Is Economic Development an Appropriate Focus for an Aid Programme?

NZADDs Working Paper[1]

Terence Wood[2] *– terence.wood@anu.edu.au*

This paper examines whether economic development is an appropriate central focus for a government aid programme. The context for the paper is the change in focus of the New Zealand government aid programme that occurred in 2009; however, the findings are intended to be applicable to other government aid agencies. The paper starts by providing definitions of development and economic development. It then examines empirical evidence, outlining the relationship between economic development and development more generally, before assessing the evidence on whether aid is an effective tool for stimulating economic development. It also examines aid's effectiveness in sectors other than economic development. The paper then draws conclusions on the basis of the evidence examined as to whether economic development is an appropriate central focus for a government aid programme. Key among the conclusions is the recommendation that, rather than having a pre-determined central focus, such as economic development, a better approach would be for the central focus of government aid to vary depending on the context of countries being worked in.

[1] NZADDs working papers do not necessarily reflect the views of NZADDs or its Steering Committee members. Views expressed within NZADDs papers are solely those of the paper's author(s).

[2] Terence would like to thank Jo Spratt, Ken Jackson, Anita Lacey, Geoff Bertram, and other forum participants for their questions and comments on this paper. Responsibility for all errors or inadequacies that remain lies solely with Terence. Further feedback is appreciated.

Introduction

Since gaining power in 2008 the National led government of New Zealand has altered the thematic focus of New Zealand Official Development Assistance. Through a cabinet decision to change the aid programme's mandate and via a number of public proclamations from the Minister in charge of the aid programme, the government has indicated that New Zealand aid will now be given with a "central focus" on economic development (Cabinet Office 2009). This shift in focus has been controversial, students picketed the speech in which the Minister announced this and other changes to the aid programme (New Zealand Herald 2009), while critical commentary was published in various local media (for example, Coates 2009).

In the following paper I examine whether economic development is an appropriate central focus for an aid agency. Clearly this question is of immediate relevance to current debates taking place in New Zealand; however, it is also of broader relevance: New Zealand is not the only country with an economic development focus for its government aid programme.

To answer my overarching question of whether a central focus on economic development is an appropriate one for a government aid programme, I break the question into three sub-questions. First, I examine whether economic development leads to improvements in human welfare more generally. Then I examine aid's track-record in promoting economic development. Finally, I examine aid's track record outside the economic sphere. This approach is based on the premise that a central focus on economic development can only be justified if it can be shown that economic development improves people's lives more generally *and* if aid can be shown to actually be capable of promoting economic development. Moreover, even if economic development is linked to broader welfare improvements and if aid can be shown to be capable of promoting economic development, it still needs to be asked whether aid mightn't bring about such welfare improvements more efficiently through direct spending in other relevant sectors.

With respect to the first sub-question, I find that on average economic development is associated with improvements in human welfare more generally. However, I also find that economic development isn't guaranteed to bring about such improvements. Moreover, I find that – in some instances – economic development is not the only means of promoting broader welfare improvements.

With regards to the second sub-question (whether aid can promote economic development) my findings are ambiguous. On average across countries it seems likely that aid has had some success in promoting economic development. However, within this overall average there is considerable variation. Aid appears to have succeeded in promoting economic development in some countries but not in others.

In the case of the third sub-question (whether aid has been successful in promoting development outside the economic sphere) I find the evidence to be less ambiguous. In areas such as improved health outcomes, aid has some clear and significant achievements to its name.

From this I conclude that economic development is not an optimal focus for an aid programme. A preferable approach would be to determine the focus of aid work based on the context where it is being undertaken, adopting the focus most likely to successfully improve human welfare, given the specific sets of needs and challenges associated with the country or region being worked in.

Underlying this paper is the assumption that the core purpose of New Zealand official development assistance (ODA) ought to be improving the welfare of people living in developing countries. There are other reasons why ODA might be given, particularly the desire to promote donor country business interests or to further donor country strategic objectives. However, whenever it has been surveyed, the New Zealand public has revealed a strong preference for giving ODA for humanitarian reasons rather than in the nation's self interest (UMR Research 2007: 39-40). Moreover, public statements both from the New Zealand aid programme itself and the current Foreign Minister suggest that, putatively at least, the purpose of the New Zealand aid programme is improving the lives of people living in developing countries (for example, New Zealand Aid Programme 2010; McCully 2011). In the paper that follows I work from the assumption that the actual rationale for the New Zealand government giving aid ought to be consistent with its stated rationale, and with the desires of New Zealand taxpayers – the people who ultimately fund our aid programme.

Development and Economic Development Defined

Debates about definitions of development are numerous and unlikely to be resolved anytime soon. For reasons of brevity I do not delve into them here. Rather, I have chosen a definition of development which I hope is both general and simple enough to be uncontentious.

For the purpose of this paper I have defined development as: *a process through which human suffering is reduced, and through which human welfare and wellbeing is increased*. As noted, this ought to be uncontroversial: it is hard to imagine anyone believing that development ought to involve increased suffering or reduced welfare.

In this paper I define economic development to mean: *economic change in countries and regions leading to increased material prosperity*. This definition is in line with most conventional definitions.

While economic development as defined here is not exactly the same as growth in countries' Gross Domestic Product (GDP) or Gross National Income (GNI) (economic growth), the two concepts are very closely related. And, owing to the relative ease of measurement of GDP and GNI, such statistics are frequently used as measures of economic development in much of the literature that I make reference to. This is reflected in the analysis I undertake.

Economic Development and Development

In the following section I examine the relationship between economic development and a range of broader indicators of human welfare. Specifically, I look in some detail at the relationship between economic development and health, the relationship between economic development and happiness, and the relationship between economic development and poverty reduction. I then briefly examine the relationship between economic development and other indicators of welfare before examining the environmental impact of economic development. Finally, I look at the issue of economic development and state sovereignty.

Economic Development and Health

One simple means of attempting to answer the question whether economic development leads to better health outcomes is to plot the level of economic development and life expectancy at birth for a range of countries on a scatter plot. This is done below in Figure 1.

