of course, it is very difficult to single out whether ineffective government utilisation or ineffective aid delivery is to blame for this dismal trend. Nevertheless, the sheer quantity of financial flows seriously brings into question the idea that a second influx of money would reverse this trend, not to mention whether the institutional capacity exists to absorb such increases.

In a revolutionary study Boone (1994) directly addressed the big push theory. His conclusions were that while large aid inflows create micro-level increases to the consumption patterns for poor households, this had no

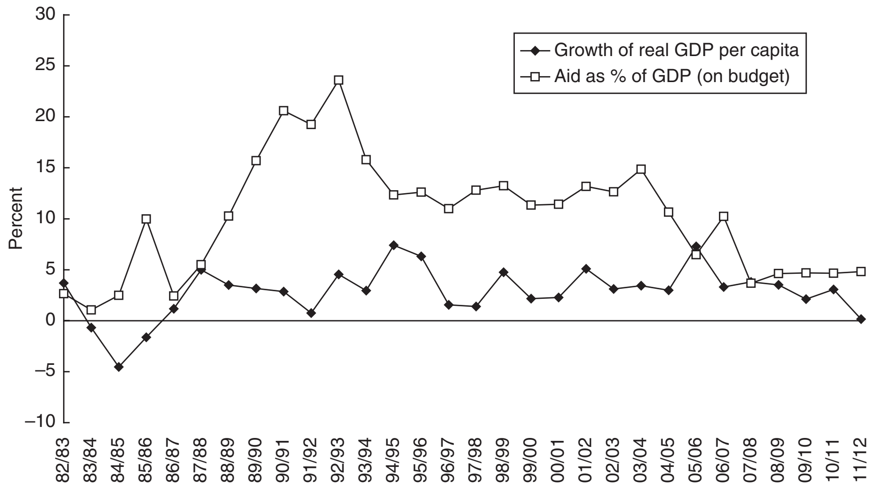

Figure 11.1 Aid and growth in Uganda

Sources: The Uganda Bureau of Statistics, and the *Background to the Budget*, various years.

impact on financing investment and growth. This study therefore proved that the big push theory had serious flaws regarding its claims of society-wide transformation. Similarly, in a cross-country study of 137 of the world's poorest countries between 1950 and 2001, Easterly (2006) tested the per capita growth increase after dividing these countries into two groups, namely those that received above-average foreign aid and those that received below-average aid. No difference was found in the growth rates between the two sets of countries, a finding that again seriously brings the big push argument into question. That said, are these big push findings applicable to Uganda? Figure 11.1 shows that the link between growth and aid is weak to non-existent in Uganda.

The figure gives a snapshot of the correlation between aid and growth in Uganda for the significant inflow of aid received since 1986. It does not represent the impact of vast population growth, the Government of Uganda's focus on stability before growth (outlined in Chapter 8 of the PEAP) or the trade-off between growth and equity, for example through the provision of public goods such as universal primary education. Nevertheless, it does raise some interesting questions given that there still exists a general consensus among development partners in Uganda that more aid will enhance growth. Jeffrey Sachs himself on a recent visit to Kampala stated that Uganda could only attain the MDGs targets through increasing donor support to finance initiatives such as the Millennium Development Villages, which rely on per capita funding of US$110 provided by the United Nations Development

Programme and private philanthropists.[4] This approach has become vastly popular in policy circles, despite coming under increased scrutiny for doing little to trigger individual initiative or the growth impact of small-scale entrepreneurial enterprises (Easterly, 2006). Moreover, the inflated unit costs to sustain a big push approach raises concerns of continued financial wastage that have been highlighted to date in Uganda (MFPED, 2004).[5]

Paradigm 2: Aid works in a good policy environment

Realising the shortfalls of the big push approach, a second paradigm emerged which argues that aid works in countries where institutional and macroeconomic frameworks are conducive, namely with good fiscal, monetary and trade policies (Burnside and Dollar, 2000). The authors implicitly addressed the issue of good governance in their study, outlining how aid can either be invested for productive means or consumed by recipient governments in an unproductive way. These findings were well received within policy circles, most notably by the World Bank and the US government. The latter subsequently announced a US$5 billion increase in foreign assistance to be administered by the Millennium Challenge Corporation (MCC). As a result, Uganda received US$10 million for being a 'good policy' country, as the Government of Uganda scored highly in the index of institutional quality established by the MCC.

According to follow-up studies, increased aid has had the growth-enhancing and poverty-reducing impact for the Government of Uganda's fiscal framework through the expansion of the development budget (Roberts and Fagernas, 2004). The findings demonstrate that a combination of increased aid coupled with specific progressive domestic reforms, namely tax administration reform, consistent cash budgeting through the Poverty Action Fund (PAF) and a medium-term consultative budget process, produced beneficial results for growth and poverty reduction.

