Bauer's "Foreign Aid, Forever? Critical Reflections on a Myth of Our Time"– 50 years later

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Abstract: *The theory and practice of international development assistance has undergone profound changes since the 1960s. Originally, aid intended to combine external finance with technical assistance to eliminate three gaps believed to prevent development: the investment-domestic savings gap, the foreign exchange gap, the capacity gap. Since the 1990s, the scope expanded with increasingly deeper involvement in the internal affairs of low-income countries (financing of "national public goods" and changing the governance structure); simultaneously a growing share of finance is directed towards "global goods" issues (environment, refugee crisis, etc). Since the 2000s China emerged as a heavyweight in international development finance, financing large-scale infrastructure investments in transport and energy with loans at near-commercial terms. Presently both approaches – the Western and the Chinese – need adjustments to make them more relevant for today's global challenges. The essay presents some of the contradictory conclusions of research on the effectiveness of foreign aid and concludes with recommending a new finance structure, which concentrates foreign aid on three topics: production of global goods, humanitarian assistance and creating a more level playing field for entrepreneurs in developing countries.*

The 1960s theory of economic development and aid

In the 1950s, nine countries in Southeast Asia, four in the Middle East, and two in Sub-Saharan Africa gained their independence; in 1960 fifteen sub-Saharan African countries were added to the list.[1] There was a consensus among Western economists and politicians that the countries needed external assistance for development. Zaire, for example, had in 1960 only 18 university-educated national staff; and the infrastructure of the former colonies was built primarily to satisfy the need for 'North-South' trade in goods, not for internal and regional economic development. There was also a consensus that the knowledge for how to deliver effective assistance by donors was available. The Marshall Aid of 1948-1951 had demonstrated how the combination of know-how transfer and financial assistance could deliver economic growth. Economic growth theory, including Rostow"s "Five Stages of Economic Growth",[2] showed the development path. The "Cobb-Douglas" model of economic growth[3] along with the theory of the 'double financial gap'[4] justified the need for financial assistance. Technical assistance could address problems of limited 'absorption capacity'[5]. Therefore, when the Danish Parliament in 1962 passed the "Law on Cooperation with developing countries", it was unanimous.

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[1] The list of countries can be found at https://en.wikipedia.org/wiki/Year_of_Africa

[2] Rostow's five stages are: Traditional Society. Preconditions to Take-off. Take-off. Drive to Maturity. Age of High Mass Consumption

[3] In its simplest form, the model sees a country's economic growth rate determined by its savings ratio divided by the investment output ratio.

[4] The theory sees the development of less developed countries limited by two gaps: (i) domestic savings are too small to finance a level of investment needed to create "take-off"; (ii) export earnings are insufficient to finance imports needed for development.

[5] The theory sees developing countries' ability to absorb financing and investment flows in their initial development limited by insufficient technical-administrative capacity.

Peter Bauer's critique of foreign aid

A few critical voices were raised. In 1973, when the United Nations passed a resolution calling on rich countries to spend 0.7% of their GDP on foreign aid, Professor P.T. Bauer, a long-term critic of foreign aid, summarised his points in the article "Foreign Aid, Forever? Critical Reflections on a Myth of Our Time".

Present day foreign aid can be broken up into three main components: *"development aid"* (physical infrastructure, institutional development, health, education, poverty alleviation), *humanitarian aid* (starvation, natural disasters, support to refugees), "*global common goods"* (climate change mitigation& adaptation, biodiversity, pandemics, transport- and digital interconnections, peace keeping forces).

Climate aid was non-existent in 1974 and Bauer did not attack humanitarian aid. His question mark concerned development aid, calling it an act of faith: "The case for foreign aid is regarded as axiomatic, so that either progress or lack of progress can be used to argue for more aid". Bauer's overall economic argument against aid as a tool for progress was simple: "where the mainsprings of progress are present, material progress will come about without foreign aid; where they are absent, no amount of aid will help". The two-gap model is a myth: if poverty prevents sufficient capital accumulation, development into modern industrial societies could not have happened in the past. When conditions for development are present, capital will be generated locally or supplied to governments and businesses from foreign sources of finance on a commercial basis. Bauer noted "a patronizing attitude pervades the whole discussion on aid" and asserted a number of negative repercussions of aid on the internal situation of recipient countries, claiming that the official aid "reinforces the disastrous tendency to politicise life in poor countries"; "influences policies into inappropriate directions by promoting unsuitable external models" and that "the hand-outs increase the power, resources, and patronage of governments compared to the rest of society".

The late 1980's Washington consensus model for development finance

In the following decades, the majority of international development aid of several trillion dollars up to 2020 was used for the development of basic infrastructure in the form of roads, bridges, hospitals, schools, water and energy supply, as well as for capacity and institution building. It was not pure altruism: until the collapse of the Soviet Union in 1991, foreign aid was the main political and economic instrument in the east-west conflict's race for sympathy in the "Third World".

The collapse of the Eastern bloc in the late 1980s removed the Soviet-Russian planned economy as a competing model of inspiration in developing countries. This led to the conviction that the Western system, with its combination of an open liberal economy dominated by the private sector and governed by a democratically elected government, was the surest recipe for economic growth. Donors and many developing countries accepted the so-called "Washington consensus" (between the World Bank and the IMF) that fiscal discipline, the liberalisation of financial markets, the privatisation of state monopolies, the removal of trade barriers and foreign direct investment were the most effective means of driving growth in developing countries. An increased inflow of private funding was a necessity, as the implementation of high-value investments in infrastructure in the developing world called for a volume of finance far higher than the amount which donor and government money could provide.

Until then, many developing countries had experimented with different development strategies, such as import substitution (especially in Latin America) and government planning, with the creation of state enterprises to build essential infrastructure and a national manufacturing industry. The new paradigm of private sector-driven development led developing countries to open their economies and financial markets in the 1990s and early 2000s to ensure easier access to foreign capital and trade. The paradigm recommended the deregulation and privatization of former monopoly markets. The objective was to increase investment in the sectors through larger inflows of private finance and achieve higher efficiency through competition. The markets for the supply of water and electricity were typically divided into 'commercial areas' in densely populated cities where suppliers did not receive subsidies, and 'non-commercial areas' in sparsely populated rural areas. In the latter, infrastructure and operation were supported by subsidies to suppliers, so that the price of services could be kept down to a level reflecting the ability of households to pay. In this context, "smart subsidies" – identification of public finance instruments which can minimise public spending needed to achieve specified objectives - became a buzz-word in development aid. Some middle-income countries managed to implement comprehensive reforms to promote private investment in infrastructure, whereas low-income countries were able only to introduce a few elements.[6]

"Leverage of private finance" became another buzzword: mobilizing private capital for priority projects and sectors through structured finance instruments in which a grant component provides risk cover for international development banks and private investors. Examples include public credit guarantees, 'blended finance', where grants from a donor co-finance a project with a loan from a development bank, and 'layered investment funds', where a grant of 10-20% of the fund's capital finances a first loss-absorbing upper tier. Since investments in infrastructure in developing countries have a higher risk than in developed countries, private investors (project developers, investment funds and commercial banks) demand a higher financial return as compensation. In this context, risk reduction fulfils two main purposes. One is to increase the amount of private capital which is made available for investments in developing countries. Regulations prevent 'institutional investors' (insurance companies and pension funds) from investing in projects whose risk level exceeds a red line. Development banks such as IFC, EBRD, EIB, EBRD, IFU make co-financing of a private project dependent on the investment not exceeding a defined risk threshold. Since they obtain the funds for their loans by issuing bonds on the international capital market, they must protect their 'AAA rating' in order to avoid rising prices for their borrowing. The other purpose is to improve the cost competitive position of capital-intensive clean energy technologies versus less capital-intensive fossil energy technologies.

