Review of "Dead Aid" by Dambisa Moyo

Owen Barder – March 31, 2009

Dead Aid should have been an interesting and challenging book. Moyo has an impressive background: originally from Zambia, she has degrees from Harvard and Oxford, and she has worked at the World Bank and at Goldman Sachs. As an economist from Africa, Moyo should have an important perspective on questions about whether aid works, whether it can do more harm than good, and what can be done to make it work better. Disappointingly, the book makes no useful contribution to the debate.

There are three parts to Moyo's case. She says that aid has demonstrably failed. Second, she says that aid has contributed to poverty. Third, she says that there are other, more effective ways of accelerating development.

All this is important. If Moyo is right, and we ignore her, then people will die. But if Moyo is wrong, and yet her book convinces enough people that aid should be reduced, then people will die. So we should make our best efforts to assess whether the evidence support's Moyo's arguments.

1. Does aid do good?

The foundation of Moyo's case is that aid has not worked. Her evidence for this is that many countries that have received aid have not secured economic growth and poverty reduction. She says:

> "Even the most cursory look at data suggests that aid has increased over time, Africa's growth has decreased with an accompanying higher incidence of poverty. ... So there we have it: sixty years, over US$1 trillion dollars of African aid, and not much to show for it."

So what is the answer to this paradox: so much aid given, and yet so much poverty remains?

The clue is in the word "cursory". If you took a cursory look at health spending, you would find something similar. The United States spends more than $2 trillion a year on health care. Despite all that spending, many Americans still get sick and die each year. What's more, the people on whom most money is spent are the ones who are most sick. More than 30% of Medicare is spent on people who die within a year. Does the correlation between health spending and sickness and death tell us that health care does not improve people's health? Only if we restrict ourselves to a "cursory" look at the data. The right question is: what would have happened to all these people without the health care they received? Would they have been more or less sick?

A cursory look at the data does not show that health care does not work. Yet it is exactly the reasoning that Moyo would have us believe about aid.

There is plenty of evidence about the benefits of aid for its most immediate beneficiaries (such as the children that go to school because aid has paid for the end of school fees) but the evidence for the overall impact on growth and development is less clear. I personally would not want to make claims about the effectiveness of aid based on what happens to economic growth in recipient countries, because the statistical power of these tests is notoriously weak.[1] But since that is the argument Moyo has chosen to use, she needs more sophisticated analysis than this. In the health care example, the logical approach is to compare what happens to people who receive treatment with people who have a similar condition but do not receive treatment. Similarly with aid, it is reasonable to ask whether there countries that get more aid do better or worse than countries that get less aid. When this kind of analysis is done carefully – by comparing growth rates in many countries over many years, and controlling for other influences such as the quality of governance, the statistical results are remarkably consistent: aid is positively correlated with growth, albeit subject to diminishing returns.[2]

Moyo is clearly aware of this literature, as she cites the finding of Burnside and Dollar that aid is positively correlated with growth, and more so in countries with good policy environments.[3] But then she casually dismisses these empirical findings:

> "It was not long before the wider economic community concluded that the Burnside-Dollar findings were tenuous and certainly not robust; perhaps eventually coming to the obvious conclusion that countries with good policies – like Botswana – would tend to make progress unassisted, and that a key point of aid is to help countries with bad one."

Moyo does not provide a single citation for the view that she attributes to "the wider economic community". More importantly, this remark shows that she has not understood the analysis. Moyo is obviously right that that countries with good policies will tend to make faster progress. But that is precisely why all the researchers – including Burnside and Dollar – have estimated the effects of aid separately from the effects of good policy. The statistical evidence, for what it is worth, is that aid is positively correlated with growth *even once you take account of the effect of good government.* So when Moyo claims that the Burnside and Dollar have mixed up the effect of good policies with the effect of aid, all it shows is that she has either not understood their analysis, or she prefers not represent it accurately.

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[1] Roodman (2007), "The anarchy of numbers: Aid, development and cross-country empirics", *The World Bank Economic Review* 2007 21(2):255-277

[2] See survey in Clemens, Radelet, and Bhavani (2004) *Counting Chickens When They Hatch: The Short Term Effects of Aid on Growth.* Centre for Global Development Working Paper No 44; Radelet (2006), *A Primer on ForeignAid*, Working paper No 92, Center for Global Development, Washington, DC.