This 'aid works in a good policy environment' argument certainly seems convincing and to a large extent fairly logical as it portrays aid as an investment, which impacts domestic output in either a positive or a negative way. However, the argument seems to contain a number of oversimplified areas that need to be investigated further. For example, the assumption that all aid to the development budget has had a productive impact is contrary to the recent analyses that break down the composition of expenditures between consumption (seminars and workshops, consultants' wages, technical assistance, and so on) and real investment in social or economic reform programmes. This composition has been referred to as unproductive and productive spending by the World Bank (2007b). MFPED (2007) has provisional estimates that the consumption element of the development budget for 2006/07 could be as high as 45–50 per cent, suggesting that not all of the aid received was reaching the intended growth-enhancing target. Instead, much of it was used on recurrent costs, which are now being scrutinised with respect to their effectiveness. This raises questions about what factors actually contributed to Uganda's growth over the period in question.

In addition to the above criticisms, there remain serious questions regarding endogeneity, in that governments with sound macroeconomic policies are conducive to growth enhancement independently of aid flows. Historical case studies certainly add weight to this argument. The most known cases of development transition from low- to high-income countries with steady progress in poverty reduction and growth have been the Asian tigers of Hong Kong, Korea, Singapore and Taiwan, each of which developed using an effective combination of home-grown industrial and trade policies, coupled with targeted loans from neighbouring Japan to develop basic industries and export facilities. This subsequently shifted their comparative advantage in the global economy. During their growth trajectory these countries were in the bottom quartile for Least Developed Countries (LDCs) in terms of aid receipts as a proportion of their income. They did not qualify under the category of 'good institutions' outlined by Burnside and Dollar, especially with regard to an open trade policy and good governance (Khan and Jomo, 2000).[6] Despite sceptics claiming the same is not possible in Africa, Botswana has followed a similar approach and has registered the world's highest per capita growth rate from 1960 to the present with little to no dependence on foreign aid.

Paradigm 3: The type of aid matters

Given the continual failures to establish a feasible link between aggregate aid and growth,[7] the debate has recently been re-ignited in research forums from the perspective of aid effectiveness prescribed in the Paris Declaration (OECD, 2005). Clemens et al. (2004) found that different types of aid modality and the composition of aid could have distinct growth impacts. More specifically, budget support or balance of payments support on the one hand, and project aid given for infrastructure and productive investments including transport, communications, energy, agriculture and industry on the other, are likely to have 'short-term growth impact', while technical cooperation and most social sector investments, including education, health, population control, environment and aid to support democracy, would have 'long-term growth impact'.[8] Stating that because of this heterogeneity in aid flows, previous studies failed to find a causal relationship, they claim that if this methodology is used, the growth impact of aid is found to be at least two to three times larger than that found in previous studies that used aggregate aid. Moreover, they found that higher than average short-impact aid to Sub-Saharan Africa raised per capita growth rates there by about one percentage point over the growth that would have been achieved by average aid flows. Institutions and domestic policy do play a positive role; however, short-impact aid will lead to economic growth even in countries with weak institutions.

Not surprisingly, given the ambiguity of the categorisations, the study was subject to criticism in research circles. Despite the criticism, it did shift the aid and growth debate into the realm of aid effectiveness. This study was closely followed by similar work by Rajan and Subramanian (2005), who, while criticising the findings of the study by Clemens et al. (2004), shed light on reasons why foreign aid does not cause growth, through their analysis of tied aid and aid for political reasons, which also may limit the effectiveness of aid. Hence, the authors concluded that although historic data fail to provide a strong link, this does not imply that aid cannot be improved in the future in terms of how it is delivered, to whom, in what form and under what conditions. Their findings therefore strongly support efforts underway to improve aid effectiveness.

Summary and lessons learned from the literature

To summarise this section, the aid and growth debate has experienced three paradigm shifts, all of which have failed to find a causal link between more aid and increased economic growth. The first paradigm shift was based on growth rates increasing through a 'big push' in aid flows to supplement public investment and stimulate rural and urban productivity. The second was along the same lines, but assumed that growth would increase only when aid was channelled to countries with sound fiscal, monetary, trade and governance policies. Serious concerns were raised in adopting these approaches, based on historic aid inflows to Sub-Saharan Africa that have failed to meet the objectives of raising economic growth or substantially reducing poverty levels. Despite the attempts of skilled econometricians, it is impossible to determine whether growth rates would have been any different without the aid that has been received. Both paradigms were criticised through statistical research and, more importantly, in the Ugandan context. The final paradigm shift directly addressed the issues of aid composition and, more specifically, how the effectiveness of aid can impact the subsequent growth effect. Cross-country research has produced contrasting findings in this new area, which is still to a large extent not covered in the literature.

