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Aid conditionality and the Third World

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Aid conditionality is largely linked with the support given by the World Bank (WB) and IMF to Third World countries in foreign exchange crisis, i.e., payments difficulties. The IMF's original role was to provide liquidity for countries in balance of payments deficit, without any conditionality. It is controlled largely by the G7, the seven major industrialised countries. IMF pressure today is almost entirely on the deficit countries and accompanied by harsh conditionality. It has virtually no influence on the economic policies of the G7.

The WB conditionality is in the form of so-called Structural Adjustment Programmes (SAPs). This is a general undermining of the concept of sovereignty of Third World countries on which the UN Charter is based. Such conditionality was not envisaged initially in the WB and IMF when these institutions were set up at Bretton Woods in 1944. Then they were engaged in the post-war reconstruction of largely West European countries through financing specific projects. Project aid did not then require any specific change in the general policies of the recipient country. Of course, there were conditions associated with specific projects like commitment by the recipient government to provide local finance to make complementary investments for operation and maintenance.

In the 1970s, the WB/IMF were largely involved in lending capital to Third World countries, which arose from the recycling of the huge financial surpluses of the oil exporter countries through the commercial banks of the developed countries. In fact, no strict conditionality was imposed when money was lent in the 1970s and debt was building up, in contrast to the 1980s after the bubble had burst and the repayment of debt and balance of payments deficits became unmanageable.

Thus, only in the 1980s aid shifted to a programme of 'policy conditionality'. This coincided with the deepening recession in the developed countries, which in turn reduced the exports of the Third World in Western markets. Further, the rise in interest rates increased debt service charges and along with this the deteriorating terms of trade for primary commodities made the Third World more dependent on the international financial agencies.

The WB conditionality refers to supply side of the economy while the IMF conditionality refers to demand side. The WB is said to improve the supply efficiency of the economy by such measures as privatisation, promotion of free markets, investment, flexible labour markets and competition. IMF aims at reducing inflationary pressures in the economy by cutting government expenditure, encouraging saving, monetary discipline, stable exchange rates and trade liberalisation and focuses on short-run reforms. In the real world this distinction may be difficult to find as there are overlapping activities. The other important point is that bilateral aid and also private investment is conditional upon countries being given 'approval' by the WB/IMF. Bilateral aid can be cut off if a country fails to implement the WB/IMF conditions.

Both these institutions claim that the programmes embodying their conditionality are freely negotiated in equal partnership between governments and WB/IMF. But this is far from true. The recipient governments are under extreme pressure, with pressing debt obligations, lack of foreign exchange reserves and balance of payment deficits. They have little choice but to submit to WB/IMF conditions. The bargaining advantage is clearly on the side of the donor rather than the recipient, as when the aid is asked for the situation is often desperate and urgent.

However, if the WB/IMF backed programmes fail, the government will blame the WB/IMF and say that the conditions were too harsh and unrealistic. The WB/IMF on their part will say that the failure of the programme was due to a lack of political will on the part of the government or the result of political manoeuvring in the recipient country. Here both use one another as scapegoats for failure. If anyone is interested that the programmes should be genuinely implemented then the conditions attached to it should be freely accepted as being in the best interest of the country itself. The question is that if a country considers the conditions as best for its own interests, then there is no need to impose these conditions in the first place.

The WB and IMF play a crucial role in shaping the economic structure and political direction in most Third World countries. They claim to be non-political institutions carrying out a purely economic role in either financing large projects – in the case of WB – or helping an indebted country with its short-term balance of payments – in the case of IMF. The real advantage goes to Western countries which control international capital and have the military muscle to back it up and also the local elites who receive their share of the loot. On the other hand, many local producers are forced into bankruptcy because free entry of foreign capital pushes them aside. For the poor the situation worsens as the prices of staple food rise substantially along with unemployment.

Another fallacy applies to the case of devaluation which is an important part of the SAPs. Devaluation, for example, in country A is equivalent to overvaluation in B, C, D, etc., competing in exports with country A. Also, devaluation may appear as a monetary measure, but it has a great impact on other sectors depending on whether the economy largely produces for exports or are imports substitutes. And also the cuts in government expenditure will affect education, health, infrastructure, agriculture, or environment subsidies. Yet the health expert from the World Health Organisation, or Food and Agriculture Organisation of the United Nations are not involved in the negotiations; not even on the government side the ministries such as health, education, food and agriculture. While the SAPs have a deep impact on such sectors.