Figure 1 – GDP per Capita versus Life Expectancy

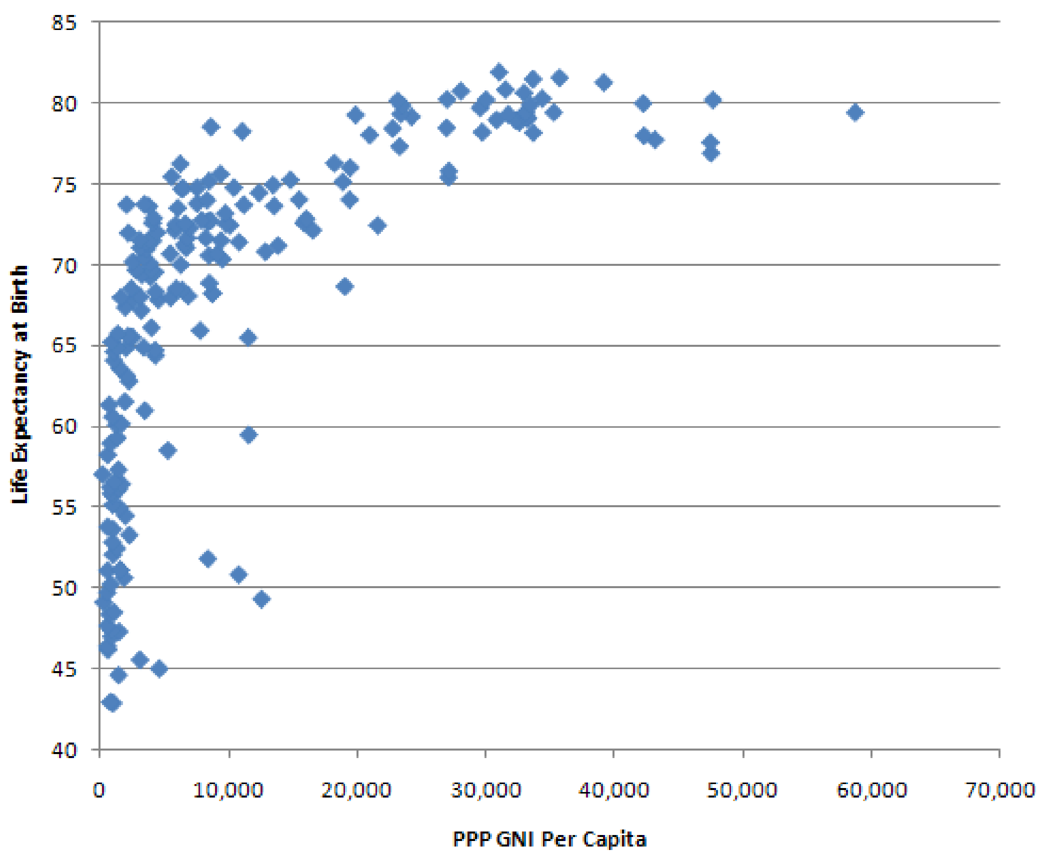

Figure Source: World Bank World Development Indicators[3]

[3] The data source explains the GNI figure as follows: "GNI per capita based on purchasing power parity (PPP). PPP GNI is gross national income (GNI) converted to international dollars using purchasing power

Figure 1 reveals one of the key stylised facts of international development, the so-called Preston Curve. At low levels of economic development there is a very strong relationship between economic development and health outcomes. This relationship begins to weaken at about $10,000/capita and appears to break down altogether around $30,000.

While the relatively weak relationship between GDP/capita and life expectancy in wealthier countries is interesting to note, it is the steeper segment of the curve that is of most relevance to the focus of this paper, as aid is typically directed towards those countries which inhabit this section of the graph[4]. And in this section of the curve the relationship is strong; wealth and health are clearly related. The strength and direction of this relationship gives reason to believe that economic development ought to lead to improved health outcomes. Yet by itself it is not definitive evidence. While the relationship is clear, the direction of causality within it is not. It is certainly plausible that economic development causes improved health, perhaps because wealthier people are able to afford better nutrition, or because wealthier countries are better able to pay for medicines or public sanitation. Yet, the other hand, potentially, causality may run in the opposite direction, i.e. it is improvements in health which drive economic development. Healthier children may be better able to learn and develop cognitively (making them more economically productive later in life), while healthier adults, for example, might be able to work longer hours and more productively (Bloom and Canning 2007).

Considerable work has gone into untangling the relationship with some scholars arguing for a virtuous cycle between economic development and nutrition but with economic development playing a crucial role in improving health and raising life expectancy (for example, Fogel 2004; reviewed in Deaton 2006). On the other hand, authors such as Bloom and Canning (2007) argue that causality flows at least in part in the other direction, and that the disease burden in developing countries which is impeding their economic development.

It is likely that the causal links in the relationship between better economic outcomes and better health outcomes do run in both directions; however, of most importance for the discussion here, there is broad consensus that improved economic development does lead to better health outcomes, on average (Spence and Lewis 2009).

Importantly, noting that improved economic development tends *on average* to better health outcomes is not the same as saying that economic development inevitably leads to better health. For example, in 2007 the United States was the world's seventh wealthiest country in

---

parity rates. An international dollar has the same purchasing power over GNI as a U.S. dollar has in the United States."

[4] For example, PPP Per Capita GNI for Solomon Islands in 2005 was $2060; for Samoa it was $3630; for Fiji it was $4360.

terms of PPP GNI per capita, yet 40 countries had a higher life expectancy than the USA, including Costa Rica whose PPP GNI per capita was only 22 percent of the USA's (World Bank 2011). As Deaton (2006: 111) notes: "Economic growth frequently needs help to guarantee an improvement in population health."

Similarly, economic development is not the only way health outcomes can be improved in developing countries. Some countries have been able to achieve dramatic improvements in health outcomes despite relative poverty. Sri Lanka for example had, through a cost effective primary health care system raised its life expectancy to 74.4 in 2004 despite low GNI per capita (Hsiao and Heller 2007).

While economic development, ought, everything else being equal, to improve health outcomes in developing countries, improvements may be modest unless increased revenues associated with such development are actually invested in health (Overseas Development Institute 2010). Meanwhile, health outcomes can in some instances, to an extent, be improved by means other than economic development alone.