Result of the Washington consensus model: mobilisation of private North-South finance

The model succeeded in mobilizing private capital. During 2010-2019, external private funding of public borrowing by developing countries increased 10% per year compared with 2% for funding from public sources. Whereas in 2010, funding from public sources was twice as high as from private ones (commercial bank loans and the sales of government bonds on the international capital market); in 2019, the two funding sources were of equal size.[7] The trend was facilitated by demand and supply side factors. Economic growth moved some countries out of the low-income group that

[6] Vivian Foster & Anshul Rana: "Rethinking power sector reform in the developing world", World Bank 2020
[7] Akihiko Nishio & Gaiv Tata, "How the structure of global aid and development finance is changing". Brrokings.edu future development blog. November 3, 2021

can receive World Bank's concessional IDA loans.[8] The World Bank's more expensive IBRD loans[9] - granted to middle-income countries – carry an interest rate which is only marginally lower than for debt finance from the international capital market (terms depend on the country's credit rating). Western countries' quantitative easing after the 2008 financial crisis increased the price of bonds, lowering the returns on investments in these. In pursuit of higher yields investors increased their risk acceptance and took a greater interest in emerging markets. This widened the range of countries that were able sell sovereign government bonds on the international capital market.

Commercial global foreign direct investment (FDI) was worth $1.54 trillion in 2019; of which, however, only $45 billion (=2.9%) was invested in Africa.[10]

The diaspora's financial transfers increasingly cover developing countries' need for external finance and hard currency. From 2000 to 2016 transfers to the 54 member countries categorised by the IMF as "Low-Income Developing Country, LIDC" (GDP less than $2,700 per capita in 2016) rose from $10 billion to $80 billion, while development finance defined as ODA rose from $10 billion to $30 billion.[11]

Private philanthropy is a source of funding for niche projects such as the fight against AIDS. In the 2016-2019 period, donations from 205 funds averaged $10.6 billion per year; 13% of it went to the poorest countries.[12]

Mission creep in Western development finance from the 1990s onwards

The increased mobilisation of private capital led Western donors in the 1990s and 2000s to reduce the proportion of aid going to 'hard investments' in physical infrastructure and instead increase the proportion of aid going to the 'soft sectors' of health, education and alleviation of extreme poverty;[13] that is, to co-finance the provision of 'national public goods'. Within the framework of the OECD Development Assistance Committee (DAC), donors agreed to eliminate 'tied aid' which binds goods and services financed by foreign aid to supplies from the donor country. In the 2005 Paris Declaration donors promised to coordinate their aid programs and give the beneficiary countries a greater say in their content.[14]

At the same time, a 'global common good' theme entered the international development agenda: the pressure on the global environment and the resulting demands for 'sustainable development'. In 1987, the World Commission on Environment and Development (WCED), set up in 1983, published the report "Our common future" (known as the Brundtland Report). It states that global environmental problems are due to overuse of resources in the North ('non-sustainable consumption and production' patterns) and extreme poverty in the South. At the United Nations

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[8] In 2022, the upper limit for access to IDA loans is a GDP per capita of USD 1,205.

[9] The interest rate on IBRD loans covers the price of bonds that the World Bank sells on the capital market, plus the bank's general administrative costs plus a small profit used for partial subsidization of IDA loans

[10] Source: UNCTAD: "World Investment Report 2020".

[11] The amounts numbers do not include Nigeria. IMF: "Macroeconomic developments and prospects in low-income developing countries", 2019.

[12] OECD: "Private philanthropy for development – second edition. Data for Action". 2022

[13] Mainly through targeted assistance to improve access to electricity, clean water, health, education.

[14] The Paris-Declaration's five principles for development aid are: ownership, alignment, harmonisation, managing for results, mutual accountability. These were subsequently expanded in Accra.

Conference on Environment and Development (UNCED) held in Rio in 1992 this led to the adoption of two conventions: the United Nations Framework Convention on Climate Change (UNFCCC) to counteract global warming caused by greenhouse gas emissions and the Convention on Biological Diversity.

Environmental assistance became a component of bilateral and multilateral development programs without leading to an expansion of international development aid. During the 1990s, the Western countries awarded themselves a double peace dividend from the break-up of the Soviet Union: they reduced their defense expenditure as well as their development aid in percent of GDP. DAC-countries ODA fell from 0.55% of Gross National Income (GNI) in 1960 to 0.35% in 1970, to 0.25% during the 1990s; since 2000 it has fluctuated around 0.30%.[15] The trend reveals that some aid in previous years had served geopolitical purposes. Denmark was an exception. In 1992, development aid reached 1% of GDP. On top of that came in 1993 funding from the new MIKA (Environment and Disaster) program, jointly administered by the Ministry of the Environment and the Ministry of Foreign Affairs. In 1998 it was renamed MIFRESTA (Environment, Peace and Stabilization) with an annual budget intended to increase gradually to 0.5% of GDP by 2005. MIFRESTA was abolished in 2003. The concept of additional finance for environment protection returned in 2009 at the COP-15 meeting in Copenhagen, where developed countries pledged to provide 'additional climate finance' of $100 billion annually by 2021.

Promotion of women's equality became an important 'cross-cutting consideration' in the approval and implementation of aid projects. In the 2000s, the concept of applying a "human rights-based" approach to poverty eradication and development spread in Western development aid. Democracy programs promote knowledge of fundamental democratic rights and principles, provide support to civil society organizations, to strengthening the country's legal systems, to combat problems of widespread corruption through good governance programs and to assist national parliaments with improving their administrative systems and procedures. While the World Bank's Statute instructs the Bank not to take a position on the internal political affairs of client countries, the European Bank for Reconstruction and Development (EBRD) was established in 1991 with the explicit mandate formulated in Article 1 to operate in countries that "commit themselves to and apply the principles of multiparty democracy, pluralism and market economy".[16] Some Western countries even engaged in military action in Iraq, Libya and Afghanistan to force 'regime change' from authoritarian to democratic rule.