The SAPs criteria are too narrowly macro-economic and biased in favour of those who are already well-off. In the case of WB/IMF, the officials imposing the SAPs are unelected technocrats without a direct democratic political mandate and without much political accountability to any kind of electorate. Its success is measured by growth of per capita GNP, rates of inflation, foreign exchange, volume of export, etc. But such indicators totally neglect other important issues like reduction of poverty and malnutrition, living conditions of the weaker sections especially for women and children, situation of health, greater equality of income distribution, more employment, self-sufficiency in food production, environment, etc., although these are the real objectives of economic and sustainable development.

Many of the Third World countries military expenditure accounts for a big chunk of government expenditure. Yet the WB/IMF does not talk about this issue while focusing on reducing overall expenditure. Of course, local elites would be strongly opposed to it and so the Western arms exporters, who earn huge profits on arms exports while it is known that large number of people suffer from the lack of minimum food requirements. Yet without cuts in the military expenditure the cuts in government usually involved development expenditures and particularly on social expenditures on health, employment, education, etc. Here the contradiction with insistence on the observance of human rights is clear: less health, education, etc., expenditure violates the human right to access to education and health facilities. While the military expenditure, in fact, is used to suppress domestic opposition and ethnic groups, thus violating human rights.

The conditions fail to take into account different circumstances, economic history, political systems and cultures of individual Third World countries. In fact, to a considerable degree the Structural Adjustment Programmes contains identical features, such as more emphasis on exports, the reduced role of government, removal of subsidies, low inflation and import liberalisation. The SAP does not make great differences between the Third World countries. Another important criticism is that WB/IMF officials often stay for a very short period (often not more than 2-3 weeks) and do not know enough about the real conditions in the countries. Further, most of these so-called WB/IMF experts are largely biased in favour of the neo-classical theory and all solutions are supposed to be found by following that theory.

The WB and IMF are important actors, the internal composition of these institutions reflects the principal donor countries, primarily the US, Germany and Japan. The WB/IMF strategies are themselves shaped and given substance by the competing economic superpowers. In this context, the liberalisation in the Third World should be examined not merely as an outcome of local ruling segments or international financial institutions, but rather shaped by the strategic economic needs of US capital. The primary fact in the post Cold-War world is the increasing competition for dominance of world markets by the US, Germany and Japan. Each economic superpower has carved out regions of domination from which to reach out to undercut competition. The US has over the past two decades lost competitive advantages in a number of product areas such as automobiles, electronics, etc. As a result, the US has been piling up a huge trade deficit with Japan and other East Asian countries and to a lesser degree with Germany. The US trade surplus with Latin American countries serve to compensate for negative trade balances with Asia and Western Europe. Low cost production in Latin America allows US producers to compete overseas and in the US market. In this context the liberalisation of Latin America was essential to providing US capital with access to markets and earnings. Liberalisation in the early 1970s was pursued via WB and IMF with full US support: Latin American dictators who promoted liberalisation were financed and supported; electoral transitions were brokered by US on condition that new elected regimes deepened the liberalisation process. In Latin America, insofar as liberalisation 'works', it has worked primarily for the benefit of US-based TNCs and banks but most importantly for the US political economy as a whole.

We should note here that earlier implicit policy conditionality during the Cold War did not raise the same problem: all the donors were interested in whether the country was on 'our' side or whether it was on 'other' side, macro-economics were less important for that. After the end of the Cold War, the donor countries are often trying to impose Western type of multi-party democracy on countries with different culture and social traditions. In countries with ethnic divisions, for example, such as the case of many African countries, there is a danger that different political parties will be associated with different ethnic groups – hence a struggle between political parties may easily result in ethnic conflict. Genuine democracy in such countries may be expressed by more accountability, less corruption, observance of human rights, better treatment of ethnic and religious minorities and self-determination at the local levels. The basic human rights should also include right to have employment, food, housing, education, etc.

Indeed, any reform intending the well being of the Third World must start with better terms of trade, cancellation of debts, lower interest rates and an end to arms exports. The objectives should be the reduction of poverty, employment creation, improvement of environment and ecology. The conditions should be more related to the specific circumstances of each country and its economic situation. In spite of what we may hear about all the changes going on within the WB and IMF, one thing remains clear: both organisations remain firmly planted in an economic order that exults profits and growth over sustainability and people. In fact, liberalisation is a product of Western economic policy-makers, bankers and TNCs allied with the Third World elites. It is specific class and state interests that dictate the new liberal political economy.

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