Relationship between Economic Development/Growth and Poverty Reduction

Poverty reduction remains an explicit component of the mandate of the New Zealand government aid programme as stated on the 'About' page of the aid programme's website:

> Support sustainable development in developing countries in order to reduce poverty and to contribute to a more secure, equitable, and prosperous world. (New Zealand Aid Programme 2010b).

Given this, it is important to investigate how effective economic development is in reducing poverty.

By definition, economic growth (growing GDP/Capita) raises the mean income of individuals living within the area experiencing the growth. This alone provides good cause to believe that economic development will lower poverty levels (Weisbrot et al. 2001). The only way it might not is if growth is accompanied by rising inequality and/or if low income groups do not share in overall rising average incomes. On the other hand if economic growth is distribution neutral, or if it disproportionately benefits the poor, then poverty reduction will automatically follow.

The key question therefore becomes, how often is economic development associated with rising inequality, how often is it distribution neutral, and how often is it actually pro-poor (that is, how often does it disproportionately benefit the poor)? This is a question that has been examined and debated in considerable detail in academic work in recent years. In summarising the state of the knowledge emerging from this research and debate Ehrenpreis (2007: 2) writes that:

> There seems to be a broad consensus among analysts and policy makers that per capita income growth is a major element of sustainable poverty reduction.

> However, similar rates of growth can have very different impact on income poverty under different conditions, varying in time and space.

Various individual research findings help explain the reasoning behind this statement:

- First, there is considerable cross country evidence (for example, Kraay 2006) showing that on average, across countries, economic growth is coupled with poverty reduction.

- However, there are a number of examples from individual countries and regions that show that, despite an overall global average relationship, growth does not always have the same impact on poverty levels. Weisbrot et al. (2001), for example, highlight periods of recent economic growth in the United States and other countries that have failed to reduce poverty at all. And Ravallion (2009) show's that in India, during different periods over the last three decades, similar rates of economic growth have been coupled with differing rates of poverty reduction. Ravallion (ibid) also shows that by reducing inequality Brazil was, over the last two decades, able to succeed in reducing poverty despite relatively low growth rates. Meanwhile Besley et al. (2006) compare the extent to which different Indian states have converted economic growth into poverty reduction finding major variances: some states, such as Kerala, have translated mid-range levels of growth into quite dramatic rates of poverty reduction, while other states such as Haryana have had much less success in reducing poverty, despite higher growth rates. Mosley (2004) even provides evidence to suggest that some growth episodes in some parts of the world have actually led to worsening circumstances for the most acutely poor.

While the range of findings may seem complex, their implications for policy makers are straightforward enough. Everything else being equal, economic development is a powerful tool for reducing poverty, and for this reason, focusing to some degree on economic development may well be appropriate for an aid programme seeking to combat poverty. Yet everything else is not always equal and an aid programme which focuses on economic development alone may well miss opportunities to enhance the benefits of economic development for the poor. Plausibly, a myopic focus on economic development may even, in extreme cases, lead to worsening poverty or worsening outcomes for the poor.

Relationship between Economic Development and Happiness

Inspired by the path-breaking work of Richard Easterlin (1974) the study of the impact of social, economic and political factors on surveyed levels of happiness or life satisfaction, has become a major research focus in recent years (for example, Layard 2006; Stevenson and Wolfers 2008; Kahneman and Deaton 2010). Typically such studies make use of survey data in which respondents are asked questions pertaining to their own self-assessed state of wellbeing. While subjective measures of this nature may seem an unreliable source of data, when individuals' self-reported levels of happiness are cross-checked against assessments made by peers or using neurological imaging they have proven relatively robust (Layard 2006). Moreover, cross country comparisons of surveyed levels of happiness or life satisfaction reveal meaningful relationships, something which is unlikely if such measures were wholly unreliable.

Numerous policy relevant findings have stemmed from this field of research; the one most relevant for this paper though, is the relationship between GDP/Capita and happiness. With respect to this relationship recently there has been debate as to the strength of the relationship in wealthier countries (for differing perspectives see Layard 2006 and Stephenson and Wolfers 2008), but in the part of the curve most relevant to official development assistance work, low GDP countries, the relationship is uncontroversial: in these countries higher levels of GDP are associated with higher levels of reported happiness (Stevenson and Wolfers 2008). Moreover, available evidence suggests that the primary causal link present in the relationship is from wealth to happiness. That is, up to a point at least, increased wealth leads to greater happiness (Stevenson and Wolfers 2008).

Once again, as with findings relating to health and poverty reduction, this finding provides some comfort to those advocating economic development as a key focus for official development assistance. Yet, once again, variance above and below the general trend exists, and other aspects of people's lives, such as health, have been shown to be important determinants of surveyed happiness (Kahneman and Deaton 2010). Material wealth is an important factor contributing to the happiness, but it isn't the only one.

Economic Development and the Environment

A common objection to economic development stems from the concern that increased levels of economic prosperity will necessarily lead to increased damage to the natural environment. This view is reflected in a range of significant publications (for example, Ehrlich 1968; Club of Rome 1972) and it is close to being conventional wisdom in some quarters. Yet it is also a view that has been challenged, particularly from within the economics profession, with opponents arguing that economic development and environmental impact have a relationship which takes the form of an inverted U-shaped curve (the so called Environmental Kuznets curve). In this view, increased prosperity is argued to lead to increased environmental damage but only up to a point. Beyond that point as countries become wealthier they subsequently adopt higher environmental standards as their citizens, having met their basic needs, place a higher premium on the environment (Grossman and Krueger 1991).

The evidence supporting the respective points in the debate is mixed. However, the following appears clear. The Environmental Kuznets curve does appear to exist for some, but not all, pollutants; and the relationship between wealth and pollution varies with other factors, such as quality of government (Carson 2010).

In some areas, especially those where the impacts of pollution are not felt immediately and within close proximity to the source of the pollution, such as Carbon Dioxide emissions (see Figure 3 below), the relationship between measures of economic development and pollution appears to be essentially linear: wealthier countries produce greater emissions and this trend does not begin to taper off beyond any particular income level (although there is greater variance in CO2 emissions levels amongst wealthier countries).