Is there anything that Uganda can learn from the extensive research in this area? The general answer is yes. This is mainly because debates appearing in the literature are still strongly reflected in the actions of the donor community today. Development partners have contrasting viewpoints as to how aid is best spent and administered in Uganda. Some believe that a 'big push' in all areas is necessary to achieve sustainable development through a diverse mix of NGO, government and private sector-based programmes (as advocated by UN agencies and the United States Agency for International Development (USAID)). Others argue that institutional strengthening is of primary importance to administer budget support for sustainable impacts (as proposed by Uganda Joint Assistance Strategy donors), whereas a final group believes that investment in key growth-enhancing areas such as roads, energy and agricultural transformation is essential (as argued by the World Bank, Japan, Norway, Germany and China).

The existing aid and growth debates mostly use aggregated total aid and rely on cross-country growth regressions, which have well-known shortcomings in identifying causal linkages between aid and growth. As a result, they fail to capture the complexity and heterogeneity of aid flows (Rodrik, 2005). Because the time period of their analyses spans from the 1950s to the present, they also fail to account for changes in foreign aid flows over the past two decades resulting from the end of the Cold War, the shift from Structural Adjustment to Poverty Reduction Strategy Papers (PRSPs) and, most importantly in the context of this chapter, developments in the aid effectiveness agenda. In light of this, a more detailed microanalysis of aid strategies performed by specific donors can help the Government of Uganda determine how these approaches should interplay with domestic growth strategies during aid negotiations. The case study section that follows will attempt to do this by analysing two frameworks that build upon the third paradigm of the literature, specifically the aid effectiveness agenda and the composition of specific aid flows to determine the possible growth impact.

3 Case study analysis

This section will compare the aid strategies of two bilateral donors in Uganda, namely the UK and Japan, building upon the third paradigm presented in the literature review. First, several indicators from the Paris Declaration on Aid Effectiveness (OECD, 2005) will be used to rank the performance of the two donors in terms of possible linkages towards economic growth. Second, a comparative analysis will be made on the composition of their assistance based on the PEAP pillars and priority sectors of MTEF. The current PEAP is built on five pillars: (1) economic management; (2) enhancing production, competitiveness and incomes; (3) security, conflict resolution and disaster management; (4) good governance; and (5) human development. In addition, the project portfolios of respective donors will be analysed in light of their consumption- or investment-orientation and the time scope of their growth effects (i.e. short-term or long-term growth effects).

In doing this, several assumptions have been made as follows.

- Transaction costs for government distort efforts to manage the economy efficiently.
- Nationally owned strategies have more effective outputs than other strategies.
- Aid is more growth-enhancing when it is targeted at pillar 2 of the PEAP through productivity-enhancing measures. It will be assumed that this has a greater short and/or medium impact on aid as compared to other PEAP pillars, which are more indirectly associated with growth, and therefore has a longer-term impact.

- Investment is assumed as a physical tangible investment and takes precedence over intangible investments such as human development and capacity building.

Comparing the UK and Japan using aid effectiveness indicators[9]

This section develops the findings of Rajan and Subramanian (2005) as mentioned in the third paradigm. They argued that efforts underway through the aid effectiveness agenda can have a benign effect on the impact on growth, primarily depending on the way it is delivered. Table 11.1 sets out a series of possible linkages between aid effectiveness targets and economic growth, built on the notion that high transaction costs distort the effectiveness of government in creating a necessary framework to foster private sector-led growth. Table 11.2 then measures each of these indicators for the UK and Japan based on their current and medium-term aid portfolios (2000–10) and their respective aid mandates in Uganda.

As Table 11.3 shows, adherence to the Paris Declaration is of higher importance to the UK than it is for Japan. The UK has taken the lead in the donor community with respect to strengthening ownership of the national budgeting process through proportionally large General Budget Support commitments. Similarly, strong political will in providing budget support aid, basket funding and untied aid makes the UK a prominent figure in Uganda's aid effectiveness agenda. Japan on the other hand only adopted its Official Development Assistance (ODA) charter in 1992 and since then has made continuous efforts to establish its own aid philosophy, which differs from the commitments to the Paris Declaration (Ishikawa, 2005).

Comparing the UK and Japan by aid composition

The aim of this analysis is to highlight the proportion of aid that is targeted towards growth-enhancing activities. This is conducted in three ways. First, it is done by decomposing the current project portfolio of both donors in accordance with PEAP objectives. Second, projects are divided into consumption and investment categories, as in Clemens et al. (2004).[10] Third, projects are sub-divided based on the time scope of growth impacts: short-term, long-term or no growth impact, also using the methodology of Clemens et al. (2004). The full list of projects and categories can be found in the Appendix. The analysis excludes the effect of General Budget Support because of the difficulty in separating it from the effect of the Ugandan government's domestic policy. This is further complicated by the fact that Uganda's strong macroeconomic performance had begun before General Budget Support was considered (OECD, 2006).