[3] Burnside and Dollar (2000). "Aid, Policies and Growth." *American Economic Review* 90(4): 847–868; Burnside and Dollar (2004): 'Aid, Policies and Growth: Revisiting the Evidence' Policy research Working Paper 3251, World Bank, Washington]

Another example of Moyo's casual treatment of evidence is her account of a recent paper which looked at the effects of aid on growth. [4] Moyo says that the authors "concede no long term impact of aid on growth". In fact the paper was important because it was the first to distinguish aid which is intended to promote economic growth, which they call "short impact" aid, from types of aid, such as humanitarian assistance. Looking only at the impact of aid which is intended to promote economic growth over a short period, the paper finds a strong statistical relationship of the kind that Moyo denies:

> "We find a positive, causal relationship between this 'short-impact' aid and economic growth (with diminishing returns) over a four-year period. The impact is large: at least two-to-three times larger than in studies using aggregate aid. Even at a conservatively high discount rate, at the mean a $1 increase in short-impact aid raises output (and income) by $8 in present value in the typical country. From a different perspective, we find 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."

Where the evidence is inconvenient for Moyo, she prefers to sweep it aside. One often-cited African success is Botswana, which in the thirty years after independence went from being one of the poorest, most aid-dependent countries to a middle income-income country which no longer needs significant amounts of external assistance. Growth per person in Botswana averaged nearly 7% a year for more than 30 years (until it was reversed by HIV). In the 1960s and 1970s Botswana also received a large amount of aid – over 30% of GDP following independence in the 1960s, and more than 10% of GDP throughout the 1970s.[5] On the face of it Botswana appears to be a counter-example to Moyo's thesis that countries are damaged by receiving a lot of aid – though it is always difficult to know whether things would have been better or worse without aid. Moyo tells us that Botswana's success was nothing to do with aid - it was simply down to good management of the economy. She offers no account of how she has managed to establish with such certainty the ingredients that led to Botswana's success, nor any explanation of how Botswana escaped aid's curse.

It is reasonable to debate whether aid has achieved as much as its proponents claimed for it. The academic literature looking at the relationship between aid and growth does not provide a knockout argument for either the aid sceptics or the aid advocates – but this uncertainty is a weakness of this kind of statistical analysis, not an observation about aid. Furthermore, while growth is important it is not everything. There have been other benefits from aid – such as big increases in life expectancy – which are much more clearly the result of aid. *Dead Aid* contributes

[4] Clemens, Radelet, and Bhavani (2004) *Counting Chickens When They Hatch: The Short Term Effects of Aid on Growth.* Centre for Global Development Working Paper No 44.

[5] See Commission for Africa (2005) Annex 8 (ppp 365-366)

nothing to this debate: the claim that aid does not work is based on simplistic comparisons buttressed (more worryingly) by misleading accounts of what the empirical evidence actually tells us.

2. Does aid do harm?

Having claimed that aid does not lead to economic growth, Moyo then turns to her explanation of the ways that aid can do harm.

There are reasonable people who think that, in some circumstances, aid might be harmful. For example, Moss, Pettersson and van de Walle write about the "aid institutions paradox".[6] Jonathan Glennie, in his recent book, discusses four possible ways in which aid may do harm.[7] I wrote a paper in 2006 listing seven possible reasons why increases in aid might do more harm than good, though I argued that each can be addressed if donors are careful about the way that they give aid.[8]

Moyo had in this book an opportunity to contribute to the debate about whether aid can be harmful and, if so, what might be done about it. Instead this section of the book is a rambling set of assertions which are never brought together into a coherent analysis. She tells us in various places that aid causes corruption, undermines local accountability, chokes off the export sector and causes bottlenecks. Yet for none of these claims does Moyo explain the argument persuasively or cite evidence to substantiate her view.