While such evidence points to some significant global challenges associated with high levels of material prosperity. It does not, on its own, mean that aid should not be used to promote economic development. In the case of localised pollution the experience of countries such as New Zealand itself suggests that reasonable levels of economic prosperity need not inevitably be associated with environmental collapse. While with respect to global issues such as climate change, it hardly seems an ethically tenable position to deny developing countries the same pathway to prosperity that our own countries have taken, along with the broader benefits associated with such prosperity, while wealthy countries continue to emit Greenhouse Gases in an unchecked manner. Moreover, if the world's developed countries (along with countries whose development trajectories are not related to aid such, as China) continue to emit Greenhouse gases at current levels these alone will be sufficient to induce significant climate change. The most important change that needs to take place to resolve this particular issue is in the consumption patterns of these countries, coupling their economic performance to increased environmental sustainability. Once this happens the technologies involved in such a transformation ought to be transferrable to developing countries. Until it happens it seems unjust to deny developing countries the benefits of such progress.

Figure 3 GNI Per Capita and CO2 Emissions

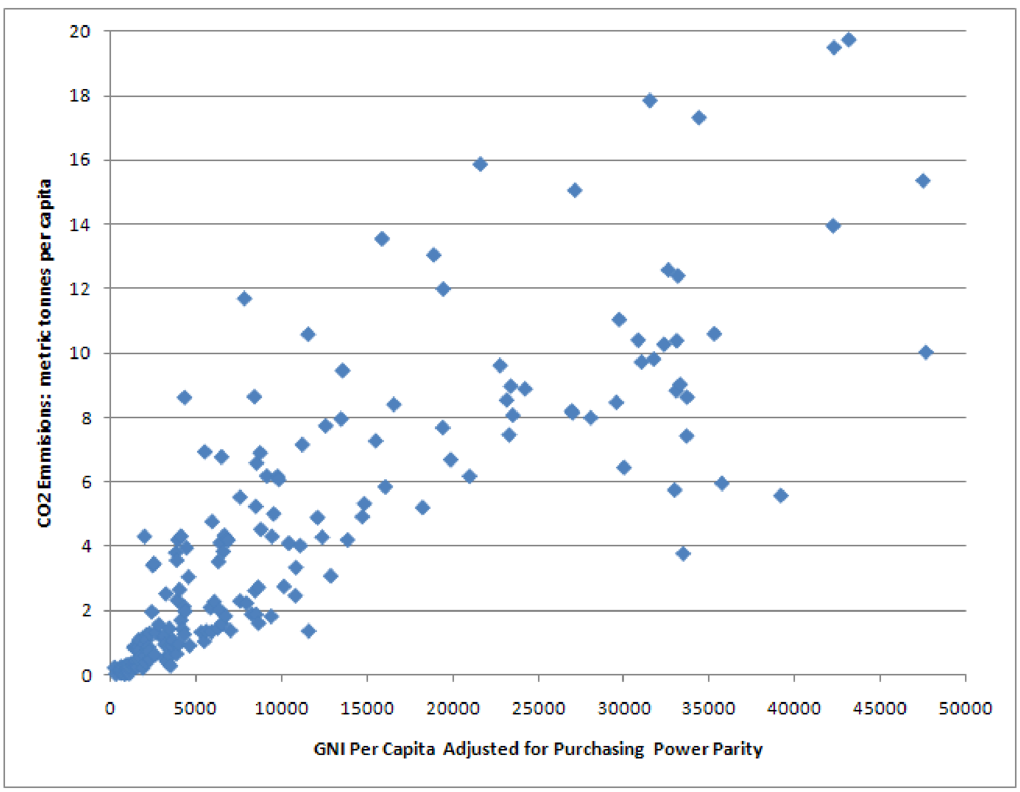

Figure Source: World Bank World Development Indicators (refer to Figure 1 for information on GNI/Capita)

The Impact of Economic Development in Other Sectors

Thus far this paper has summarised the results of research looking at the relationship between economic development and three components of development more broadly defined: health, poverty and happiness. In each instance the findings have been similar: economic development is typically positively associated with better health outcomes in developing countries, reduced poverty, and happier citizens; however, at the same time, economic development is not guaranteed to bring about improvements in these sectors – it can be more or less effective in engendering development depending on its nature and on context specific factors. Also, importantly, in some instances and up to a point, worthwhile improvements in development outcomes can be made in the absence of economic development.

While this paper has been limited to examining three aspects of development, other work (for example, Overseas Development Institute 2010) has investigated the relationship between economic development and other development outcomes such as education, finding similar results.

Economic Development and Sovereignty

Before moving on to the next section of the paper one final point in favour of economic development ought to be noted. This is to do with sovereignty and independence. While some developing countries have managed to fund meaningful social schemes that have improved outcomes in sectors such as health and education from their own domestic revenues, the world's poorest countries are unlikely to be able to fund a large range of such programmes in the absence of continuing foreign aid. This means that in the absence of economic development these countries will remain dependent on the largess of wealthier members of the international community. Clearly this is not an optimal situation for aid recipient countries to be in. The need to meet the demands of aid donors reduces their own domestic policy space, while at the same time the need for external assistance leaves such countries to some extent at the mercy of other nations. Recent history has shown aid flows to be volatile and the intentions of wealthy countries not always benign. Clearly there is an advantage to developing countries in escaping such dependence if they possibly can.

Figure 4, on the following page, shows GDP/Capita and ODA/Capita figures for South Korea and provides a useful example of the previous point. As shown in the figure, as South Korea's economy has grown, its reliance on Official Development Assistance has decreased, illustrating an important point in favour of economic development: with it comes reduced reliance on aid and increased economic sovereignty.