The results in Tables 11.4 and 11.5 demonstrate how Japanese project aid is more growth-oriented than that of the UK. The largest share of its current project portfolio (40 per cent) is geared towards enhancing

Table 11.1 Selected Paris Declaration Indicators localised for Uganda

Paris Declaration commitment	*Implications for donors and Government of Uganda*	*Benefits for Government of Uganda*	*How these benefits could be linked to economic growth*
Ownership (Indicator 1)	Recipient ownership of national poverty reduction strategy linked to the MTEF.	Single national policy and expenditure programme to promote government leadership.	Ownership ensures a greater desire to achieve objectives and results so aid money is spent efficiently.
Alignment to National Policies (Indicator 2)	Aid flows are aligned to national priorities.	Focused goals and objectives targeted towards priority areas that support service delivery by government.	Alignment can reduce duplication and wastage of projects, therefore encouraging efficiency.
Predictability of Aid (Indicator 7)	Disbursements are released in accordance with agreed schedules to meet MTEF planning requirements.	Enhanced budgeting mechanisms for better and more predictable future planning.	Investment and spending plans can be utilised in productive areas without disbursement delays.
Aid is Untied (Indicator 8)	Contracts for the purchase of goods and hiring of consultants are not linked to the host country.	Allowing goods and services to be procured competitively in the recipient country.	Local resources can be used to generate employment and wealth creation.
Harmonisation (Indicator 9)	Aid flows and activities are harmonised in accordance with Sector Investment Plans (SIPs) and PEAP priorities.	Reduced transaction costs through coordination of aid delivery with government programmes to avoid duplication.	Harmonised donor activities reduce the transaction costs for government (reporting, missions, etc.). This extra capacity can be used in productive areas.

production, competitiveness and incomes (PEAP pillar 2). Almost half of its project assistance has a short-term impact on economic growth based on the definitions by the study of Clemens et al. (2004) and a quarter is investment-oriented. This is equally represented in the share of aid disbursements, with agriculture, roads and Economic Functions and Social Services (EFSS) obtaining the greatest shares, in addition to the heavily supported

Table 11.2 Performance of UK and Japan on aid effectiveness

Paris Declaration commitment	*Aid effectiveness indicator*	*UK*	*Japan*
Ownership (extent to which aid is provided according to PEAP priorities)	Percentage of total aid allocated through budget support.	Around 50% of total aid from 2000 is through budget support. This level is to be maintained in the medium term.	All project aid (technical assistance and grant aid) is derived through sector priority areas. Currently, no budget support is provided.
Alignment to national policies	Percentage of total aid that is recorded on budget.	70% on average (2002/03–2008/09).	35% on average (2002/03–2008/09).
Predictability of aid	Percentage of aid released according to agreed schedules.	Predictability of budget support was 100% from 2000/01–2004/05, but reduced for the first time following the 2006 elections. Project performance has been consistently high in 2004/05 and 2005/06, at 86% and 74%, respectively.	Recent disbursements are significantly higher than what is allocated in the MTEF. In 2006/07, for example, disbursements were 137% of the commitment. Two significant projects in 2007/08 are expected to triple the MTEF allocation for this year.
	Flexibility in MTEF planning (level of decentralisation).	UK operates on a fully decentralised system and negotiations are underway for the implementation of ten-year horizons for development assistance. Such horizons are currently in use for several other countries in which the UK operates.	The Ministry of Foreign Affairs plays a central role for aid allocations, limited to a one-year forecast horizon. The primary reason for Japan's unpredictable aid flows is that its project approval is bound by the annual budget cycle, making it difficult to accommodate the MTEF cycle.

Table 11.2 (*cont.*)

Paris Declaration commitment	*Aid effectiveness indicator*	*UK*	*Japan*
Aid is untied	Percentage of aid that is tied.	All aid is untied, as mandated in the 1997 and 2000 DFID White Papers.	Grant aid and technical assistance are fully tied although the proposed Japan Bank for International Cooperation (JBIC) loan (1st in Uganda) is untied.
Harmonisation to sector investment plans and PEAP priorities	Percentage of aid received through programme-based approaches[1] and/or basket funding.	The share of programme-based approaches for 2005/06 is 73%.[2] All on-budget project assistance is channelled through basket funding with other donors to limit transaction costs for the Government of Uganda.	The share of programme-based approaches for 2005/06 is 51%.[3] Requests for grant aid and technical assistance are derived from sector ministries. Apart from off-budget humanitarian assistance (channelled predominantly through UN agencies), no basket funding is provided for central government aid flows.[4]

Notes:
1. These are defined as coordinated support for a locally owned programme such as a national development strategy or a sector programme. Programme-based approaches share features of: a) leadership by the host country; b) a single comprehensive programme and budget framework; c) a formalised process for donor coordination and harmonisation of donor procedures for reporting, budgeting, financial management and procurement; and d) efforts to increase the use of local systems for programme design and implementation, financial management, monitoring and evaluation (OECD, 2005).
2. OECD (2007).
3. See Note 2 above.
4. This excludes Japanese assistance to the Financial Management Accountability Programme (FINMAP), which remains unsigned at the time of writing.