'Mission-creep' – gradual shifts in objectives leading to more and more purposes being taken into account in development aid – accelerated after 2000. In 2000, the UN adopted eight Millennium Development Goals for 2015.[17] The hugely inspirational Development Goals for 2030, adopted in 2015, comprise 17 development objectives and 169 sub-objectives.[18]. The goals are to be achieved

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[15] The development is shown in a chart at Official development assistance - Wikipedia

[16] This led the EBRD to e.g. suspend all sovereign operations in Uzbekistan after the brutal government crackdown on political opposition in 2005.

[17] The goals are: Eradicate extreme poverty and hunger. Achieve universal primary education. Promote gender equality and empower women. Reduce child mortality. Improve maternal health. Combat HIV/AIDS, malaria and other diseases. Ensure environmental sustainability. Develop a global partnership for development.

[18] The goals are: No poverty. Zero hunger. Good health and well-being. Quality education. Gender equality. Clean water and sanitation. Affordable and clean energy. Decent work and economic growth. Industry Innovation and infrastructure. Reduced inequalities. Sustainable cities and communities. Responsible

as common responsibility, in a "Global Partnership for Sustainable Development", where "each country has primary responsibility for its own economic and social development", but "public funding, both national and international, will play a vital role in providing essential services and public goods and catalyzing other sources of funding."

On the heels of the 2015 migration crisis which hit several EU countries, then-German Chancellor Angela Merkel suggested that the EU launch a Marshall-Aid like plan for Africa to eliminate the root causes of migration. Whereas *absolute poverty* is a causal factor for internal displacements and South-South cross-border migration, the belief that it is the major driver of South-North migration is misled. Poor people earning less than $2 a day cannot afford to pay people smugglers $5,000-15,000; only middle-class families can raise such sums. South-North migration is driven by *relative poverty,* the huge differences in GDP per capita, and by the relative scarcity of quality jobs in countries which experience high population growth. Slightly rising per capita incomes will increase the number of middle-class families which can finance migration attempts. Equally naïve is the expectation of some EU Governments that reducing access to development aid can pressure governments to repatriate citizens who have entered irregularly into the EU.[19] Remittances, including from irregular migration, are important for their economies and the population would react violently against what would be perceived as racist pressure. Negotiations on the repatriation of irregular migrants must be conducted within agreements to facilitate regular migration.

The entry of China in development finance from 2000 onwards

The world's belief in the superiority of the Western system was undermined by the financial crisis of 2007-2009 and by China's economic growth, which raised its share of world GDP from 2% in 1980 to 19% in 2019.[20] China's ability to lift hundreds of millions of its inhabitants out of deep poverty within 20 years showed the world that there is an alternative effective development paradigm: state-driven growth led by an authoritarian regime. China's ability to influence economic policies was enhanced by its increasing impact on the economic situation of developing countries. China's rapidly growing demand for imported raw materials, which from the year 2000 drove up international commodity prices[21], triggered a commodity boom, which pushed growth in many developing countries. The explosive increase in imports of goods from China[22] in emerging economies is accompanied by an inflow of Chinese contractors who work or settle locally.[23]

The adoption by the People's Congress of the "going out"/"going global" initiative in 2000 led to a dramatic expansion of China's lending to developing countries. The economic objective of China's development funding is to strengthen the globalisation of Chinese companies. The political objective is to change the international governance structure for development aid and break its Western

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consumption and production. Climate action. Life below water. Life on land. Peace, justice and strong institutions. Partnerships for the goals.

[19] The Danish development strategy "Common about the World" adopted in 2021 states "As a starting point we will not give long-term development assistance to states that refuse to accept their own nationals".

[20] https://www.silkroadbriefing.com/news/2019/07/04/us-1-billion-belt-road-africa-fund-launched

[21] The oil price per barrel rose from $20 (expressed in real terms 2021 prices) in 2000 to an all-time high of $156 in 2008. Source: Historical Oil Prices Chart (inflationdata.com)

[22] In the 1980s, China's trade with Africa amounted to $10 million per year, in 2006 it reached $55 billion.

[23] The number of Chinese settlers in Africa is estimated at 1 million in 2018, plus just over 200,000 workers. An estimated 200,000 Africans work in China. Source: https:// en.wikipedia.org/wiki/Africa-China_relations

dominance. The policy received a practical expression in 2013 with the adoption of the “Road and Belt” initiative, which aims to create six economic corridors to connect up to 65 countries more closely with China's economy. In 2014, the Silk Road Fund was set up with a capital of $40bn.

The slogan for China's development cooperation is the implementation of "mutually beneficial projects" to build a "global community of shared future". The idea is that inadequate infrastructure is blocking economic growth in the partner countries and that, by remedying shortcomings in these, mutual benefits in terms of increased trade are created.[24] China funds major infrastructure projects, especially in transport (railways, ports, airports, highways) and in energy, as well as investments in oil and mining. Financing is offered without being conditioned on internal reforms, and the approval and implementation of projects is faster than when loans are approved by international development banks. A policy of ‘no questions asked' is pursued and construction contracts are not awarded through open bidding, but given to Chinese companies.

Economic infrastructure projects are financed by the China Development Bank and by the major state-owned commercial banks: Industrial and Commercial Bank of China, China Construction Bank, Bank of China, Agricultural Bank of China, as well as by individual non-state-owned banks. The loans are non-concessional, i.e. close to the conditions of the private capital market, and require solid collateral. For example, in the form of a mortgage on the financed infrastructure (port in Sri Lanka, power grid in Laos); by placing future revenues from the funded project in an "escrow account" from which money is drawn first for loan repayments before any other purposes can be funded (Uganda Airport), by collateral in the revenues of the country's oil exports (Angola and Venezuela). From 2008 and 2019, the China Development Bank and Export-Import Bank of China lent US$462 billion, which matched the World Bank's US$467 billion during the period.[25]

Chinese development aid in a form similar to ODA (Overseas Development Assistance) is of modest scale, never reaching more than $3bn per year during the 2003-2019 period.[26] Grants are used to finance technical assistance, welfare projects and humanitarian aid; interest-free loans are given for the construction of public facilities, concessional loans finance economic and infrastructure projects.[27] Both types of loans are granted only against sovereign guarantee. The implementation is split between China International Development Cooperation Agency (CIDCA) established in 2018 and Export-Import Bank of China; the former manages the grant and interest-free loans, the latter the concessional loans.