Figure 4 – South Korea: GDP/Capita and ODA/Capita

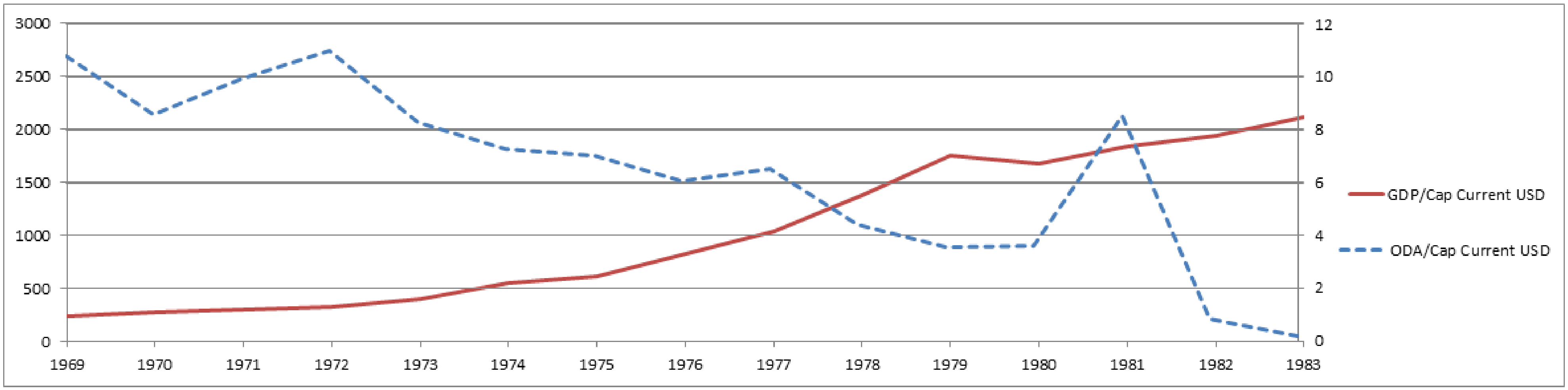

Figure Source: World Bank World Development Indicators

Figure Notes: Left Axis is GDP/Capita

Can Aid Foster Economic Development

Taken together the above points suggest that, *assuming aid can promote it*, economic development may potentially be an appropriate focus for an aid agency. As long as the aid agency takes steps to ensure the economic development associated with its work favours the poor (or at least does not harm them) and that at least some of the material wealth generated is channelled into spending in sectors such as health, economic development work ought to lead to broader welfare improvements. Moreover, if the ultimate end goal of development is for poorer countries to one day be able to provide such services to their citizens independently of aid, economic development is essential to achieving this.

This paper now turns its attention to the assumption made above: is aid actually likely to succeed in promoting economic development?

Whether aid can promote economic development has been the subject of much research in recent years. This research has typically taken one of two forms: cross country research using regression analysis and within country studies that attempt to examine the histories of particular countries (either using econometric techniques or some form of process tracing). In both types of work the dependent variable is GDP per capita (or another similar measure) and the independent variable is aid.

Whichever way it has been gathered, the evidence that has been produced on the relationship between aid and growth has been ambiguous.

In the case of cross country evidence, while there have been a number of well-regarded studies purporting to find a positive relationship (for example, Clemens et al. 2004; Arndt et al. 2010; Minoiu and Reddy 2010) a similar range of studies have shown aid to have no statistically significant impact (Easterly et al. 2003; Rajan and Subramanian 2008). In part, this ambiguity is the result, not of the deficiencies of aid, but rather the limitations of aid/growth regression analysis. The data used are often poor and blunt (failing, for example, to differentiate between high and low quality aid) while problems associated with determining the causal direction of relationships between aid and growth have proven extremely difficult to resolve in regression analysis (Roodman 2007).

To the extent that it is possible to squeeze conclusions from the body of research as a whole, the balance of evidence appears to suggest that aid has a small positive impact on growth, on average across countries (Arndt et al. 2010). However, given the range of results produced by different studies, such a conclusion is by necessity a tentative one. Also, importantly, it is a conclusion that is based around average impact across countries. It is quite possible that a small average positive relationship across countries is a product of aid successfully promoting economic development in some countries, while achieving nothing, or even having a negative impact in others. Indeed, this is the finding of at least one cross country study, which differentiates aid recipients by political characteristics, and finds aid to have a positive impact in some countries, but a negative one in others (Wright 2010).

The second body of relevant literature, within country studies, is smaller. But those within country studies that do exist return a range of results and in doing so add further evidence to suggest that the impact of aid on economic development varies from country to country. For example, Arnt et al. (2007) find aid to have had a positive impact on economic development in Mozambique, while Gounder (2001) finds aid to have had a positive impact on economic development in Fiji. Feeny (2005) on the other hand finds aid to have had little positive impact on economic growth in Papua New Guinea. As with cross country regression work there are methodological challenges associated with within country studies and, once again, these challenges may explain some of the variance in results returned. However, the degree of divergence is significant enough to suggest that aid is very unlikely to contribute equally to economic development in all circumstances.

To summarise, the results of recent research which looks at the relationship between aid and economic development are far from emphatic. In part this is a product of the methodological challenges involved in reliably identifying aid's impact in this area but, importantly, it is also a product of the fact that aid's impact on economic development is ambiguous. What is likely is that in some contexts some forms of aid can boost economic development. However, it would be a mistake to conclude that aid will inevitably increase economic development in all contexts or that, even when the impact is positive, it will necessarily be large.

Uncertainty in the Causes of Economic Development

This already uncertain picture is further compounded by the fact that, despite decades of research, it is not by any means clear exactly what the key determinants of successful economic development actually are in developing countries. In the long run it appears that the quality of political and economic institutions within countries has played an important role in determining the varying levels of economic development seen across the globe today (Acemoglu et al. 2001; Acemoglu et al. 2002; Acemoglu et al. 2005) and it is possible that geographically determined factors such as disease environments may have also played some role in determining the wealth of nations (Sachs 2003). Similarly, human capital almost certainly contributes to economic development (Bloom et al. 2004; Cohen and Soto 2007; Hanushek and Woessmann 2009). Yet beyond this there is considerable uncertainty (Lindauer et al. 2002; Rodrik 2006; Easterly 2007). As Easterly (2007: 329) puts it:

> In the new millennium, a remarkably broad group of academics and policymakers seem to agree that, after all that, maybe we don't know how to achieve [economic] development, although [they are] reluctant to say so exactly.