Table 11.3 Summary of aid effectiveness performance

Paris Declaration commitment	*UK*	*Japan*
Ownership	Good progress being made	Some progress being made
Alignment	Good progress being made	Some progress being made
Predictability	Good progress being made	Some progress being made
Aid untying	Good progress being made	Little or no progress made
Harmonisation	Good progress being made	Some progress being made

Source: Assembled by the author, based on Tables 11.1 and 11.2.

Table 11.4 Composition of UK and Japanese project aid: classification by Poverty Eradication Action Plan (PEAP) priorities

PEAP pillars	*UK*	*Japan*
Pillar 1: Economic Management	17%	—
Pillar 2: Enhancing Production, Competitiveness and Incomes	17%	40%
Pillar 3: Security, Conflict Resolution and Disaster Management	7%	25%
Pillar 4: Good Governance	25%	—
Pillar 5: Human Development	24%	35%
Multiple	10%	—

Notes:
1. Based on the information on project aid (on- and off-budget) for 2000–10 for the UK and for 2003–09 for Japan.
2. Japanese aid for pillar 3 is delivered through the UN system.

Table 11.5 Predicted impact of aid on economic growth: UK and Japan

	UK	*Japan*
Growth impact of project aid		
No impact	7%	5%
Short term	12%	45%
Long term	81%	50%
Consumption/investment ratio		
Investment	19%	25%
Consumption	81%	75%

Source: Estimated by the author, based on the tables in the Appendix.

Notes:
1. The percentages reflect the number of projects in a given category as a proportion of the total projects in the respective portfolios shown in the tables in the Appendix.
2. The growth impact for each project is estimated using the methodology from the study by Clemens et al. (2004) and utilising Development Assistance Committee (DAC) classifications of aid categories.

hospital rehabilitation programme, which skews the figures for the health component. For example, in 2006/07 Japanese disbursements to agriculture, roads and health sectors accounted for more than 90 per cent of its total disbursements. From 2007/08 the share of EFSS has been increasing.

The UK perspective is completely the opposite. The major share of support has been seen and will continue to be in the area of good governance with accountability, public administration and public sector management featuring prominently. Specifically, the share of UK disbursements to the accountability sector has increased since 2004/05. It is projected that from 2007/08 the accountability sector will account for almost half of the total disbursements. This is hardly surprising given that institutional strengthening is supposed to be a by-product of General Budget Support and not a productivity-enhancing measure. Eighty per cent of project assistance could have possible long-term growth effects and the same amount is consumption-based, due to a high level of capacity building projects.

4 Discussion and analysis

Results above indicate that the UK performs better when judged on the Paris Declaration Indicators, whereas the composition of Japanese aid is more focused towards increasing productivity, investment and, subsequently, economic growth. The findings show that the composition-based results offer a more robust insight into a possible growth impact with respect to the PEAP pillars, disbursements into MTEF sectors and the consumption-to-investment ratios.

Aid effectiveness and growth

The main point of analysis here is the extent to which the aid effectiveness agenda can assist economic growth through reduced transaction costs, increased country ownership and policy alignment. The UK is leading the way in the aid effectiveness agenda. It is also undeniable that country ownership is imperative to ensure that aid money is better spent. However, it is becoming increasingly difficult to judge whether and how much adherence to the aid effectiveness agenda will contribute to productivity increase. The linkage at best remains weak as too many interplaying variables remain, making it impossible to conclude that the aid effectiveness agenda will lead to economic growth. It is yet to be seen, for example, whether or not basket funding leads to reduced transaction costs, given that the process is in its infancy. It is therefore uncertain as to how much reduction in transaction costs will free up greater resources within the Government of Uganda to steer the economy along a more efficient growth path.

Furthermore, the Paris Indicators only give a small representation of a donor's activity in a developing country, as understandably all results-oriented systems have shortfalls. For example, although the majority of Japan's project aid is in the form of technical assistance, it is proportionally outstripped by Japan's assistance to humanitarian relief, therefore giving an unbalanced picture of on- and off-budget aid. More importantly, the indicators used fail to capture Japan's 'request-based' approach that strongly supports country ownership. This is demonstrated by the joint pre-discussions regarding technical assistance and grant aid to identify need, which subsequently strengthened policy dialogue with the Government of Uganda in determining the allocation of aid. Japan's assistance has minimal to no conditionalities.[11] This approach was built on lessons learned from aid relationships with East Asian neighbours, in which mutual trust was established when Japan provided aid without attaching conditionalities (Ishikawa, 2005).