For example, Moyo is rightly concerned about corruption, which is a serious problem in many developing (and some developed) countries. Moyo tells us that aid causes corruption: "the point about Africa is not that it exists: the point is that aid is one of its greatest aides". Her evidence is simply this: "because foreign aid is fungible – easily stolen, redirected or extracted – it facilitates corruption". Now, it may unfortunately be true that some aid is lost to corruption – though aid agencies take many steps to minimise this, as a result of which there is probably less corruption of aid than of other sources of revenue.[9] Moyo is right to observe that a lot of aid goes to countries with a high level of corruption but this neither proves that the aid itself is used corruptly nor that aid encourages corruption elsewhere in the economy. Moyo does not explain how any of this amounts to a reason for thinking that aid is one of corruption's "greatest aides".

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[6] Moss, Pettersson and van de Walle (2006) *An Aid-Institutions Paradox? A Review Essay on Aid Dependency and State Building in Sub-Saharan Africa*. Center for Global Development Working Paper 74

[7] Glennie (2007) *The Problem With Aid*

[8] Barder (2006). "Are the Planned Increases in Aid Too Much of a Good Thing?" Center for Global Development Working Paper 90.

[9] Collier (2005). "Is Aid Oil? An Analysis of Whether Africa Can Absorb More Aid", Oxford University.

More worryingly, where Moyo does cite evidence, she misrepresents it. In one passage she talks about education in Uganda:

> "In Uganda, for example, aid-fuelled corruption in the 1990s was thought to be so rampant that only 20 cents of every US$1 dollar of government spending on education reached the targeted local primary schools." (p53)

The public expenditure tracking survey to which Moyo refers was financed by donors, as part of the process of granting debt relief. The survey found that spending – mainly financed by Uganda's own tax revenues rather than aid – was not reaching the schools, though the survey did not conclude that this was a result of corruption. As a result of this survey, and with the support of aid from the United States, the Ugandan government ran an information campaign which told local communities how much money should be reaching each of their schools. The results were dramatic: the amount of money reaching schools increased from 20 percent in 1995 to more than 80 percent in 2001.[10] So the reality of this case was not that aid was used to fuel corruption, but rather that aid played an important part in increasing the transparency and accountability of Ugandan government spending, reducing the scope for corruption and (most importantly) improving the quality of education for schoolchildren. Given that Moyo was able to report the findings of the original survey, she either knew or should have known what happened next – yet she chooses not to share any of this heart-warming aid success story with her readers.

The rest of Moyo's argument about the harm that aid can do is similarly cavalier with the evidence. She refers to the literature on "Dutch disease" (which is the risk that aid might push up the exchange rate and so reduce the competitiveness of a nation's exports) without noting the near-unanimous conclusion – now shared by the IMF whom she cites – that while this is a theoretical possibility, there is no evidence that it happens in practice.[11]

Proponents of aid do have a case to answer about the impact of aid on accountability and governance. The concern is that a government that receives high levels of external aid is less likely to be properly held to account by internal political processes. The necessity of taxing citizens to raise revenues has historically been an important step in establishing a "social contract" between citizens and the state, and high levels of external revenues (whether from aid or from revenues from exports such as oil) may impede the evolution of this kind of accountability.[12] Conversely, there are many good examples of how aid has increased accountability (for example, by supporting more effective civil society, or by increasing the

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[10] Jakob, Svensson ; Ritva, Reinikka. (2004) The power of information: evidence from a newspaper campaign to reduce capture. The World Bank Policy Research Working Paper Series. No 3239.

[11] Gupta, Powell & Yang (2006), "Macroeconomic Challenges of Scaling Up Aid to Africa", IMF.

[12] See for example Brautigam, Fjeldstad, Moore (2008) *Taxation and State-Building in Developing Countries: Capacity and Consent*, Cambridge University Press.

transparency of public spending). Furthermore, there is an uncertain empirical relationship between receiving aid and the extent to which a government raises revenues from its citizens (surprisingly, tax revenues appear superficially to be *positively* correlated with aid).

Unfortunately, Moyo does not do justice to any of this. She does not explain how aid undermines accountability, nor does she provide any evidence or examples of how this has occurred in practice.

Even if Moyo had produced a convincing account of the way that aid can be harmful, she would have to make two further arguments to reach her conclusion that aid should be stopped altogether. She would have to show that the harm outweighs the good. And she would have to show that these flaws are inherent in the aid relationship and could not be addressed by improving the way aid is given. Moyo does not address either question.