Even the degree of consensus around the importance of quality institutions in fostering economic development is of limited assistance to policy makers. While we can be fairly certain institutions are important, it is much less clear which institutions are important or what form good institutions will take in different contexts. As Chang (2007: 2) puts it:

> First of all, we still do not know which institutions in exactly what forms are useful for economic development in which contexts... Second, even when we can identify a particular institution as beneficial in a given context, we often do not know how we can build such [an] institution.

Not only is aid's impact on economic development unclear and prone to change depending on context, but – beyond this – exactly how and where an aid agency should intervene should it wish to promote economic development is unclear. When these facts are taken into account, the case for focusing aid on economic development becomes considerably weaker.

Can Aid Achieve Other Outcomes

Having examined the impact of economic development on human welfare, and having examined the impact of aid on economic development, the final part of the process of answering the question 'should economic development be a central focus of an aid programme?' is to consider the record of aid in sectors that do not fall under the rubric of economic development. As stated in the introduction, this paper is predicated on the idea that aid should be given for the ultimate purpose of improving human welfare. One way aid could do this is by promoting economic development which, as we have seen, does (with caveats) tend to improve welfare more generally. However, as I have demonstrated, aid's track record in promoting economic development is decidedly mixed, and the task of promoting economic development a complicated one. The alternative is for aid spending to be directly focused on promoting welfare – for example, through the funding of health care, or supporting education, or preventing conflict[5].

If aid can be shown to improve human welfare more effectively by being spent directly in sectors associated with wellbeing then this provides evidence for the argument that economic development is *not* an optimal focus for an aid agency.

Research investigating the impact of aid on other aspects of development comes in a range of forms, from cross country regressions similar to those used in studies looking at the impact of

[5] A complicating factor here is that something such as a health clinic could plausibly be funded both by an aid agency with economic development as its central goal (on the premise that improved health will contribute to economic development) and by an aid agency whose central focus was human welfare. The key distinguishing fact being the reason why the health clinic is being funded: in one case to improve economic productivity, in the other simply to help the sick.

aid on economic development (but in this case with health or some other component of human wellbeing as the dependent variable), to case studies. Amongst this work an increasing body of evidence is accumulating that suggests that aid has had positive impacts on human welfare, in some instances dramatic ones, although impacts vary from place to place and sector to sector.

Health is one area where aid has had dramatic successes. Not only has aid funding contributed to the near elimination of polio, the elimination of small pox and to declining infant mortality rates globally (Easterly 2008) but it has had significant successes in a range of other health related programmes (see, for example, the aid funded cases presented in Levine 2007). A recent study examining the health impacts of aid-funded anti-Malaria work in Zambia noted the following.

> Evidence from the 2001 and 2007 waves of the Demographic and Health Survey confirms the picture painted by the HMIS. The percentage of children under five reported with a fever over the two weeks preceding the interview dropped from 44.6% in 2001 to 17.9% in 2007, a reduction of close to 60%. (As a comparison, the fraction of children suffering from diarrhea fell by only a quarter, from 41.9% to 31.8%, over the same time period.) The progress made in all-cause child mortality between the two surveys is remarkable: The under-five mortality rate fell from 168 per thousand live births in 2001 to 119 in 2007. As discussed below, the latter figure may not even reflect the full mortality reduction to date. This decline was not solely the result of the malaria initiative, however, since other health campaigns were taking place at the same time.
>
> There are different ways to quantify the magnitude of Zambia's recent success in health improvement. The reduction in under-five mortality represents approximately 25,000 children's lives saved per year. To compare the mortality improvement with more "economic" outcomes, we can do a back of the envelope calculation using the Human Development Index (HDI), which weighs economic and non-economic characteristics into an overall measure of quality of life. Using the formula for the HDI, one can calculate the amount of income growth that would be equivalent to a particular rise in life expectancy at birth. A conservative estimate, using just the data on under-five mortality, is that life expectancy at birth in Zambia rose by 2.25 years over the period 2000-2007.2 Plugging this into the HDI formula shows that an equivalent rise in HDI would be achieved if income per capita grew by 25%. (Ashraf et al. 2010: 3)

While the authors subsequently revise down some of the findings of the household surveys detailed in the quote above, their conclusion remains that the welfare improvements associated with health work in Zambia are significant. As is the case with the Malaria programme that was the specific focus of the study, most of the more general health work in Zambia is aid funded.

The success of specific aid undertakings in health is also reflected in cross country regression studies (for example, Chauvet et al. 2009; and Mishra and Newhouse 2009). Cross country studies also provide some evidence of aid effectiveness in sectors such as education (Michaelowa and Weber 2007; Dreher et al. 2008). A finding which is reinforced by evidence of within country successes in aid supported education initiatives in countries such as Ethiopia (Engel and Rose 2010).

In other areas, where one would expect positive outcomes to have direct welfare benefits, such as democracy promotion and conflict resolution there is also evidence of aid having an impact. For example, Savun and Tirone (2011: 1) find that: "Democratizing states that receive high levels of democracy assistance are less likely to experience civil conflict than countries that receive little or no external democracy assistance."

Taken together, these findings are not evidence that aid that seeks to improve human welfare by directly assisting social spending, or through promoting conflict resolution, will inevitably succeed. Nor are they evidence that aid will inevitably do a better job of promoting human welfare through direct spending in these sectors, than through spending on economic development. However, the findings are evidence that aid not targeted to economic development can have significant and worthwhile positive impacts on people's lives. Moreover, the evidence for aid effectiveness in areas such as health is less ambiguous than that for aid's efficacy in promoting economic growth.

Conclusion and Recommendations

In this paper I have attempted to answer the question: is economic development an appropriate central focus for an aid agency? To do this I have asked three questions:

1. Does economic development lead to improved development outcomes more generally?
2. Is aid an effective tool for promoting economic development?
3. Is aid an effective tool for improving broader development outcomes through mechanisms other than economic development?

I have found that, generally, particularly for low income countries, economic development is associated with broader development benefits. However, I also identified evidence which suggests that the extent to which economic development leads to improved welfare varies. And I noted that, up to a point, some welfare improvements can be brought about in the absence of economic development.

Combined with the fact that economic development also brings with it the potential for aid recipient countries to reduce or eliminate their dependence on aid (and therefore their vulnerability to the whims of other sovereign nations) these points all suggest that there is a good case for economic development to be a central focus for an aid agency, *if it can be shown* *that aid is an effective tool for brining economic development about.* Economic development isn't everything, but it does appear to be an important component of the successful long term development of developing countries.