China attacked the Western institutional dominance directly in 2015 with the creation of two multinational development banks: the Asian Infrastructure Investment Bank (AIIC), based in Beijing, which at present has 105 members, and, the New Development Bank (NDB) based in Shanghai which since its creation has Brazil, India, Russia and South Afrika as co-owners.[28]

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[24] Estimates of the impact on trade, economic growth and foreign direct investment can be found in the report ”Belt and Road Economics. Opportunities and Risks of Transport Corridors”. World Bank. 2019

[25] Source: China pulls back from the world: rethinking Xi’s ‘project of the century’, FT 12.12.2020

[26] China Africa Research Initiative: “Chinese Global Foreign Aid” (sais-cari.org)

[27] State Council of the PRC: “White paper on China’s international development cooperation”. 2021

[28] Bangladesh, United Arab Emirates (UAE), Uruguay and Egypt joined the bank in 2020.

China succeeded in breaking the western world's dominant position in international economic cooperation. In 2018, more African leaders attended the Forum on China-Africa Cooperation (FORAC) meeting in Beijing than at the UN Annual General Assembly two weeks later.[29]

Challenges faced by the Chinese approach to development finance: need for rethink

China's focus on large commercial loans for infrastructure projects, which are approved quickly and without conditions for the implementation of economic reforms, was so popular on the borrowers' side, that China upended the international structure for the financing of sovereign loans. While low-income countries[30] owed three quarters of their $65 billion debt to Paris-Club countries in 2006; in 2021 they owed more than half of their $200 billion debt to China and less than a third to Paris-Club countries.[31] The rapid growth in lending from China caused the public debt of the low-income countries to move from 33% of their GDP in 2013 to 48% in 2021. This eroded their debt repayment ability. By 2021, 55% of low-income countries were either in debt distress, or exhibited "high risk of debt distress," compared to 23% in 2013.[32] China joined the debt relief initiatives of the G-20 cooperation in 2020 and 2021, although very tentatively.

The debt situation weakens China's soft power propaganda, which recommends the country's development model as inspiration for application in other countries. China's growth model used a domestic savings ratio of over 40% of GDP to finance huge investments in both infrastructure and in building an internationally competitive manufacturing industry. The average savings ratio of most low-income countries was and is less than half that rate and their ability to repay foreign borrowing was and is limited by the absence of an internationally competitive industry - high-productivity sectors are typically found in the mining sector as low-employment enclave economies.[33] Countries without large oil and mineral deposits experience large trade deficits. In 2015, Kenya imported $5.9 bn in goods from China (much of it for materials for the Mombassa-Nairobi railway) and exported $99 million to China. Africa's large trade deficit with China - $46 bn in 2016 - prompts African governments to react and demand that China makes active efforts to develop imports from Africa, including the creation of African companies that can be subcontractors for Chinese manufacturers.

China has begun to adapt its funding to the fragile debt capacity of its loan-recipients. At the Belt and Road Forum for International Cooperation held in Beijing in 2017, President Xi Jinping called it the project of the century and talked about an investment volume of over $1 trillion which China was willing to fund. But in both 2020 and 2021, China's Belt&Road funding of $60 billion, was 48% below 2019 levels.[34] The three-year cooperation budget of $40 billion presented by China at the Forum on China-Africa Cooperation (FOCAC) meeting in November 2021 was a third less than the $60 billion pledges made at FOCAC meetings in 2015 and in 2018.

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[29] More African presidents went to China's Africa forum than UN general assembly — Quartz Africa (qz.com)

[30] The 69 countries in Africa, Asia and South Africa that have access to loans from the IMF's interest-free Poverty Reduction and Growth Trust (PRGT).

[31] Kristalina Georgieva and Ceyla Pazarbasioglu:" The G20 Common Framework for Debt Treatments Must Be Stepped Up" IMF Blog 02.12.2021

[32] IMF Policy Paper:"Macroeconomic Developments and Prospects In Low-Income Countries-2021. March 2021

[33] Professor Dani Rodrik's lecture "The Future of Growth in Developing Countries" on Youtube highlights how important employment in industry is for a country's take-off; and how difficult it is for Sub-Saharan Africa to follow this path.

[34] Christoph Nedopil Wang: "BRI Investment Report 2021", Green Finance Development Center, Fuhan University. 2022

China has become more aware of the need to avoid problems of corruption[35], funding white elephants[36] or causing environmental damage. Increasing environmental awareness within China and negative public reactions to environmental problems created by Chinese projects abroad led the Ministry of Commerce (MOFCOM) and Ministry of Ecology and Environment (MEE) to issue "Guidelines for Greening Overseas Investment and Cooperation" in 2020 and "Guidelines for Ecological Environmental Protection of Foreign Investment Cooperation and Construction Projects" in 2022.

Soft topics and support for global goods are being given greater weight in China's development assistance. At FORAC 2021, poverty alleviation (technical assistance for smallholder production) received more funding and China pledged to donate 1 billion doses of corona vaccines to Africa. At the UN General Assembly in September 2021, Xi introduced the 'Global Development Initiative' (GDI) as a complement to the BRI to support sustainable development with grants and capacity building. The main stated objectives are (i) to accelerate the implementation of the 2030 Agenda in close cooperation with UN agencies and interested collaboration partners and (ii) to help developing nations adjust to the COVID-19 shock with a focus on greener and healthier global development. In January 2022, the 'Group of Friends of GDI' was initiated at the United Nations as a consultation forum, and has been joined by more than 60 countries.

Challenges faced by the Western approach to development finance: need for rethink

The OECD/DAC countries' aid concept, characterized by a high share of funding in the form of grants and a broad field of objectives and internal interventions, also faces pressures for change.

One issue is the impact of mission creep on the effectiveness of development aid. The broadening of objectives leads to less clarity about what donors consider important and less important in aid[37] and to institutional fragmentation. From 2000 to 2019, the number of institutions channeling official aid to developing countries increased from 191 to 502 and the number of countries and multilateral institutions providing official funding from 47 to 70[38]. Institutional fragmentation is a response to the fact, that addressing the challenges of a more complex globalised world requires more specialized institutions. But is also a consequence of donors attempting to address too many issues. Lack of focus led donors during the last twenty years to reduce the number of staff in their aid administration and to replace technical experts with generalists.

[35] Dr Mahathir, Malaysia's Prime Minister, renegotiated in 2018 loan terms entered into by his corrupt predecessor Najib Razak, cancelling both the $20bn expensive East Coast Rail Link belt-and-road project and two oil pipelines in Sabah province.

[36] In 2014, a motorway project in Montenegro, which the EIB refused to finance as non-economic, received a €944 million loan from the Export-Import Bank of China. The project ran out of money before the completion of the construction. Montenegro has payment problems and tried to get the EU to take over the loan, which was rejected.

[37] "World in 2030 Denmark's development policy and humanitarian strategy" from 2017 mentioned which of the 17 Sustainable Development Goals were important for the strategy. The new strategy adopted in 2021 "Common about the World" has no explicit priorities.