Composition of aid flows

The analysis of the composition of aid flows offers a clearer indication on growth orientation of a specific donor as compared to the aid effectiveness study. This gives credit to the methodology of the study by Clemens et al. (2004) and to a lesser extent supports the conclusions of Rajan and Subramanian (2005). This analysis is certainly not free from criticism. The omission of General Budget Support from the analysis makes a comprehensive cross-country comparison incomplete. Similarly, subjective outcomes were at times employed in order to predict a short- or long-term growth impact. Nevertheless, the project portfolios of respective donors, i.e. their composition and disbursement data, offer strong evidence of their underlying thinking: while the UK clearly follows institutional strengthening in areas of good governance, Japan adheres to a more growth-led development strategy based on historical commitments to East Asian neighbours.

This is not to render the aid effectiveness agenda ineffective—far from it. The primary aim of the aid effectiveness agenda is to reduce wastage and burdensome bureaucracy for the recipient, and to a lesser extent to result in direct productivity gains. The findings of this study are simply from a growth perspective, whereas the aid effectiveness agenda is multifaceted and aims primarily to evaluate donor performance in aid delivery. If anything, the findings simply tell us that different donors have different perspectives. The Government of Uganda should be fully aware of these perspectives at the negotiating table.

Implications

These findings raise a number of questions that centre on the extent to which poverty reduction is achieved through economic growth. Both the UK and Japan hold that 'economic growth is the single most powerful way of pulling people out of poverty' (DFID, 2006, p.57). Nevertheless, the case study analysis shows a divergence in the approaches donor countries take to accomplish this goal. The UK believes that effective states, which are accountable to their citizens, create more stable investment climates to foster long-term growth. Hence, developing systems of accountability—audit institutions and parliamentary committees, among others—will promote this environment. Japan, on the other hand, is a strong believer in aid for trade, whereby concessional loan-based support is injected into public funds to promote economic infrastructure development[12] that is initiated by external private sector development, as experienced with China, Korea, Thailand and more recently with Vietnam. Poverty reduction through growth has been achieved by targeting rural areas to lower unit costs of inputs such as fuel, electricity and phone bills. This subsequently improves access to markets and competitiveness of existing and potential firms to stimulate employment generation. This is a critical first step in increasing FDI, leading to greater exports and subsequent economic growth.

So what do these contrasting aid strategies mean from the perspective of the Government of Uganda? The findings have several implications, and in many ways raise more questions than answers. First, should the Government of Uganda be promoting an agenda based on Japanese assistance, which is based on 'growth first' empirical results from East Asia and Botswana? To what extent does institutional development matter in the context of aid policy? What additional priority areas should be targeted beyond infrastructure development? Of course there is no clear-cut answer to these questions and aid policy must be balanced to address all of these areas, especially given that institutional development is based on the notions of self-help and sustainability, which are the underlying principles upheld by the Government of Uganda. In addition, initiatives are needed to ensure that investment leads to employment generation. This is dependent upon sufficient regulation and accountability.

In light of a recent budget speech by the Minister of Finance, Planning and Economic Development on 14th June 2007 (MFPED, 2007), which prioritised rural development, increasing competitiveness, productivity and access to rural finance, it appears that the Japanese model is more attuned to the Ugandan government's way of thinking: to stimulate home-grown development based on the dynamism of individuals, firms and free markets, as opposed to relying on foreign aid. Moreover, despite having experienced poverty reduction and economic growth over the past 20 years, the economy remains largely infrastructure constrained, with economic growth outstripping road and energy infrastructure, a situation which is clearly highlighted by the congestion around Kampala and power shortages (World Bank, 2007a).[13] Japan's strategy directly aims to overcome this infrastructure constraint, so as to remove these barriers to growth. Given that aid flows have historically been linked to a plethora of areas advocated in the PEAP, the Government of Uganda is now faced with re-considering future allocation and modalities of aid flows so as to reflect these pressing priorities. This does not imply that social sectors and institutional strengthening are to be ignored, but the current concentration of off-budget aid flows in these areas (ODI, 2008) could signal a needed shift towards a growth-led model. Currently, the World Bank and the African Development Bank dominate this area of support through concessional loans, with the EU and to a lesser extent Denmark and Norway providing support through grant aid. With greater consensus and support among other donors, a concerted drive could produce results like those experienced in Southeast Asian countries such as Vietnam.