However, in answering my second question above I have presented a range of evidence that suggests that aid is not, on average, a particularly effective tool for promoting economic development. The overall average impact of aid on economic development is likely (but not certain) to be positive, albeit small. When this average is broken down into individual country experiences it would appear that aid's track record varies significantly from country to country; in some countries it appears to have had some success, but in others it has either not had an impact or potentially even had a negative impact.

This contrasts with aid's record in directly promoting other aspects of development more broadly conceived. Aid has had considerable success, particularly in health initiatives, but also in education, and in other areas such as conflict prevention. Even in these areas aid's success is not guaranteed but its track record appears to be more positive than in the realm of economic development.

The final question that remains to be answered is what does all this mean in aggregate? Is economic development an appropriate central focus for an aid programme? Is it the best way for an aid programme to bring about development more generally?

Based on the evidence above, the answer to these questions would appear to be no. Generally, economic development is a laudable outcome (even if it isn't everything), but there is little to be gained by focusing aid in this area if it is unlikely to achieve results. This is particularly the case if, as it appears from the evidence, there are other means of achieving improved development outcomes, and if aid is more likely to be successful when devoted to these means. A far better approach, based on aid's track record to date, and based on the range of sectors where aid has had some success, would be for the central focus of an aid programme to be to aim to foster development generally, and to then let country context dictate the specific sectors that aid is devoted to.

Following this approach would mean that aid agencies would determine their focus for each specific country not on the basis of a politically determined preference for a particular type of work but rather based on two key questions:

First, what are the binding constraints on welfare in this country?

And second, given the limitations of aid, given what we know about the workings of this country, and given what we've learnt from past experience, which of these binding constraints are we most likely to be able to meaningfully work on easing?

Even this approach isn't a guarantee of success. Development work is complicated, and interpreting context itself isn't easy but, given the challenges associated with aid work, and given aid's uneven track record to-date, it seems considerably more likely to succeed than rigid adherence to a central focus predetermined in the capital city of a donor country.

References

Acemoglu, D., S. Johnson, et al. (2001). "The Colonial Origins of Comparative Development: An Empirical Investigation." The American Economic Review **91**(5): 1369-1401.

Acemoglu, D., S. Johnson, et al. (2002). "Reversal of Fortune: Geography and Institutions in the Making of the Modern World Income Distribution." The Quarterly Journal of Economics **117**(4): 1231-1294.

Acemoglu, D., S. Johnson, et al. (2005). Institutions as a Fundamental Cause of Long-Run Growth. Handbook of Economic Growth. A. Philippe and N. D. Steven, Elsevier. **Volume 1, Part 1:** 385-472.

Arndt, C., S. Jones, et al. (2007). Aid and Development: The Mozambican Case. Theory and practice of foreign aid. S. Lahiri. Amsterdam, Elsevier**:** 235-288.

Arndt, C., S. Jones, et al. (2010). "Aid, Growth, and Development: Have We Come Full Circle?" Journal of Globalization and Development **1**(2): Article 5.

Ashraf, N., G. Fink, et al. (2010). "Evaluating the Effects of Large Scale Health Interventions in Developing Countries: The Zambian Malaria Initiative." National Bureau of Economic Research Working Paper Series **No. 16069**.

Besley, T., R. Burgess, et al. (2006). The Policy Origins of Poverty and Growth in India. T. Besley and L. J. Cord. Washington DC, World Bank**:** 59-78.

Bloom, D. E. and D. Canning (2007). "Commentary: The Preston Curve 30 years on: still sparking fires." International Journal of Epidemiology **36**(3): 498-499.

Bloom, D. E., D. Canning, et al. (2004). "The Effect of Health on Economic Growth: A Production Function Approach." World Development **32**(1): 1-13.

Cabinet Office. (2009). "New Zealand Agency for International Development: Mandate and Policy Settings (Paper Three)."   Retrieved 16.3.2011, from http://www.beehive.govt.nz/sites/all/files/CAB%20Min%203.pdf.

Carson, R. T. (2010). "The Environmental Kuznets Curve: Seeking Empirical Regularity and Theoretical Structure." Review of Environmental Economics and Policy **4**(1): 3-23.

Chang, H.-J. (2007). Stranger than Fiction? Understanding Institutional Changes and Economic Development, World Institute for Development Economic Research (UNU-WIDER).

Chauvet, L., F. Gubert, et al. (2009). Are Remittances More Effective than Aid for Improving Child Health? An Empirical Assessment using Inter and Intra-country Data. Annual World Bank Conference on Development Economics 2009, Global People, Politics, and Globalization. Y. L. Justin and B. Pleskovic, World Bank**:** 173-205.

Clemens, M., S. Radelet, et al. (2004). "Counting Chickens When They Hatch: The Short-term Effect of Aid on Growth." Center for Global Development Working Papers **44**.

Club of Rome (1972). The Limits to growth; a report for the Club of Rome's project on the predicament of mankind. New York, Universe Books.

Coates, B. (2009). "Aid is about poverty, not politics." Retrieved 16.3.2011, from http://www.stuff.co.nz/2258558/Aid-is-about-poverty-not-politics.

Cohen, D. and M. Soto (2007). "Growth and human capital: good data, good results." Journal of Economic Growth **12**(1): 51-76.

Deaton, A. (2006). "The Great Escape: A Review of Robert Fogel's The Escape from Hunger and Premature Death, 1700–2100." Journal of Economic Literature **44**(1): 106-114.

Dreher, A., P. Nunnenkamp, et al. (2008). "Does Aid for Education Educate Children? Evidence from Panel Data." The World Bank Economic Review **22**(2): 291-314.

Easterlin, R. A. (1974). Does Economic Growth Improve the Human Lot? Some Empirical Evidence. Nations and Households in Economic Growth. P. A. David and M. W. Reder. New York, Academic Press.

Easterly, W. (2007). "Was Development Assistance a Mistake?" The American Economic Review **97**(2): 328-332.