[38] Akihiko Nishio and Gaiv Tata: "How the structure of global aid and development finance is changing". November 3, 2021. www.brookings.edu

Another is the geopolitical realization that China's funding of large infrastructure has given China a higher visibility and popularity than Western donors' funding of budget support and soft projects.[39] That Chinese technical standards spread in sectors such as railways and digitalization became a cause for concern for Western economic interests. Therefore, funding of large infrastructure projects is back on the DAC countries' priority list. In June 2021, the US launched the Build Back Better World (B3W) initiative, an infrastructure partnership to mobilize public and private capital for investments in climate, health and digital technology. In December 2021, the European Commission launched the 'Global Gateway Initiative' (GGI), which promises to mobilize up to €300 billion between 2021 and 2027 for projects in green and digital transformation and for developing links in transport, health, education and research systems across the world. The G7 Leaders' Summit in June 2022, launched the 'Partnership for Global Infrastructure (PGII)'. The initiatives emulate the BRI concept in two aspects: (i) although they also finance health and education, a great share concerns the financing of infrastructure projects which promote interconnections and transnational cooperation between the involved countries; (ii) grants make up a small share of the finance, which mostly is development bank and private finance.[40] The PGII raises two question marks. (i) Is the high reliance on debt finance the right response to the needs of the targeted countries, at a time when many of these face a debt crisis? (ii) Is there a qualitative difference between the PGII-supported projects and projects financed by investors from non-PGII countries; or does the PGII serve to strengthen the international competitive situation of PGII-investors? As example: what is the added value of the contract of the U.S. firm AfricaGlobal Schaffer Sun Africa (Miami, FL), with the Government of Angola to develop a $2 billion solar project in four southern Angola provinces [41] compared to Masdar's agreement with Tanzania Electric Supply Company Ltd. (TANESCO) to develop renewable energy projects with a total capacity of up to 2 GW, or Dubai's Solen Renewable's investment in the 120 MWp Ayémé Plaine solar PV in Gabon?

In addition, the PGII Initiative suffers from another weakness of Western aid: its paternalism. Despite years of rhetoric about programming development assistance in partnership between donor and recipient, the interests of donors continue to play an overly dominant role in the selection of cooperation themes. The EU Commission's 'A Comprehensive EU Strategy for Africa Trade and Investments' from 25 June 2020 insists, that it involves "a shifting from a donor-recipient model to a relationship based on mutual cooperation". Yet, African commentators criticize that the EU Global Gateway initiative was launched without previous consultation with African leaders, whereas China held consultation meetings for several months ahead of the Forum on China-Africa Cooperation in 2021.[42] In addition, the EU's presentation of the initiative is heavy with 'virtue-signaling' about the

[39] According to Afrobarometer: "Africans' perceptions about China: A sneak peek from 18 countries" 3 September 2020, 59% of respondents believed that China's political and economic influence was predominantly predominant, while only 46% of respondents thought the same about the assistance of the former colonial powers.

[40] The expected composition of GGI's €300 bn: €18 billion grant funding from the EU budget. €145 billion in loans from European financial and development finance institutions. €135 billion of private finance to be leveraged by €40 bn in guarantees from the European Fund for Sustainable Development+ (EFSD+)..

[41] For a short description read: White House FACT SHEET: President Biden and G7 Leaders Formally Launch the Partnership for Global Infrastructure and Investment. June 26, 2022

[42] Faten Aggad of Algeria, previous advisor to the African Union's high representative on Africa-EU negotiations quoted in Chloé Farand: "As EU seeks to rival China's infrastructure offer, Africans are skeptical". Climate Home News 20. dec. 2021

promotion of Western values.[43] Value promotion statements from DAC countries are popular with the domestic OECD country audience. But moralization from previous colonialists backfires in the ears of the external cooperation partners. Although EU countries in 2018 provided 46% of total ODA aid to Africa, and Africa's trade in goods with EU countries worth €235 bn was almost double their €125 bn trade with China[44,] some African voices criticize that "China provides bridges, the EU admonishing lectures."

The paternalism of DAC donors finds its strongest expression in the belief that externally financed democracy promotion programs can trigger structural change towards more democracy and respect for human rights in recipient countries. The results of 30 years of action can be seen in the annual democracy index published by the Economic Intelligence Unit (EIU) by the Economist. The index score assesses the situation in five areas: electoral process and pluralism, civil liberties, government function, political participation and political culture. Under the unipolar world order of the 1990s and early 2000s, the number of countries classified to some extent as having a democratic form of government increased. Beginning in 2010, the trend reversed. In 2020 the index fell to its lowest level since the start of the 2006 polls. The ambitious attempts of regime change through military intervention suffered a crank fate in Afghanistan, Iraq and Libya. Bosnia-Herzegovina's constitution and political structure, introduced with massive external expertise, is a prescription for the creation of a 'failed state'. The institution of a UN High Representative for Bosnia and Herzegovina with authority to adopt and repeal laws was established to support the reconstruction of Bosnia and Herzegovina. It is still in place 27 years after the conclusion of the Dayton Agreement.

Capacity-building 'bottom-up' activities at grassroot level - building the capacity of local civil society organisations to act as advocates for marginalised groups, promoting the role of women as economic and political actors and improving two-sided communication and interaction between local authorities and citizens – make sense. Yet, whether the capacity-building of civil society leads to real improvements in the country's political-social-economic decision-making processes depends on the goodwill of local politicians and elites. The elite will listen to the voices of civil society only if it serves its interests, while public support for newly created democratic institutions depends on citizens being able to see improvements in their economic and social situation. The people of Afghanistan in 2004 and Iraq in 2005 flocked enthusiastically to the ballot box because they believed that by allowing their voices to be heard they could promote economic and social progress; in the 2019 elections, the turnout was below 50%. Evaluations of Danida's democracy and human rights efforts are laudatory, but have difficulty in documenting impact. It is questionable whether sending experts is cost-effective when intelligent use of the Internet makes it an excellent instrument for the worldwide exchange of information, ideas and insights. It makes sense to direct donor efforts towards improving the global internet as a medium for promoting democratic values and human rights. The 'Tech for Democracy Initiative' by the Danish Ministry of Foreign Affairs is a promising example of this approach.[45]

The paternalism of the DAC countries is rife with double standards. At the COP-26 meeting in Glasgow in 2021, 20 Western countries adopted a declaration to stop using public funds to finance

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[43] See EU Commission's factsheet "global-gateway-partnerships.pdf". December 2021

[44] Explainer: "Towards a Comprehensive Strategy with Africa".- Modern Diplomacy March 12, 2020

[45] Find information about the program at www.techfordemocracy.dk. See videos with the presentations from The International Conference Tech for Democracy, 18 November 2021.