3. Alternatives to aid?

Having convinced herself that aid is not effective and that it does more harm than good, Moyo moves on to discuss other ways that developing countries can move forward without relying on aid. Moyo's proposed solutions are: raising money in capital markets, attracting foreign direct investment, reducing restrictions on trade and promoting financial services for the poor.

We should be note that – apart from trade – the evidence for these measures is no better than the evidence for the benefits of aid. As with aid, we can show that there are gains for the direct beneficiaries, but unlike aid, nobody has yet shown any correlation between microfinance and overall growth and development. Moyo clearly sets a different evidentiary standard for the interventions of which she approves. Nonetheless, these are all sensible policies – and they are already being widely pursued.

I turned to a textbook on development economics to verify that Moyo's proposals are already part of mainstream development thinking. [13] The nearest book on my bookshelf has 6 chapters on resource flows for development, of which just one is about aid. The other five chapters are about savings, foreign direct investment, fiscal policy, financial policy, and foreign debt. A further six chapters deal with production and trade (eg agriculture, exports, trade, managing an open economy). These are the issues that Moyo rightly says are important for African nations – and they are the questions that are extensively dealt with in development economics. Simiilarly, the 2005 Commission for Africa has a chapter on trade, and discussions about improving the environment for foreign direct investment and microfinance.[14]

[13] Perkins, Radelet & Lindauer (2006) "Economics of Development", Sixth Edition.

[14] Commission for Africa (2005).

Moyo suggests that aid donors should commit themselves to cut off aid after five years, to encourage greater use of these other instruments which she has discovered. The question is why these policies and instruments should be an alternative to aid, rather than working alongside it.

There are many examples of aid being used to promote exactly the policies which Moyo supports. For example, foreign direct investment (FDI) may be easier to attract if developing countries are able to provide better transport, communications and power infrastructure, or to reform the bureaucracy to make it easier to register a new company or to pay taxes. Aid can be used to finance these things, and so "crowd in" foreign direct investment – which is perhaps why there is a positive correlation between aid and FDI.[15] Aid is also used to promote the development of financial services for the poor.[16] If Moyo thinks that foreign direct investment and improvements in financial services for the poor are valuable, it is not clear why she should be so opposed to using aid to facilitate and accelerate them.

Moyo is certainly right that here are important ways to accelerate development aside from the contribution from foreign aid. I would add others to her list, such as efforts to promote peace and stability, tackling climate change, reducing global corruption, changing immigration policies, reform of patent law, and increasing research and development into global public goods. Arguably these are more important than aid – but that does not mean that they can be better pursued in the absence of aid than with it.

4. Conclusion

Moyo has been unlucky with the timing of her book, which was published as the credit crunch was unfolding. Her suggestion that developing countries will be able to borrow more and more from private capital markets now looks optimistic as credit for the poorest countries is drying up. The prospects for progress on the international trade talks look worse at a time of a growing mood of protectionism. And in the meantime, many of these countries and families will need assistance from abroad more than ever to help them to survive.

However, there are important questions to answer about whether aid can be harmful in some circumstances, and whether this harm outweighs the good that aid can do. This kind of thinking would yield important policy conclusions for where and when, and especially how, aid is given. One might even reach the conclusion that the problems are so large, and so intrinsic to the nature of aid, that it is better not to give aid at all to some countries. But Moyo does not take us through those arguments or the evidence. She simply asserts that aid causes corruption and weakens accountability, and dismisses the body of evidence which shows, on the contrary, that the rates of return to aid are higher than almost any other form of public spending.

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[15] Karakaplan, Neyapti and Sayek *Aid and Foreign Direct Investment International Evidence*

[16] See http://www.cgap.org/p/site/c/template.rc/1.26.1389/

Moyo has the cheek to accuse people working in the aid industry of promoting their own interests, and then – as an investment banker from Goldman Sachs – to advocate instead that the poorest countries should be encouraged to borrow more in private capital markets. And her argument is based on what appears to be a deliberate mis-statement of the evidence.

Moyo advocates some commendable policies other than aid which might accelerate development. But these are already conventional wisdom, and Moyo's book does nothing to challenge the view that progress on these can be faster with more support from aid.

There is a debate to be had about aid, but Moyo's book, sadly, does not advance it. *Dead Aid* is poorly researched, badly argued, mendacious in its use of evidence, and pedestrian in its suggestions for alternatives to aid.

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