Easterly, W. (2008). "Can the West Save Africa?" National Bureau of Economic Research Working Paper Series **No. 14363**(published as William Easterly, 2009. "Can the West Save Africa?," Journal of Economic Literature, American Economic Association, vol. 47(2), pages 373-447, June.).

Easterly, W., R. Levine, et al. (2003). "New Data, New doubts: A Comment on Burnside and Dollar's "Aid, Policies, and Growth" (2000)." National Bureau of Economic Research Working Paper Series **No. 9846**(published as Easterly, William, R. Levine and D. Roodman. "New data, new doubts: A Comment on Burnside and Dollar's 'Aid, Policies, and Growth' (2000)." American Economic Review 94, 3 (June 2004): 774-780.).

Ehrenpreis, D. (2007). "Analysing and achieving Pro-Poor Growth." Poverty in Focus **March 2007**.

Ehrlich, P. R. (1968). The Population Bomb. New York, Ballantine Books.

Engel, J. and P. Rose (2010) "Ethiopia's Story."

Feeny, S. (2005). "The impact of foreign aid on economic growth in Papua New Guinea." Journal of Development Studies **41**(6): 1092-1117.

Fogel, R. W. (2004). The escape from hunger and premature death, 1700-2100 : Europe, America, and the Third World. Cambridge, Cambridge University Press.

Gounder, R. (2001). "Aid-growth nexus: empirical evidence from Fiji." Applied Economics **33**(8): 1009-1019.

Grossman, G. M. and A. B. Krueger (1991). "Environmental impacts of a North American Free Trade Agreement." National Bureau of Economic Research Working Paper Series.

Hanushek, E. A. and L. Woessmann (2009). "Do Better Schools Lead to More Growth? Cognitive Skills, Economic Outcomes, and Causation." National Bureau of Economic Research Working Paper Series **No. 14633**.

Hsiao, W. and P. S. Heller (2007). "What Should Macroeconomists Know about Health Care Policy?" IMF Working Papers **WP/07/13**.

Kahneman, D. and A. Deaton (2010). "High income improves evaluation of life but not emotional well-being." Proceedings of the National Academy of Sciences **107**(38): 16489-16493.

Kraay, A. (2006). "When is growth pro-poor? Evidence from a panel of countries." Journal of Development Economics **80**(1): 198-227.

Layard, R. (2006). Happiness: lessons from a new science. London, Penguin.

Levine, R. (2007). Case studies in global health: millions saved. Sudbury, Jones and Bartlett Publishers.

Lindauer, D. L., L. Pritchett, et al. (2002). "What's the Big Idea? The Third Generation of Policies for Economic Growth [with Comments]." Economía **3**(1): 1-39.

McCully, M. (2011). "Speech to Resilience in the Pacific Conference." Retrieved 16.3.2011, from http://www.beehive.govt.nz/speech/resilience-pacific-conference.

Michaelowa, K. and A. Weber (2007). Aid Effectiveness in the Education Sector: A Dynamic Panel Analysis. Theory and practice of foreign aid. S. Lahiri. Oxford, Elsevier**:** 357-385.

Minoiu, C. and S. G. Reddy (2010). "Development aid and economic growth: A positive long-run relation." The Quarterly Review of Economics and Finance **50**(1): 27-39.

Mishra, P. and D. Newhouse (2009). "Does health aid matter?" Journal of Health Economics **28**(4): 855-872.

Mosley, P. (2004). "Severe Poverty and Growth: A Macro-Micro Analysis." **No. 51**.

New Zealand Aid Programme. (2010). "New Zealand Aid Programme: Overview." Retrieved 16.3.2011, from http://www.aid.govt.nz/library/docs/New_Zealand_Aid_Programme_oct_2010.pdf.

New Zealand Aid Programme. (2010b). "About." Retrieved 16.3.2011, from http://www.aid.govt.nz/about/.

New Zealand Herald. (2009). "NZ aid to the Pacific 'a failure': Govt." 16.3.2011, from http://www.nzherald.co.nz/politics/news/article.cfm?c_id=280&objectid=10569858.

Overseas Development Institute (2010). "Economic growth and the MDGs." ODI Briefing Papers **60**.

Rajan, R. G. and A. Subramanian (2008). "Aid and Growth: What Does the Cross-Country Evidence Really Show?" Review of Economics and Statistics **90**(4): 643-665.

Ravallion, M. (2009). "A Comparative Perspective on Poverty Reduction in Brazil, China and India." World Bank Policy Research Working Papers **WPS5080**.

Rodrik, D. (2006). "Goodbye Washington Consensus, Hello Washington Confusion? A Review of the World Bank's "Economic Growth in the 1990s: Learning from a Decade of Reform"." Journal of Economic Literature **44**(4): 973-987.

Roodman, D. (2007). "Macro Aid Effectiveness Research: A Guide for the Perplexed." Center for Global Development Working Papers **135**.

Sachs, J. D. (2003). "Institutions Don't Rule: Direct Effects of Geography on Per Capita Income." National Bureau of Economic Research Working Paper Series **No. 9490**.

Savun, B. and D. C. Tirone (2011). "Foreign Aid, Democratization, and Civil Conflict: How Does Democracy Aid Affect Civil Conflict?" American Journal of Political Science: no-no.

Spence, M. and M. A. Lewis (2009). Health and growth. Washington, DC, World Bank.

Stevenson, B. and J. Wolfers (2008). "Economic Growth and Subjective Well-Being: Reassessing the Easterlin Paradox." Brookings Papers on Economic Activity **2008**(1): 1-87.

UMR Research. (2007). "Overseas Aid A Qualitative and Quantitative Study." Retrieved 16.3.11, from http://www.aid.govt.nz/library/announcements/umr-overseas-aid-study-july07.pdf.

Weisbrot, M., D. Baker, et al. (2001). "Growth May Be Good for the Poor – But are IMF and World Bank Policies Good for Growth?" Center for Economic and Policy Research Briefing Paper.

World Bank. (2011). "World Bank World Development Indicators." Retrieved 16.3.2011, from http://data.worldbank.org/data-catalog/world-development-indicators.

Wright, J. (2010). "Aid Effectiveness and the Politics of Personalism." Comparative Political Studies **43**(6): 735-762.