'unabated fossil-fuel projects' abroad. The policy argument is that developing countries by leapfrogging into renewable energy can avoid repeating the failure which the developed countries made by locking themselves into a fossil-fuel based energy structure with long economic lifetimes. Meanwhile, donors continue to approve fossil-fuel using energy projects in their own countries. In 2022, the European Commission included natural gas in its 'green energy taxonomy' list.

The 1992 Rio Conference Declaration on Environment and Development states in Principle 7: "In view of the different contributions to global environmental degradation, States have common but differentiated responsibilities". There is agreement that rich countries and poor countries have 'differentiated responsibilities' in climate cooperation. The extent of the rich countries' responsibility, however, is a contentious issue.

The rich OECD countries have not yet fulfilled their COP 2009 pledge of $100 bn per year in additional climate finance to be reached by 2020. According to OECD, 'additional climate finance' from DAC-countries in 2019 amounted to $79.6 billion.[46] Not all the money was really additional and only a fraction of it was channeled to the 'NAMAs (Nationally Appropriate Mitigation Action)' and 'NAPAs (National Adaptation Programme of Action)' which developing countries prepare to attract climate finance. Nor does the composition of the finance express the wishes of the recipient countries which prefer most of it to be channeled to adaptation investments and to be in the form of grants. The adaptation finance ($20.1 billion) made up 25%, the share of grant finance ($16.7 billion) 21% of the $79.6 billion.

The inclusion of 'climate loss and damages' - compensating costs that countries can't avoid or adapt to - into the funding debate further increases the 'finance expectation/finance supply' gap. The V20 Group comprises 58 nations with a total population of 1.5 billion, who account for a 5% share of global emissions.[47] A V20 report published in June 2022 estimated their combined climate-linked losses over the last two decades at $525 billion, equal to about 20% of their collective GDP in 2020.[48] With reference to the legal-economic 'polluter pays' principle, a number of developing countries backed by NGOs insist that rich countries pay the poorest countries compensation for the losses and damages which climate change inflicts on them. The validity in principle of the claim was accepted in the 2015 Paris Agreement by the rich countries as they promised to "address the losses and damage caused by the harmful effects of climate change". To get around the limited political 'willingness to pay' of rich countries, some activists take the matter to national courts.[49] Vanuatu has asked the International Court of Justice to issue an opinion on the rights of present and future generations to be protected from adverse climate change impacts. Yet, despite its justification in principle, the enforcement of the compensation claim is problematic operationally[50] and legally[51].

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[46] The OECD statistics cover four components of climate finance: bilateral public climate finance, multilateral climate finance (attributed to developed countries), climate-related officially supported export credits, and private finance mobilised by developed countries public finance interventions.

[47] Members - V20: The Vulnerable Twenty Group (v-20.org)

[48] Climate Vulnerable Economies Loss Report_Project alternative (b-cdn.net)

[49] Climate activists in the Netherlands have filed a lawsuit against Shell demanding that Shell pays compensation for the climate damage that is caused by Shell's historic oil and gas production.

[50] One example: The determination that a storm which inflicted damage in a region was caused by changes in the weather due to climate change? Storms have existed as long as the earth has had an atmosphere. More general: Estimates of loss and damages rely on econometric modelling of a counterfactual situation; though based on best available scientific data, their specific results are subject to uncertainties.

The issue must be dealt with pragmatically by accepting the moral justification to assist particularly vulnerable countries with specific funds and in general by expanding funding for disaster relief; to enshrine damage compensation as a legal international treaty obligation will lead to a poisonous, counter-productive relationship.

What can be said about the relevance of Bauer's critique 50 years later

In light of the dynamic evolvement and changes in development aid over time, what can be said about the relevancy and appropriateness of Bauer's "foreign aid forever" critique 50 years later?

Bauer's views have obvious weaknesses. If a newborn nation lacks basic institutional and physical infrastructure, then it is obvious that a well-executed foreign aid can facilitate the development of 'mainsprings of progress'. Bauer was blind to the importance of geographical location. Sub-Saharan Africa's development is handicapped by unfavorable geography[52] and at the beginning of independence in 1960 of a small population of 229 million spread over a vast area. By contrast, Singapore's development into one of the world's richest and most technologically advanced countries was favored by its position as a trading and maritime hub for emerging economies in East and Southeast Asia. His rejection of the two-gap theory with the statement that pre-industrial Western Europe was poor, yet managed to finance the industrial revolution, overlooks that the finance came from profits made in long-distance trade (Asia-Europe and West-Indies-Europe) and from the concentration of agricultural surpluses in the semi-feudal estates. The concentrated financial surplus in mineral and fossil fuel rich developing countries is mainly shared between the state and foreign owners; relatively little is owned by local entrepreneurs.

Other views and predictions of Bauer are more relevant.

Unlike Marshall Aid, foreign aid has not become a short-term parenthesis in the history of the world. In 2020, the level of ODA set a new record in absolute terms to the tune of US$161 billion[53] ; net transfer (after deduction for repayments on previous loans) was US$117 billion.[54] Only four countries achieve the 0.7% target: Luxembourg, Norway, Sweden, Denmark; the first three contribute 1% of GDP, Denmark 0.7% of GDP.

The 'mainsprings of progress' hypothesis finds some confirmation in that the greatest economic progress happened in countries where development aid made a modest contribution to the state budget: China and South-East Asia.[55] The countries in Sub-Saharan Africa received the largest contribution as a percentage of the state budget (25-60%) and as a percentage of GDP (10%)[56].

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[51] Kuwait has become rich in producing and exporting oil, which in consumption has led to CO2 emissions. Climate change will boost the already high temperatures in Kuwait to over 50 degrees Celsius for several months of the year within a decade or two. Does Kuwait's oil production oblige the country to pay compensation? Or does the temperature rise make the country eligible for compensation?

[52] Convincingly described by Jared Diamond in "Guns, Germs and Steel," 1998

[53] COVID-19 spending helped to lift foreign aid to an all-time high in 2020 but more effort needed - OECD

[54] World Bank: "International Debt Statistics 2022 report".

[55] One exception is South Korea, which from 1948 to 1975 received massive and sustained assistance from the United States and in the later part of the period from Japan.

[56] During the 1970 to 2012 period, the share fluctuated between a low 7% of GDP in 1971 and a high 20% i 1994. Source: Lauren Tait, Abu Siddique and Ishita Chatterje: «Foreign Aid and Economic Growth in Sub-Saharan Africa" University of Western Australia., March 2016.

Progress in Africa was solid in a number of areas. From 1970 to 2013, access to higher education increased by 4.3% per year (global average 2.8%)[57]; average life expectancy increased from 47 to 64 years[58], the proportion of Africans living in extreme poverty fell from 54% in 1990 to 41% in 2015.[59] All countries, with the exception of the socalled 'fragile states', now have highly competent officials, engineers, finance experts.