As the big push theory appears to be coming to the fore, the Government of Uganda must first fully comprehend the aid composition of its leading development partners. The government must be in a position to dictate where and how aid is spent so as to promote the intentions laid out in the recent budget speech. This position should come hand-in-hand with the government pushing for the aid effectiveness agenda. Without such leadership, aid is at risk of being used inefficiently; much has been squandered in the past, and such handling of aid will only fuel aid dependency and a culture of handouts as opposed to one of investment-led growth. As the time approaches for the Government of Uganda to revise its development strategy, recommendations could be to prioritise among the PEAP pillars so as to give more weighting to growth-enhancing areas and incorporate a harmonised investment productivity and savings strategy to draw specific donor support. Such an adjustment is especially important because the social and governance areas have had an overabundance of donor aid inflows in the recent past.

Appendix

Table 11.A1 Detailed breakdown of DFID's project portfolio (2000–10)

MTEF sector	*Project name*	*PEAP pillar*	*Investment/ consumption*	*Growth impact*
Agriculture	Aquaculture in Uganda / Fish Farming	2	Investment	Short term
	Support to Plan for Modernisation of Agriculture Secretariat	2	Investment	Short term
	Improving Rural Livelihood (NARO) (TA)	2	Consumption	Long term
Education	Education Sector Programme (ESIP)	5	Investment	Long term

Table 11.A1 (*cont.*)

MTEF sector	*Project name*	*PEAP pillar*	*Investment/ consumption*	*Growth impact*
Health	Health Planning Unit Project (TA)	5	Consumption	Long term
	Support to Water & Sanitation Programme / Environment Health Division	5	Consumption	Long term
	Support to Malaria Control and Prevention	5	Consumption	Long term
	Uganda Aids Commission	5	Consumption	Long term
	Partnership Fund Project	5	Consumption	Long term
Accountability	Financial Accountability Programme (Financial Aid)	4	Consumption	Long term
	MFPED Economic Advice	1	Consumption	Long term
	Support to Ministry of Finance	1	Consumption	Long term
	Public Financial Management (FINMAP)	4	Consumption	Long term
	Evidence Based Decision Making (MFPED)	1	Consumption	Long term
	Support to Uganda Bureau of Statistics	1	Consumption	Long term
	Evidence Based Decision Making (UBOS)	Multiple	Consumption	Long term
	Population Census	Multiple	Consumption	Long term
	Support to Privatisation Utility Reform	1	Consumption	Long term
	Deregulation	1	Consumption	Long term
	Poverty Monitoring & Policy Analysis	Multiple	Consumption	Long term
	Anti Corruption Support	4	Consumption	Long term
	Democratic Deepening Project	4	Consumption	Long term

MTEF sector	*Project name*	*PEAP pillar*	*Investment/ consumption*	*Growth impact*
Economic Functions and Social Services (EFSS)	Evidence Based Decision Making	Multiple	Consumption	Long term
	Uganda Revenue Authority	1	Investment	Short term
	Decentralisation Support Programme	4	Consumption	Long term
	Support to National Forestry Authority	2	Consumption	Long term
	Pilot Cash Transfer	N/A	Consumption	Long term
Justice, Law and Order Sector (JLOS)	Commercial Justice System Reform	4	Consumption	Long term
	Law Revision/Printing	4	Consumption	Long term
Public Sector Management	Public Service Reform Program	4	Consumption	Long term
Public Administration	Support to Parliament (through Strategic Fund)	4	Consumption	Long term
	Support to EU-GoU Capacity Building Programme	4	Consumption	Long term
Water and Environment	Integrated Lake Management	2	Investment	Long term
	National Water and Sanitation Programme	5	Investment	Long term
Security	Support to Defence Review Unit	3	Consumption	No impact
Off Budget Projects				
Accountability	Civil Society Programme	4	Consumption	Long term
Security	Humanitarian Aid	3	Consumption	No impact
	Conflict Reduction/ NGOs and Amnesty Commission	3	Consumption	Long term
Health	Support to Measles and Polio	5	Consumption	Long term
	HIV Umbrella Programme	5	Consumption	Long term
	Response to Meningitis	5	Consumption	No impact
Agriculture	Enhancing Competiveness of Commercial Agriculture	2	Investment	Short term
EFSS	Support to Private Sector	2	Investment	Short term

Table 11.A2 Detailed breakdown of Japan's project portfolio (2003–09)