Yet, despite significant progress in institution and capacity building, the gap between the GDP per capita of EU countries and Africa widened. Measured in 2019 fixed prices, Denmark had in 1960 a GDP per capita of $3,464, which was 14 times greater than Ghana's of $254 and 19 times greater than Tanzania's of $180. By 2020, Danish GDP per capita of $60,909 was 26 times larger than Ghana's $2,329 and 57 times greater than Tanzania's $1,076.[60] Although the average economic growth rate of African countries over the period was higher than the Danish rate of 2.3% - Ghana's was 3.7% and Kenya's at 4.7%[61], the high African population growth in sub-Saharan Africa (to over 1 billion people in 2018) increased the difference in income per capita.[62] Population growth is driven by poverty, by a low level of education of women, by African politicians who believe that a large population promotes a country's international weight, and by comparatively low levels of urbanisation. The average median age of 19.7 years in African countries (EU = 42.5 years) leads to the high dependency ratio[63] of 1.23 (EU = 0.65). Before growth can accelerate, the dependency ratio must go down.[64] Looked at the development from a positive angle, it should be noted that Ghana's per capita income over the period has increased from 7% to 67% of the Danish level in 1960.

The uneven development during the last 50 years kept alive academic and political debates about the contribution of foreign aid to economic growth. At micro-level, economists agree that most development projects yield a positive return. The controversy is at macro-level: whether it is feasible to document positive impacts of development aid on the economic growth of the recipient countries? Nobel laureate Angus Deaton denies that foreign aid promotes economic growth[65], while Paul Collier insists it has lifted the growth rate to the poorest billion people over the past 30 years.[66] At times there was not even a 'Washington consensus' about the issue. A World Bank research report in 1998 concluded that aid has a positive impact on economic growth provided that the country pursued the right policy.[67] In two research papers from 2005, the IMF could not

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[57] Figures of the Week: Higher education enrollment grows in sub-Saharan Africa along with disparities in enrollment by income (brookings.edu)
[58] Africa: life expectancy 1950-2020 | Statista
[59] World Bank:"Accelerating Poverty Reduction in Africa", October 2019
[60] https://www.macrotrends.net/countries
[61] https://www.theglobaleconomy.com
[62] World bank Population Estimates and Projections database
[63] The ratio of "population younger than 20 or older than 64 years"" to "population from 21 to 64 years". Source: "Africa's high birth rate is keeping the continent poor" Economist 22.09.2018
[64] East Asia's economic take-off from the 1970s came after a sharp drop in fertility rates. Source: David Philing "Africa's population boom doesn't spell a demographic dividend". FT 26.12.2021
[65] Angus Deaton, his Nobel Prize, and foreign aid (brookings.edu)
[66] Michael Clemens, Steven Radelet and Rikhil Bhavnani: "The short term effect of aid on growth". Center for Global Development. Working Paper Number 44 July 2004
67 "Assessing aid: what works and what doesn't", World Bank Policy Research Report November 1998. . Stefan Dercon's "Gambling on Development: Why Some Countries Win and Others Lose" published 2022 argues that economic growth lies not in a specific set of policies, but rather in a key 'development bargain', whereby a country's elites shift from just protecting their own positions to striving for growth and development.

demonstrate a positive influence[68]; whereas in 2009 an IMF paper did.[69] International studies looking at individual sectors, that received aid finance, conclude that aid for social infrastructure, especially education and health, and general budget support, have a significant positive effect on economic growth.

Danish academia also lack consensus. Aarhus economists Martin Paldam and Christian Bjørnskov note in their studies that the effect is positive and small.[70] According to Henrik Hansen and Finn Tarp from the University of Copenhagen, the detection of a small effect in studies is due to the choice of a short time horizon (typically four years). A time horizon of 10 years or longer shows stronger impacts; according to Tarp an aid of 10% of GDP raises the country's annual growth rate per capita by more than 1 percentage point in the long term. [71]. Tarp applies the 'Rubin Causal Model' method to estimate the effect of development aid, which compares reality with a model estimate of what development would have looked like without aid. The rate-of-return results, therefore, depend on the assumptions made in the model.

However, the claim that aid had an insignificant impact on the investment and growth rates of the recipient countries, is difficult to accept, since large financial inflows have Keynesian expansionary impacts and capacity building assistance raises productivity. Zero impact presupposes that major distortions in the allocation of funds counter-balance the expansionary impact of funding. For example,: that projects are decided by donors and not by the real needs of the beneficiary countries; that donor funding eliminates the need for those in power to collect taxes; that the influx of large amounts of donor money into the economy has negative 'Dutch disease' effects in the form of an overvalued national currency which stifle exports; etc..

Yet, because of the continued existence of deep poverty and backwardness, criticism reminiscent of Bauer's views can be heard on the recipient side. Zambian economist Dambisa Moyo stated in her 2009 book "Dead aid" that aid does not work. Her main argument is that to justify its position, a national government must be able to deliver public goods, such as- education and health, on its own; it is its job as ruler. Foreign co-financing of public goods leads to a lack of transparency/accountability for the result which promotes corruption. Moyo recommends that all economic development aid for public goods be scaled back over a five-year period. At a press conference with French President Emmanuel Macro in 2017, Ghana's President Nana Akufo-Addo called on African countries to 'free themselves from foreign aid because it has never worked and never will'.[72]

Adapting DAC assistance to today's key challenges

[68] Nadia Masud and Boriana Yontcheva: "Does Foreign Aid Reduce Poverty? Empirical Evidence from Nongovernmental and Bilateral Aid." IMF working paper 2005/100. Raghuram G. Rajan and Arvind Subramanian: "Aid and Growth: What Does the Cross-Country Evidence Really Show? IMF working paper 2005/127

[69] Camelia Minoiu and Sanjay G. Reddy: "Development Aid and Economic Growth: A Positive Long-Run Relation". IMF WP/2009/118

[70] Christian Bjørnskov: "Types of Foreign Aid", Economics Working Papers 2013-08. Hristos Doucouliagos and Martin Paldam: "Finally a breakthrough? The recent rise in the size of the estimates of aid effectiveness", Economics Working Papers 2014-07

[71] Channing Arndt, Sam Jones, and Finn Tarp: Aid, Growth, and Development. Have We Come Full Circle? UN-WIDER Working Paper No. 2010/96

[72] Ghana's president surprised Macron with aid rejection | FairPlane

A reform of international development aid must address two macro issues.

One is the need to clarify the practical implications of the concept of 'common responsibility for achieving the 2030 development objectives' and the associated interpretation of 'primary responsibility'. In an interconnected world, the concept of common responsibility is ethical and rational: all civil and public actors must, within their field of responsibility, do what they can to pursue goals which make the world a better and more equitable place to live in. For example, that private firms take ESG (environmental, social, governance) serious, implement progressive gender policies and comply with or surpass environmental regulations. The crucial issue for development assistance is where to draw the line for where international co-financing responsibility ends and national exclusive responsibility starts? Damisa Moyo makes the pertinent argument that providing basic public goods and combating extreme poverty is the core function of a national Government and that joint national-foreign financing removes transparency about the national government's responsibility for providing these goods and postpones the introduction of revenue raising reforms to finance them.[73] International co-financing of national public goods and of pro-poor social payment support continues the paternalistic donor-client relationship in development cooperation.

The second is the high indebtedness of low income and lower-middle income countries, which calls for reconsidering the ratio of grant and debt finance in international development finance. Whereas Chinese development finance has made some downward adjustments in its lending volume, the composition of the EU's 'Global Gateway initiative' is debt heavy, albeit much of it in terms of DFI.

International development cooperation can become a more effective response to the global challenges of our time if it concentrates on addressing three topics:

1. Production of 'global goods' (climate mitigation and adaptation, biodiversity, regional environmental pollution, digitalization, cross-border transport and communication, combating pandemics; UN peacekeeping efforts).
2. Humanitarian aid (food crises, refugee aid, disaster relief).
3. Creating a more level playing field for entrepreneurs in developing countries above all in their domestic but also in the international markets.

The focus on the above three topics establishes a partnership of equals between donors and recipients of aid money around the achievement of common global objectives.

Because the achievement of the global common goods objectives depends on the existence of strong local actors, cooperation on the strengthening of national administrative and regulatory infrastructure will continue, but with focus on creating the necessary conditions for the realization of global common goods. Thus, there will be continued involvement in health (e.g. pandemic preparedness), education (e.g. capacity building of clean energy technicians), agriculture (e.g climate resistant crops) and in the national finance sector (e.g. promoting higher national co-funding of clean investments.)

Poverty alleviation has been a central focal point of DAC-countries' development aid since the 1990s. Redefining poverty alleviation as a 100% national government task will not reduce the extent

[73] The median tax revenues in percent of GDP of the 54 Low Income Developing Countries were 13% of GDP in 2013 and also in 2019 despite technical assistance for their increase. Source: IMF Annual reports

of pro-poor activities. The preservation of internal stability forces Governments to continue them, while UN monitoring of progress towards the achievement of the 2030 development goals – all of which have direct or indirect poverty alleviation impacts - generates external pressure. The inflow of global goods finance expands the national taxation base, which creates public revenue for the continuation of national pro-poor programs.

In global goods cooperation, Governance best practice is spread through the organization structures that will be set up for the co-financing of projects in countries and at regional level. Democratic and transparent processes are created on the ground through clear guidelines prescribing the involvement of citizens and civil society organizations in the identification, design, and implementation of projects. It includes maximum account of gender and the protection of the legitimate interests of minorities. An excellent governance model for devolved finance in adaptation is Kenya's County Climate Change Fund (CCCF) for the financing of adaptation measures that are locally founded while in line with national climate change policies and development plans.[74]

As climate finance becomes a key element of cooperation, there is no need for separate 'additional climate finance' calculations. An increase in 'total aid finance', however, is essential for the implementation of high value 'global goods' investments. The required level of public finance support for the capital-intensive investments in in climate, environment, transport, communications and digitalization exceeds the savings from reduced external financing of 'national public goods'. The IMF estimates that annual needs for adaptation finance exceed 1 percent of GDP in about 50 low-income and developing economies for the next 10 years.[75] The self-interest of rich countries in the 'global goods' should be a strong political argument for raising DAC countries' average annual development funding gradually from the current 0.32% of GNI towards the 0.7% goal.

In order to shoulder the burden of climate loss and damages, the composition of international climate finance must be reversed in accordance with the wishes of low-income countries.[76] Investments in climate adaptation reduce the extent of future climate losses and damages, but do not generate money from new revenue or operational cost reductions which can be used to repay loans. They, therefore, need grant finance support from donors. The supplementary function of helping low-income countries to repair damages caused by severe weather conditions, is performed by money from disaster relief funds.

The large investments in global goods create an important market in low-income countries for new and advanced technology. The active participation of national contractors and investors in this market increases national value creation. Local content requirements in public procurement must be supplemented by green business and technology policy initiatives. The creation of links between international funding of projects and local business development activities must be an important performance parameter for North-South cooperation on global goods. Kenneth Rogoff's proposal "to create a new, focused agency, a World Carbon Bank, that provides a vehicle for advanced economies

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[74] See Esbern Friis-Hansen, Lily Salloum Lindegaard, Marie Gravesen and Mikkel Funder: "Devolved Finance and Governance of Climate Change Adaptation", DIIS REPORT 2022: 02

[75] Kristalina Georgieva, Vitor Gaspar & Ceyla Pazarbasioglu:"Poor and vulnerable countries need support to adapt to climate change", IMF blog 23.03.2022

[76] "Group of Like Minded Developing Countries and the African Group of Negotiators". Decision XX/CMA.4: COP-26

to coordinate aid and technical transfer, and that is not simultaneously trying to solve every other development problem"[77] deserves attention- although the downside is institutional fragmentation.

High interest rates in low-income countries are an obstacle in the transition towards a low-carbon economy: they reduce the financial attractiveness of green investments as well as the ability of local entrepreneurs and investors to gain market shares. The transition to lower carbon intensive economies, therefore, requires the introduction of radically new finance tools to create greater equality between financing conditions in DAC and low-income countries.

One structural adjustment task is to increase the involvement of local entrepreneurs in the financed activities. This includes local co-finance of investments as it increases national value creation, and thus, GNI more than GDP. It is time to get away from the focus of 'private finance leverage subsidies', counted as ODA, on the mobilization of private capital from DAC-countries and put more emphasis on leveraging local finance for investments in infrastructure. At the practical level there is a need for continued assistance to improve access to information on state-of-the-art technology and the identification of suitable partners in international supply chains.

Another structural challenge is to create a more level playing field in international finance: to enable low-income countries (most of which have no investment grade credit ratings or are barred from new borrowing by high debt levels) to sell sovereign green bonds on the international capital market at terms roughly equivalent to those enjoyed by government bonds from DAC countries. Jeffrey Sachs illustrates the great advantage that the United States and EU countries have in that their central banks can always buy up their own internationally used currency: interest rates on government bonds from highly indebted Italy are significantly lower than for government bonds issued by low-indebted Ghana.[78] This would require the introduction of international guarantees specifically for such bonds and the creation of a new financial back-up facility at the IMF.

77 Kenneth Rogoff: "It's high time to create a World Carbon Bank", The Guardian 8.7.2019

78 Jeffrey D. Sachs: "Time to Overhaul the Global Financial System". Project Syndicate Dec 3, 2021 Sach's argument, though, overlooks another very important explanatory factor: tax revenue in percent of GDP in Ghana is in the 12-15% range, Italy's is around 42%.