MTEF sector	*Project name*	*PEAP pillar*	*Investment/ consumption*	*Growth impact*
Roads and Works	Improvement of Traffic in Kampala City Council	2	Investment	Short term
	Study on Greater Kampala Road Network	2	Consumption	Short term
Agriculture	Study on Post Harvesting and Marketing	2	Consumption	Short term
	Study on Sustainable Irrigation	2	Consumption	Short term
	Technical Capacity of Animal Disease Control	2	Consumption	Short term
Education	Nakawa Vocational Training Institute	5	Consumption	Long term
	Secondary Science and Mathematics	5	Consumption	Long term
Health	Rehabilitation Health Facilities Eastern Region	5	Investment	Short term
	Improvement of Health Infrastructure Development & Management	5	Consumption	Long term
EFSS	Project for Rural Electrification Phase II	2	Investment	Short term
	Bujagali Interconnection Project	2	Investment	Short term
	Medium Wave Radio Broadcasting Network	2	Investment	Short term
Off Budget Projects				
Security	Emergency Assistance to Conflict-Affected Areas	3	Consumption	No impact
	Northern Uganda Youth Rehabilitation Fund	3	Consumption	Long term
Agriculture	Cassava-Agricultural Support in West Uganda	3	Consumption	Long term
	Emergency Food Supply in Northern Uganda	3	Consumption	Long term
Health	Provision of Long-lasting Insecticide Net	3	Consumption	Long term
	Expanded Programme on Immunisation Revitalization & Polio Eradication	5	Consumption	Long term

MTEF sector	*Project name*	*PEAP pillar*	*Investment/ consumption*	*Growth impact*
	Protection and Promotion of Rights of Children in Acholi Area	5	Consumption	Long term
Multiple	Support to Grassroots Projects	5	Consumption	Long term

Source: MTEF, Ministry of Finance, Planning and Economic Development.

Notes

* All opinions expressed in this paper are the author's personal views and do not necessarily reflect those of the Ministry of Finance, Planning and Economic Development of the Government of Uganda, at which the author serves.

1 The debate has been multifaceted, but it mainly centres on the issue of reverse causality or endogeneity, i.e. natural bias, given that aid is historically provided to failing or slow-growing economies. Aid in response to an economic crisis, for example, will always yield beneficial results in the short term, but it is difficult to determine what the results would otherwise have been. A large amount of aid provided to crisis countries distorts not only the domestic efforts of the host economy, but also the ability of researchers to evaluate the performance of an increase in aid.

2 The PEAP is Uganda's Poverty Reduction Strategy Paper. The first PEAP was prepared in 1997 with subsequent revisions in 2000 and 2004. The current PEAP was approved by the Cabinet in November 2004 as the national framework for development, covering the period of 2005–08.

3 A recent study by the Asian Development Bank found that income inequality has risen in many East Asian economies, bringing into question the 'growth with equity' claims that the tiger economies proclaimed during the 1990s. Similarly, a recent independent evaluation of the World Bank cited inequality as one of the three weakest areas in its economic growth-led programmes (*The Economist*, 2007a).

4 The initiative of the Millennium Villages has been promoted by Jeffrey Sachs, who headed the independent advisory body to the United Nations Secretary-General to develop concrete action plans to achieve the MDGs. This is based on an idea that impoverished villages can transform themselves and meet the MDGs if they are empowered with proven, powerful, practical technologies through investments in health, food production, education, access to clean water and essential infrastructure.

5 A notable example of this is the health sector, where the shift from donor-funded project spending to spending through the Government of Uganda budget brought a major improvement in the allocation of expenditures towards priorities identified in the Health Sector Strategic Plan.

6 The ratios of aid to GDP from 1980 to 2002 for the Asian tigers were: Hong Kong 0.02, Korea 0.03, Singapore 0.07 and Taiwan 0.00. Taiwan and Korea had received a high level of US assistance in the 1950s and 1960s, strongly in line with policies of local technocrats that carried out land reform and export-led growth (Haggard, 1990).

7 Easterly et al. (2004) discarded the Burnside and Dollar study, using the same statistical techniques but with an extended sample. They found no evidence that aid raised growth among countries with good policies.
8 According to Clemens et al. (2004), 'short-term growth impact' aid can stimulate economic growth within a four-year period. A US$1 increase in short-term aid raises output and income by US$8 in a typical developing country. This has diminishing returns once short-term aid reaches 8 per cent of GDP. 'Long-term growth impact' aid is likely to have no relationship to growth within a four-year period.
9 The UK aid flows are those provided by the Department for International Development, and Japan's aid flows are those provided by the Ministry of Foreign Affairs and the Japan International Cooperation Agency.
10 Consumption includes the consumption of goods such as drugs for a health project, personnel financed through technical assistance or materials for information, education and communication projects. Investment captures physical infrastructure and technical assistance that leads to enhancing competitiveness in rural and urban settings, which in turn contributes to human capital development.
11 Generally, the only condition is that an exit strategy is adopted with domestic funds ensuring project maintenance and continuation to promote sustainability.
12 DAC defines this as energy generation and supply, transport and storage and communications.
13 Other characteristics that suggest this are the underemployment of secondary school graduates and the high return to capital in formal businesses that restrict the entry of new firms to compete.

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Index

Note: references to Figures and Tables appear in bold type